ReDefine Wealth Management's Monthly Market Commentary

03-31-2019

ReDefine Wealth Management

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Market Performance Roundup

As of 03-31-2019

ReDefine Wealth Management

WORLD MARKETS

		1 MO.	Q1 19	YTD	2018	1 YR.	3 YR.
Global Equities (USD, % chg.)	MSCI All Country World (Total Return)	1.32%	12.33%	12.33%	(8.93%)	3.16%	11.27%
	MSCI World (Total Return)	1.38%	12.65%	12.65%	(8.20%)	4.61%	11.31%
	MSCI EAFE (USD) (Total Return)	0.74%	10.13%	10.13%	(13.36%)	(3.22%)	7.80%
	MSCI Emerging Markets (Total Return)	0.86%	9.95%	9.95%	(14.24%)	(7.06%)	11.09%
Country Equities (Local, % chg.)	Dow Jones Industrial Average (Total Return)	0.17%	11.81%	11.81%	(3.48%)	10.09%	16.37%
	S&P 500 (Total Return)	1.94%	13.65%	13.65%	(4.38%)	9.50%	13.51%
	NASDAQ (Total Return)	2.70%	16.81%	16.81%	(2.84%)	10.63%	17.97%
	Russell 2000 (Total Return)	(2.09%)	14.58%	14.58%	(11.01%)	2.05%	12.92%
	Nikkei 225 Stock Average (JPY) (Total Return)	(0.03%)	6.89%	6.89%	(10.29%)	0.92%	10.30%
	STOXX Europe 600 Euro (Total Return)	2.17%	13.18%	13.18%	(10.22%)	5.88%	7.56%
	FTSE 100 (Total Return)	3.29%	9.49%	9.49%	(8.73%)	7.69%	10.00%
	DAX 30 (Total Return)	0.09%	9.16%	9.16%	(18.26%)	(4.72%)	4.97%
	Shanghai Composite	5.09%	23.93%	23.93%	(24.59%)	(2.47%)	0.95%
Global Fixed Income (USD, % chg.)	Barclays Global Treasury (Total Return)	1.21%	1.60%	1.60%	(0.38%)	(1.62%)	0.96%
	Barclays US Treasury (Total Return)	1.91%	2.11%	2.11%	0.86%	4.22%	1.04%
	Barclays Global Aggregate (Total Return)	1.25%	2.20%	2.20%	(1.20%)	(0.38%)	1.49%
	Barclays US Aggregate (Total Return)	1.92%	2.94%	2.94%	0.01%	4.48%	2.03%
	Barclays Global High Yield (Total Return)	0.46%	6.33%	6.33%	(4.06%)	2.38%	7.33%
	Barclays US Corporate High Yield (Total Return)	0.94%	7.26%	7.26%	(2.08%)	5.93%	8.56%
	S&P Leveraged Loan Index (Total Return)	(0.21%)	3.96%	3.96%	0.47%	2.96%	5.65%
	Barclays Emerging Markets (Total Return)	1.37%	5.43%	5.43%	(2.46%)	4.38%	5.36%
Real Assets (USD, % chg.)	USD DXY	1.17%	1.16%	1.16%	4.40%	7.91%	0.94%
	Dow Jones US Real Estate Index (Total Return)	4.19%	17.08%	17.08%	(4.03%)	19.41%	8.08%
	Bloomberg Commodity Index	(0.18%)	6.32%	6.32%	(11.25%)	(5.25%)	2.22%
	S&P GSCI Gold	(1.34%)	1.34%	1.34%	(2.14%)	(2.17%)	1.67%
	S&P GSCI Precious Metals (Total Return)	(1.79%)	0.55%	0.55%	(3.58%)	(3.34%)	0.49%

April 8, 2019 ***ReDefine Wealth Management** provides clients and business partners with a differentiated suite of services and products. This monthly commentary encapsulates how our team is looking at the world and the practical implications of our approach. It is designed to illuminate the process behind the implementation of investment decisions within **ReDefine Wealth Management Global Thematic Active Asset Allocation Portfolios.***

Anecdotal and historical evidence suggest that mitigating portfolio draw-down has the greatest impact on portfolio success. *Quite simply, it is more efficient to grow wealth by not losing wealth.*

In order to facilitate portfolio success, ReDefine Wealth Management employs a Global Thematic Active Asset Allocation approach to our investment portfolios.

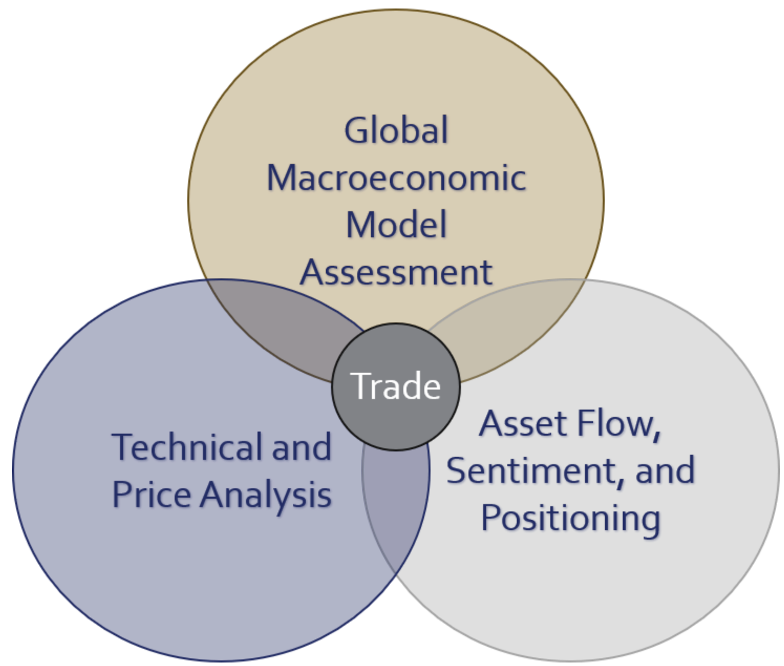
Our Global Macroeconomic Analysis provides the basis for attractive reward versus risk within global investment opportunities and helps to inform our Active Asset Allocation. We divide assets between the best opportunities that we can source within three primary portfolio components – *Global Equities, Fixed Income/Cash, and Real Assets*.

Like a traffic signal, Active Asset Allocation allows RWM to invest or overweight opportunities where we feel strongly (green light), avoid or underweight asset classes where we feel unconvinced or cautious (yellow light), and even take inverse positions when we feel strongly negative (red light).

Once the allocation is decided, we begin our investment selection to specifically choose the financial instruments we will use to implement our globally thematic strategic asset allocation. Our disciplined processes allow us to handpick and tactically manage highly-liquid financial instruments, such as: *ETFs, Mutual Funds, Stocks, Bonds, CEFs, and Options.*

So, while we may hold similar "investments" as traditional portfolios, it is our approach and flexibility that allows for asymmetric returns relative to risk.

Global Thematic Active Asset Allocation



Fundamental Global Macroeconomic Backdrop

Déjà Vu All Over Again?

With the start of baseball season, we thought it was appropriate to borrow a classic Yogi Berra quote for our theme this month. It seems fitting given the markets through the first quarter of 2019. Much like the rallies of January and October of 2018, this year's bounce off the December 2018 lows has a number of curious similarities. Equity prices seem to be getting a little ahead of themselves, especially given the negativity of the global macroeconomic outlook and data. Of course, this isn't overly unusual. Since the end of the Great Financial Crisis, the Global Central Banks have used liquidity infusions to maneuver the global markets. So again, this is an all too familiar occurrence over the last decade.

Before we discuss the current environment's similarities to 2018, when the equity markets experienced very quick drawdowns of 12% and then 20%, we would draw attention to a few similarities to the 2013 – 2016 time period. During that time a few asset classes, that historically were very correlated, exhibited some disconnection.

Could it be déjà vu all over again?

Exhibit 1 shows the performance of the S&P 500 Index and that of the 10-year US Treasury Yield from October 2018 to the end of March 2019. Typically, these indices tend to move together or at least trend in the same direction over time. Since the end of 2018, the divide between them expanded rapidly and they are trending in opposite directions.

Exhibit 1. Source: Bloomberg as of March 28,2019

Historically, this has been a signal that perhaps the markets are not trading in a normal fashion. Over time we expect these lines to come together again in what we call a reversion to the mean. This reversion will most likely take the form of the S&P 500, which in our opinion has gotten ahead of its support, eventually retreating toward the levels of the 10-year yield. One major reason behind our belief is that the 10-year yield, as a proxy for the US bond market which typically reflects macroeconomic reality, while the S&P 500, as a proxy for the US equity market, can at times reflect Wall Street's hopes.

That stated, our opinions of what the future may hold for the US equity markets are not built upon one chart, presented in a vacuum. *We believe current market conditions and trends, examined through multiple lens, combine to reveal where the potential risks are for equity prices.* As we examine the change in earnings per share for the S&P 500 in the first quarter of 2019 in contrast to the change in price for the same index over the same period, we are seeing yet another divergence. Exhibit 2.

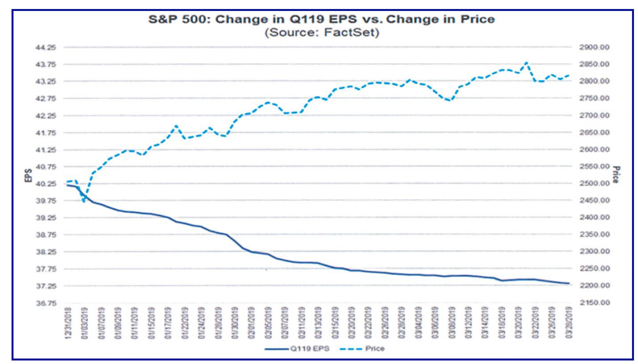


Exhibit 2. Source FactSet as of March 28, 2019

Too many years ago then we care to acknowledge, we were taught that stock prices tend to follow earnings.

Fundamental Global Macroeconomic Backdrop (cont.)

If a company's earnings rose, it was not unusual to see the company's stock price follow suit… and vice versa. We are seeing those two variables - earnings per share and stock prices - that historically (and logically should) track each other… diverge. In the more recent past we have noticed numerous times that prices have diverged from earnings and take on a life of their own… At least for a period of time before correcting or reverting back toward the level of their earnings.

By combining excess liquidity and zero interest rate policies since the Global Financial Crisis, Central Banks have asserted the largest influence on these types of divisions. As a stand-alone, we wouldn't give too much credence to this chart, but *it is interesting to see the markets rally in the face of deteriorating earnings and earning's forecasts*. Also, given the volatility of the past fifteen months, corporations really need to announce improving business conditions in their 1Q earnings reports and forecasts, or they risk the similarities of last year taking hold.

In order to move from the macro to the micro, let us examine a powerful part of the global equity markets, Semiconductors. The semiconductor sector of the global economy has become increasingly important over the last 10 years. After becoming a big part of the 1990's Tech Boom, the sector has been relatively commoditized. Semiconductors can be found in almost every consumer and business product, from planes, trains, and automobiles, to appliances, phones, and computers. In fact, the sector – made up of the semiconductor stocks - has become a key indicator used to gauge the relative health of the global economy. Partly because their prices, access, and sales crossover almost all major industries; and party because semiconductor sales have been a primary driver of the recent technology rally.

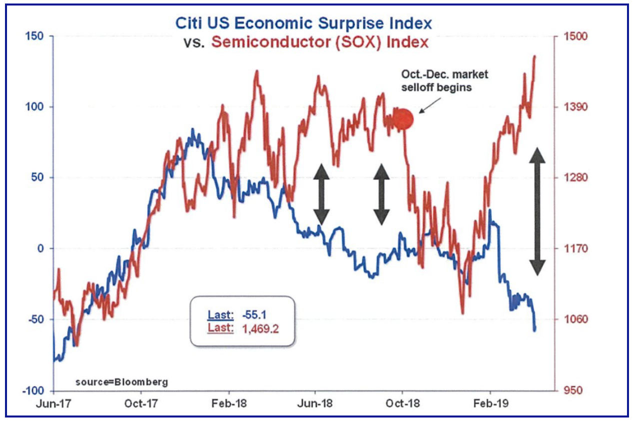


Exhibit 3. Source Bloomberg as of March 28, 2019

We find it useful to observe how the Citi US Economic Surprise Index (CESI), which can be an excellent proxy for global economic health as it basically collects major economic data and illustrates it in an index format. The CESI is a decent macroeconomic indicator and a great way to see how economies are doing in general given current inputs. The Semiconductor Index (SOX) is a semiconductor price index that is constructed with the stock prices of all the semiconductor stocks. When we chart the CESI versus the SOX – Exhibit 3 – we find another interesting pattern.

Again, we are seeing a wide separation between two indexes that historically more or less track each other. One of two conclusions can be drawn from this information: 1) Semiconductor stock prices are very high, historically speaking; or 2) Major improvement in US economic numbers are on the horizon. Viewed in a historical context, at the beginning of 2018 these two indexes were demonstrating similar divergence, only to have the SOX revert toward the CESI. Again, the divergence of the indexes between last May-September was followed by a SOX reversion to the CESI in the fourth quarter of 2018. Currently, the divergence between the two are stressed to the point where we tend to believe something is going to give - one way or another.

Is the CESI vs SOX an outlier? Or are there other indications that the markets could see a severe reversion that becomes a major correction in the SOX? And what are the ramifications of SOX correction on the technology sector in general?

Once again, we have a divergence between an equity price index, in this instance the SOX and major macroeconomic input, Korean Semiconductor Exports. The current divergence is the largest we have observed since 2004. Simultaneously, semiconductor manufacturers around the globe have generally begun reporting lower earnings than analyst expectations – like Intel did on March 21, 2019 – and recently Samsung and other semiconductor manufacturers have been actively cutting future earnings forecasts.

Our research partners at MI2 Partners, provided an illustrative view of the SOX (blue line) when positioned versus data that

Fundamental Global Macroeconomic Backdrop (cont.)

tracks a major manufacturer and exporter of semiconductors, the Korean Semiconductor Exports (red line) – Exhibit 4.

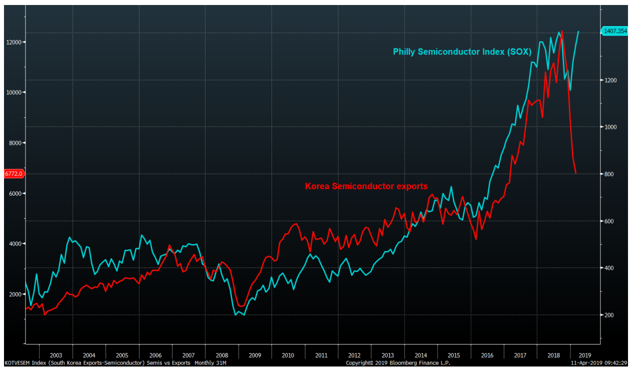


Exhibit 4. Source MI2 Partners, Bloomberg as of March 28, 2019

Is the Korean Semiconductor Export data important?

Let's compare this valuable economic input to one America's darling companies, Apple. Apple has historically been a massive consumer of semiconductor chips over the last 20 years. After all, each of their products uses more and more semiconductors every year – Exhibit 5.

In our humble opinion, we have observed a significant divergence between price and macroeconomic inputs. With the discrepancies observed with examination of the hard data, the question should be: *Why are equity markets moving the way they are?*

As discussed in previous commentary, the shift in Central Bank policy since December 19th along with continuous jawboning coming from the White House has given hope to the markets that the economic data is going to reverse and become stronger in the near future. If economic strength is on the horizon, we have difficulty processing the actions of President Donald Trump and his economic officials who are pushing the Fed for another 50-basis point rate cut. If the economy is strong and the markets have recovered, why push for a rate cut. Our issue is that we fear another sell-off similar to what we saw in the 4Q of last year…

Déjà Vu All Over Again?

Exhibit 5. Source Bloomberg as of March 28, 2019

In previous commentaries we have hypothesized that a quick, violent correction in the equity markets would force the Fed to cut rates and begin the inevitable descent of the US dollar into secular weakness - thus setting the table for the reflationary trade that we believe is coming. The Fed has shown it will not let the market take our economy into a recession. The White House and the Fed would prefer the strong rebound in the economy scenario, but we are not seeing it at this time. Corporate earnings reports over the next few weeks, as well as upcoming economic data releases, could provide a greater clue to what's to come. Therefore, we remain patient.

We have continued to closely monitor the Brexit situation overseas, as we do believe there are potentially catastrophic economic risks if it does not go smoothly. Currently, both sides have until April 12, 2019 to come up with a resolution or suffer a "hard" Brexit. Our sources assure us that the UK and the European Union will extend the process to closer to the end of the year. If they do not come up with an agreement to extend, then we could see some economic fireworks on a global scale. However, we believe that the odds are in favor of the "kick the can down the road" strategy.

Global Equities

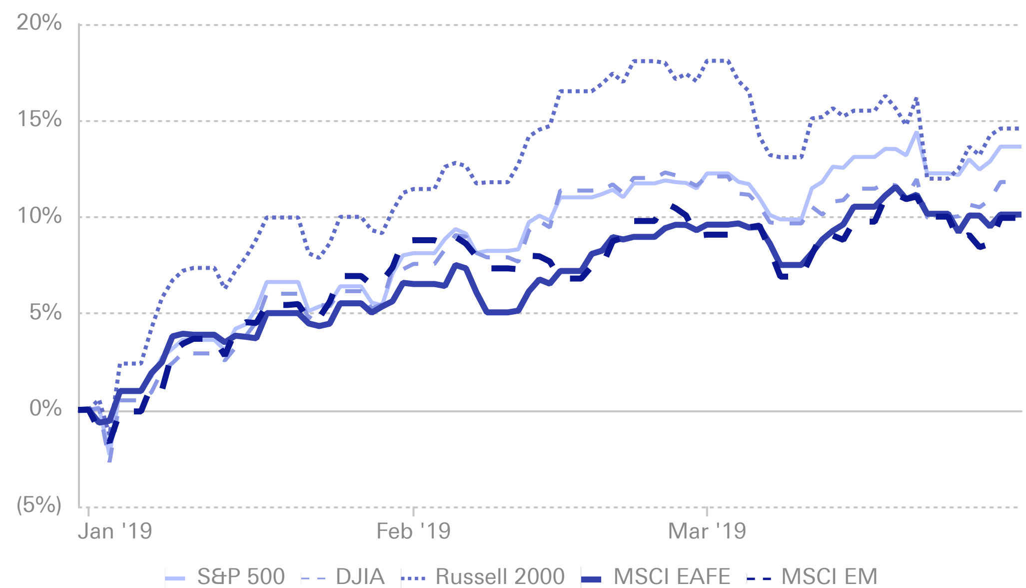
We believe that valuations are stretched significantly and that the markets need a big turnaround in earnings and economic data in order to maintain current levels and continue to go up from here.

We are focused on any sign of semiconductor demand improvement for us to believe global economies are showing signs of life.

We continue to prefer to be in US equities over almost anywhere else at the moment. Europe and Japan are still messy and struggling mightily to stave off recession. Also, as discussed in the past, we are watching for signs of the US Dollar to turnover, before we are comfortable establishing positions in Emerging Market Equities.

Once the US Dollar does begin to show signs of weakness, we believe Emerging Markets – and potentially Frontier Market Equities - will be a beneficiary.

Year-to-Date Global Equity Performance



	1 MO.	YTD	2018
S&P 500 Index (TR)	1.94%	13.65%	(4.38%)
Dow Jones Industrial Average (TR)	0.17%	11.81%	(3.48%)
Russell 2000 Index (TR)	(2.09%)	14.58%	(11.01%)
MSCI EAFE Index (TR)	0.74%	10.13%	(13.36%)
MSCI Emerging Market Equity Index (TR)	0.86%	9.95%	(14.24%)

Global Fixed Income

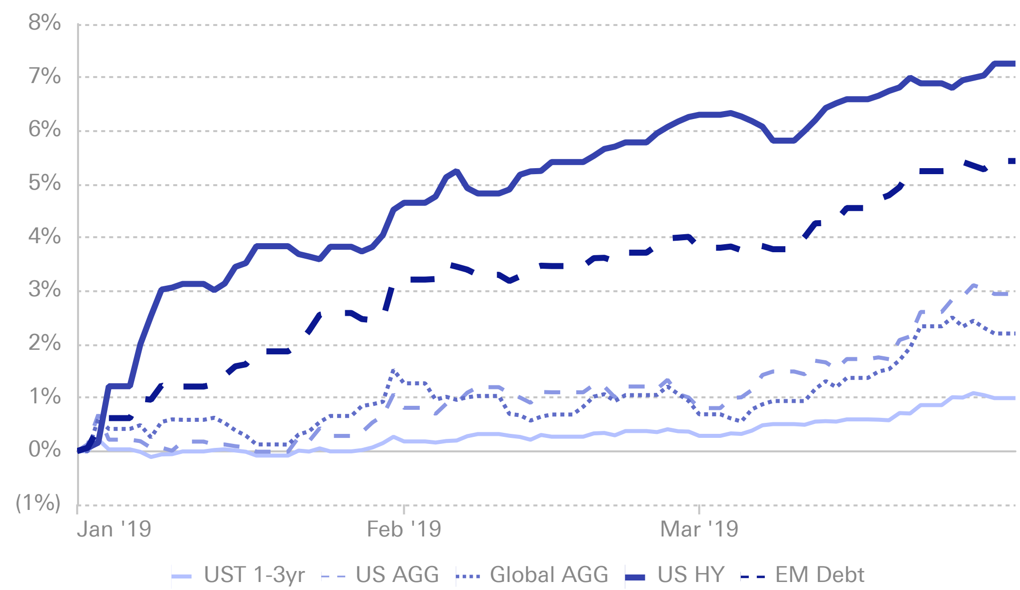
We cannot discuss fixed income without touching on something that has received a significant amount of financial press, the inversion of the yield curve. An inverted yield curve is an interest rate environment in which long-term debt instruments have a lower yield than short-term debt instruments of the same credit quality. This type of yield curve is rare and is considered to be a predictor of a US economic recession within the next 12-24 months.

Unfortunately for predictive purposes, an inverted yield curve has become a less reliable signal over time. Internally at RWM, we joke that an inverted yield curve has predicted 12 of the last 3 recessions. This information needs to be taken with a grain salt, as we have had numerous examples of inversion without recession.

However, we are watching to see if the curve corrects and then re-inverts over the coming months. That situation has actually turned out to be a stronger indicator of an upcoming recession, than if the reversion is a one off. A recent example is when the U.S. Treasury yield curve inverted in late 2005, 2006, and again in 2007 before U.S. equity markets collapsed.

In the meantime, the general drop in US bond yields seen in the first quarter has our attention, as it tends to imply global economic slowing. If we see economic numbers begin to strengthen, then we would expect bond yields to rise and put pressure on bond prices. If the market does start to correct, we would most likely continue to see bond prices go up and yields continue to fall. As with equities, we are neutral on bonds at these levels, or until we see if global economic growth returns.

Year-to-Date Global Fixed Income Performance



	1 MO.	YTD	2018
US 1-3 YR Treasury Index (TR)	0.62%	0.99%	1.56%
US Aggregate Bond Index (TR)	1.92%	2.94%	0.01%
Global Aggregate Bond Index (TR)	1.25%	2.20%	(1.20%)
US Corporate High Yield Bond Index (TR)	0.94%	7.26%	(2.08%)
Emerging Market Bond Index (TR)	1.37%	5.43%	(2.46%)

Global Real Assets

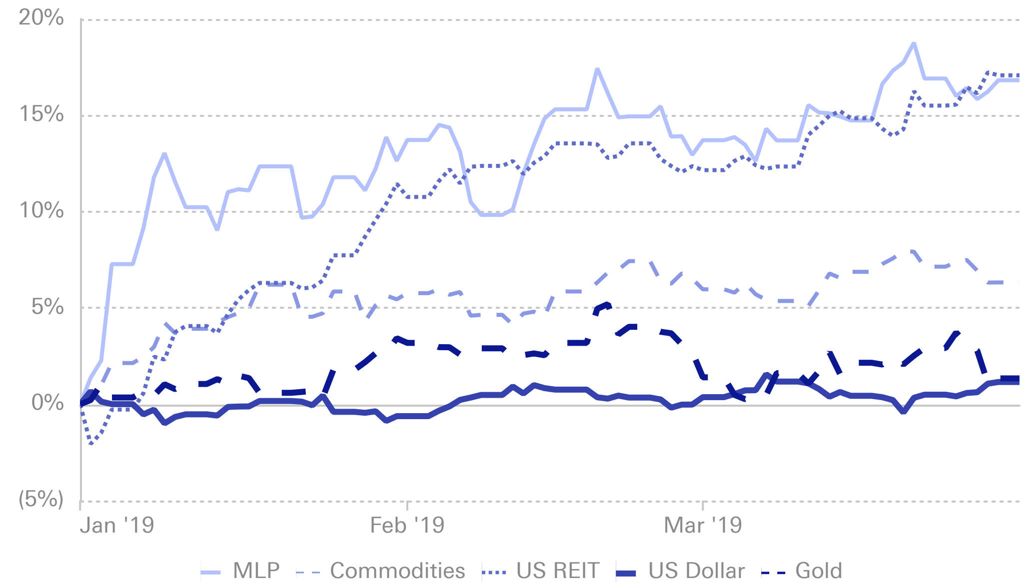
We are waiting to see what the US dollar is going to do. It has been stuck in a range for the recent past and doesn't seem willing to share any clues as to when it will begin to weaken.

We feel assured that if the US Federal Reserve Board does indeed cut rates, especially if they cut rates along the lines of the 50-basis points cut that the President has intimated, that action would provide us confirmation of the beginning of the dollar weakening process.

As stated in previous commentaries, we believe a weakening dollar would be bullish for commodities, and Real Assets in general.

We have continued to establish small positions in precious metals, as they can act as a hedge in a difficult stock market. That said, commodities will not move in earnest until the US dollar capitulates.

Year-to-Date Global Real Asset Performance



	1 MO.	YTD	2018
Alerian MLP Index (TR)	3.43%	16.82%	(12.42%)
Bloomberg Commodity Index (TR)	(0.18%)	6.32%	(11.25%)
Dow Jones US REIT Index (TR)	4.19%	17.08%	(4.03%)
US Dollar Index (TR)	1.17%	1.16%	4.40%
GSCI Gold Index (TR)	(1.34%)	1.34%	(2.14%)

ReDefine Wealth Management

Conclusion

We are at a crossroads for the equity markets and the global economy. We tend to believe the equity markets are overvalued at these levels, especially when considering the underlying economic data. That does not mean equity prices cannot push higher from here. If we have the aforementioned Brexit delay, a China trade deal, and another surprising Fed policy change – or any combination of two or more of those events – equity prices will most likely continue their unsubstantiated and meteoric rise. For our money, the risk of the economic numbers not improving swiftly enough to justify the current valuations is very strong. Thus, the probability of another sharp equity correction – akin to 4Q2019 – is pushed to the forefront.

Our 2019 Market Outlook favors high-quality equities and bonds, U.S. and EM equities, value over growth, active versus passive, and real asset strategies.

Our four major ***Global Investment Themes*** *and general market assumptions for 2019*

Volatility and Global Political Unrest Will Continue to Rise

Commodity Prices Will Rise and the US Dollar Will Begin to Decline

US Interest Rates and Global Inflation Will Move Sideways

Balance Sheets Matter Again - Value Over Growth, Quality Over Credit

Disclosures

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Investment returns are compared to the performance of several indexes shown herein. Broad-based securities indices are unmanaged and are not subject to fees and expenses typically associated with managed accounts or investment funds. The number and types of securities found in the index can differ greatly from that of the accounts held in the strategy shown. Investments cannot be made directly in an index. Diversification does not guarantee a profit nor protect against loss. The investment portfolio does not seek to replicate or correlate with these indices. Market conditions vary between the investment portfolios and the indices, and the indices do not include reinvestment of capital as to the investment portfolios. Furthermore, investment portfolios invest in strategies and positions not included in these indices.

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