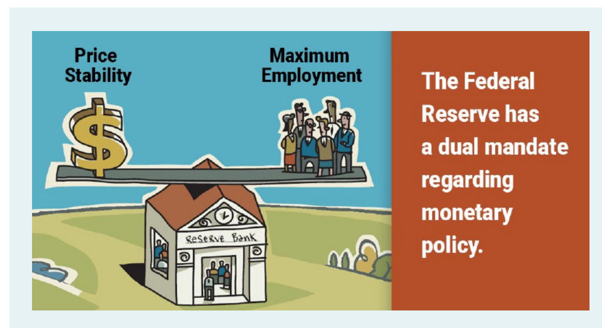
Brinker Capital

WEEKLY WIRE | August 5, 2019

What did the Fed just do? Why? What comes next?



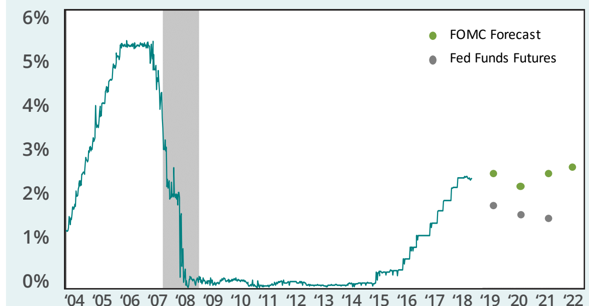
Last week, the Federal Open Market Committee, the monetary policymaking body of the US Federal Reserve (Fed), met and announced it was lowering the Federal Funds rate by 25 bps (the first interest rate cut in more than 10 years) to a range of 2.0% to 2.25% and ending the runoff of its $3.8 trillion asset portfolio. Before we examine why the Fed took these two very important steps to support the US economy, a bit of background. Our central bank, the Fed, was created in 1913 and has two primary jobs: price stability and maximum employment. While the Fed has a lot of tools at its disposal to accomplish both goals, the most powerful is the Fed Funds Rate, or the rate at which banks lend money to each other. Set the rate too high, and credit can become too expensive, pushing the economy into recession; set the rate too low, and the cost of credit could become too cheap, stoking inflation and asset bubbles. Getting it just right isn't easy.

Many investors thought it was a mistake for the Fed to cut rates, as the US economy is growing 2%+ and our unemployment rate is near a 50-year low. Those who wanted the Fed to cut – and keep cutting – cite muted inflation, weakening manufacturing, and other central banks lowering rates as justifying a more accommodative posture by the Fed.

We believe the Fed made the right call in cutting rates and ending its balance sheet reduction program, particularly as inflation is contained and growth outside the US is slowing, likely as a result of uncertainty driven by the ongoing US/China trade dust-up. We also think the Fed will cut one to two more times this year and would point out that on more than one occasion the Fed has eased while our economy was still clearly on firm footing, and doing so at the time both lengthened the economic expansion and was supportive of risk assets. The big caveat to our Fed call is US/China trade – solve for it, and the Fed can likely take a step back; inflame tensions further, and the Fed will likely have to be more aggressive on the interest rate front.

It could be a bumpy ride into year-end, but we remain optimistic about the economy and markets.

Effective Fed Funds Rate (%)



Stocks, bonds, and commodities (8/2/19)

Security name	Last	QTD chg	YTD chg	12mo chg
S&P 500	2932.05	-0.33%	16.96%	3.23%
MSCI AC World ex USA	275.16	-3.49%	7.73%	-5.95%
MSCI EAFE	1863.85	-3.04%	8.37%	-5.95%
MSCI EM	1003.76	-4.84%	3.93%	-6.48%
Bloomberg Barclays US Agg	105.48	0.74%	5.39%	5.74%
Crude Oil WTI	55.19	-5.61%	21.54%	-19.42%
Natural Gas	2.14	-7.24%	-24.90%	-24.96%

Treasury rates (8/2/19)

	Price	Yield
2Y	100.022 / 100.0	1.710
3Y	100.072 / 100.0	1.668
5Y	100.140 / 100.1	1.657
7Y	100.284 / 100.2	1.738
10Y	104.226 / 104.2	1.845
30Y	110.142 / 110.1	2.383

Weekly reports

This week
- PMI Composite
- Producer Price Index

Last week
- Chicago PMI 44.4
- Private Nonfarm Payrolls 164K

Image source: https://pbs.twimg.com/media/DkKL6aHU0AESaNq.jpg:large. Chart source: FactSet, as of July 31, 2019. The views expressed are those of Brinker Capital and are not intended as investment advice or recommendation. For informational purposes only.

Brinker Capital Market Barometer

AUGUST 2019

The weight of the evidence still leans positive; however, a number of factors have added to global uncertainty in the near term, increasing the potential for additional volatility. Given this outlook, portfolios will maintain a relatively neutral overall risk positioning.

SHORT-TERM FACTORS (< 6 months)

Factor	CHANGE	NEGATIVE	NEUTRAL	POSITIVE	Comment
Momentum	←		●		Market momentum has weakened with recent sell-off
Trend	←	●			Still support at 200-day moving average for S&P 500 Index
Investor sentiment	→			●	Investor sentiment moved to pessimism with recent sell-off
Seasonality		●			Seasonality remains a headwind until mid-October

INTERMEDIATE-TERM FACTORS (6-36 months)

Factor	CHANGE	NEGATIVE	NEUTRAL	POSITIVE	Comment
Fiscal policy				●	Fiscal stimulus expected to increase leading up to 2020 election
Monetary policy				●	Fed beginning insurance cuts; global central banks more accommodative
Inflation				●	Global inflation low and slowing; inflation expectations muted
Interest rate environment			●		Longer-term rates range-bound; yield curve inversion at short end
Macroeconomic			●		Global growth slowdown but still positive; US/China trade war concerns
Business sentiment			●		Small biz confidence off record high; CEO confidence little improved
Consumer sentiment				●	Remains at elevated levels; still supportive
Corporate earnings				●	US earnings growth rates declining but still positive; still soft ex-US
Credit environment				●	Credit spreads have remained in check

LONG-TERM FACTORS (36+ months)

Factor	CHANGE	NEGATIVE	NEUTRAL	POSITIVE	Comment
Valuation			●		US equity valuations at long-term averages; more attractive ex-US
Business cycle				●	Long recovery but has been muted; few signs point to recession
Demographics			●		Mixed (US and emerging markets positive; developed intl negative)

Source: Brinker Capital. Information is accurate as of August 6, 2019. Themes and specific funds utilized to implement themes are discussed within the context of Brinker Capital's managed asset allocations and are based on current market conditions and constitute Brinker Capital's judgment and opinions, which are subject to change without notice. Past performance does not guarantee future results. Statements referring to future actions or events, such as the future financial performance of certain asset classes or market segments, are based on the current expectations and projections about future events provided by various sources, including Brinker Capital's Investment Management Group. These statements are not guarantees of future performance and actual events may differ materially from those discussed. Brinker Capital Inc., a registered investment advisor. MSCI AC World ex US Growth: An index made up of approximately the top 50% of the MSCI AC World ex US Index as composite ranked by five growth rates. This is a common proxy used to represent the growth segment of the developed international market. MSCI EAFE Index: A market-capitalized weighted index representing developed international equity markets located in Europe, Australia, Asia and Far East (EAFE). S&P 500 Index: An index consisting of 500 stocks chosen for market size, liquidity and industry grouping, among other factors. The S&P 500 is designed to be a leading indicator of U.S. equities and is meant to reflect the risk/return characteristics of the large-cap universe. Companies included in the Index are selected by the S&P Index Committee, a team of analysts and economists at Standard & Poor's. Barclays US Aggregate Index: A market capitalization-weighed index, maintained by Barclays Capital, and is often used to represent investment grade bonds being traded in the US. MSCI Emerging Markets: a float-adjusted market capitalization index representing 13% of global market capitalization. Captures mid and large cap across more than two dozen emerging market countries.