ReDefine Wealth Management's Monthly Market Commentary

05-31-2019

ReDefine Wealth Management

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Market Performance Roundup

As of 05-31-2019

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)*	(5.85%)	12.33%	9.38%	(8.93%)	(0.75%)	9.66%
	MSCI World (Total Return)	(5.68%)	12.65%	10.08%	(8.20%)	0.27%	9.62%
	MSCI EAFE (USD) (Total Return)	(4.66%)	10.13%	8.05%	(13.36%)	(5.26%)	6.35%
	MSCI Emerging Markets (Total Return)	(7.22%)	9.95%	4.18%	(14.24%)	(8.34%)	10.28%
Country Equities (Local, % chg.)	*Dow Jones Industrial Average (Total Return)*	(6.32%)	11.81%	7.54%	(3.48%)	4.05%	14.45%
	S&P 500 (Total Return)	(6.35%)	13.65%	10.73%	(4.38%)	3.78%	11.72%
	NASDAQ (Total Return)	(7.79%)	16.81%	12.85%	(2.84%)	1.23%	15.90%
	Russell 2000 (Total Return)	(7.78%)	14.58%	9.26%	(11.01%)	(9.04%)	9.75%
	Nikkei 225 Stock Average (JPY) (Total Return)	(7.44%)	6.89%	3.85%	(10.29%)	(5.26%)	8.23%
	STOXX Europe 600 Euro (Total Return)	(4.73%)	13.18%	12.04%	(10.22%)	(0.17%)	5.59%
	FTSE 100 (Total Return)	(2.87%)	9.49%	8.83%	(8.73%)	(2.54%)	9.15%
	DAX 30 (Total Return)	(5.00%)	9.16%	11.06%	(18.26%)	(6.97%)	4.55%
	Shanghai Composite	(5.84%)	23.93%	16.23%	(24.59%)	(6.36%)	(0.21%)
Global Fixed Income (USD, % chg.)	*Barclays Global Treasury (Total Return)*	1.75%	1.60%	2.72%	(0.38%)	2.48%	1.36%
	Barclays US Treasury (Total Return)	2.35%	2.11%	4.22%	0.86%	6.28%	1.77%
	Barclays Global Aggregate (Total Return)	1.35%	2.20%	3.28%	(1.20%)	3.09%	1.86%
	Barclays US Aggregate (Total Return)	1.78%	2.94%	4.80%	0.01%	6.40%	2.50%
	Barclays Global High Yield (Total Return)	(1.04%)	6.33%	6.11%	(4.06%)	3.97%	6.05%
	Barclays US Corporate High Yield (Total Return)	(1.19%)	7.26%	7.49%	(2.08%)	5.51%	7.04%
	S&P Leveraged Loan Index (Total Return)	(0.20%)	3.96%	5.49%	0.47%	3.83%	5.16%
	Barclays Emerging Markets (Total Return)	0.62%	5.43%	6.50%	(2.46%)	7.31%	5.10%
Real Assets (USD, % chg.)	*USD DXY*	0.28%	1.16%	1.64%	4.40%	4.01%	0.64%
	Dow Jones US Real Estate Index (Total Return)	(0.01%)	17.08%	17.03%	(4.03%)	15.25%	7.84%
	Bloomberg Commodity Index	(3.36%)	6.32%	2.31%	(11.25%)	(12.37%)	(1.73%)
	S&P GSCI Gold	1.98%	1.34%	2.33%	(2.14%)	0.49%	2.50%
	S&P GSCI Precious Metals (Total Return)	1.31%	0.55%	1.04%	(3.58%)	(1.32%)	1.03%

June 7, 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.

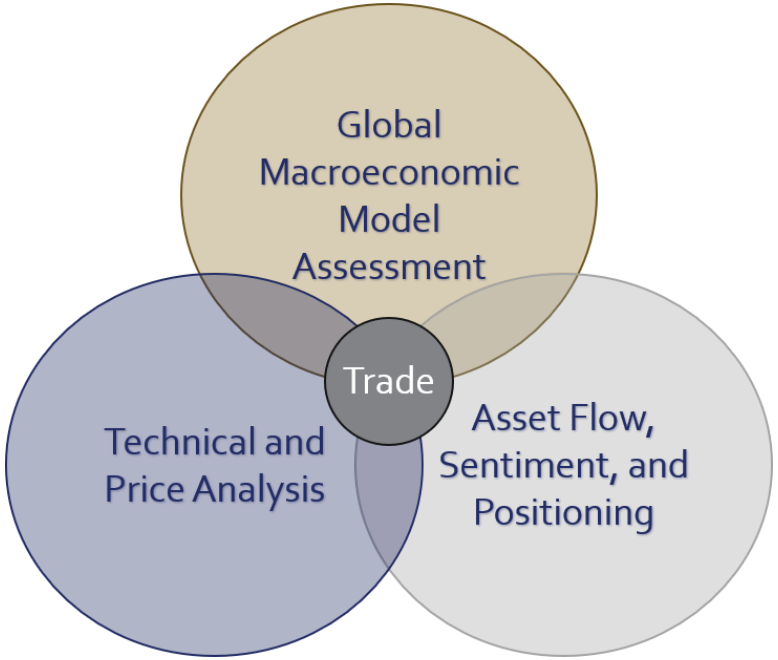
Our Global Macroeconomic Analysis provides the basis for attractive reward versus risk within global investment opportunities and helps to inform our Active Asset Allocation. We divide assets between the best opportunities that we can source within three primary portfolio components – *Global Equities,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

It Might Get a Little Bumpy

Typically, when beginning final approach for landing flying into Denver International Airport, you will hear the pilot utter the words "it might get a little bumpy" over the intercom. After flying back to Denver last week, I again heard this common message and I couldn't help but relate it back to current market conditions. In the first five months of 2019, we have experienced dramatic price increases, only to be followed by an ugly drop. Following an interesting pattern that we saw a couple times throughout 2018. Oftentimes I believe that if the S&P 500 had a pilot, we might hear "tighten your seatbelts" at least a couple times per year, especially as the global markets seem to swing on every presidential tweet, economic data release, or Fed meeting minute publication.

As we have stated since the beginning of the year, it is our opinion that the 2019 rally has been a *"Bear Market Rally"* or stated another way… a *"Dirty Rally"*. We hold this opinion because it is not supported by rosy corporate data or even positive economic numbers. It has been almost completely driven by the Fed turning dovish last December - in their words not their actions - as well as with the White House's (near) daily chatter. The markets have been lured higher with promises of an impending trade deal and more easy money from the Fed.

Unfortunately, we have seen neither promise fulfilled. Which may have finally become apparent to investors last month when China backed off any prior Trade Deal

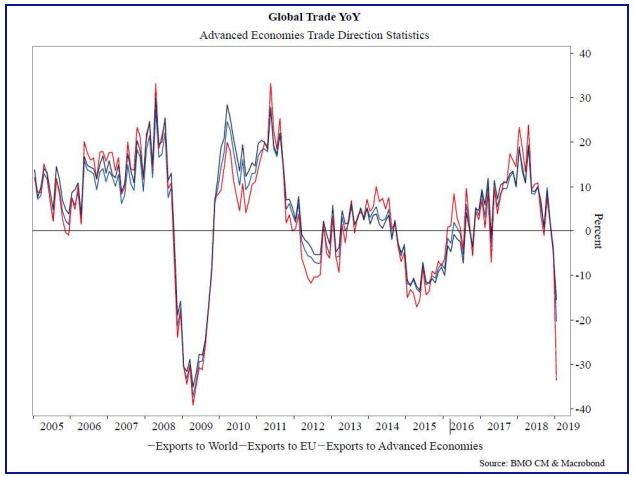


Exhibit 1. Source: BMO CM &Macrobond as of April 30, 2019

promises they had made. In return, US equity markets responded by dropping 6%-8% (depending on the index) for the month.

To add to the global market uncertainty, the global economic numbers continue to deteriorate - as we exemplified last month through showing global exports already at 2008-2009 recession levels. Exhibit 1. And those numbers do not reflect the most recent round of Trump tariffs.

To further add fuel to the potential fire, global manufacturing data has been falling to economic contraction levels. The US is currently at its lowest manufacturing number (ISM) since Trump became President. Once you start pouring on weak durable goods orders, weaker home sales, weakening auto sales, and deteriorating corporate earnings, the economy seems to be continuing the slowdown that started in earnest in 2018. Housing, an always an important growth indicator, reported that the number previously owned houses going under contract fell for the 16th consecutive month and existing home sales fell for the 14th month in a row. Auto sales dropped for the 5th consecutive month and now it has been reported that new vehicles are sitting unsold on dealer lots for the longest amount of time since 2009.

If the preceding barrage of negativity were not enough…

President Trump has responded to China's potential trade deal negotiation exit by further raising tariffs and promising to increase them to $300 billion. Trump also

Fundamental Global Macroeconomic Backdrop (cont.)

issued a threat of new tariffs on Mexico for not doing their part in helping the US control its southern border. Finally, President Trump turned his attention to India where he terminated India's preferential trade status.

President Trump has now made it very clear to all countries – friend or foe – that he is not afraid to use whatever means necessary to get them to the table to discuss (i.e. rewrite) trade agreements and other issues viewed as unfavorable to America. Many political pundits openly question the President's tactics and antics, yet few pundits question the need for trade reforms or the results that Trump could be achieving. We are not a political organization. We merely attempt to discern global market reactions to worldwide macroeconomic and public policy posturing and decision making. That stated, Trump's actions only seem to be increasing market uncertainty. Educated predictions are likewise impaired because we have no real way of knowing how these countries (especially traditional allies) will respond to Trump's moves.

Then we factor in a couple of other unknowns: what will the Federal Trade Commission (FTC) and Trump's Department of Justice (DOJ) do with investigations into huge US corporate bellwethers such as Apple, Facebook, Google, and Amazon; how far will presidential impeachment proceedings go; and how will Trump go after the "bad actors"?

What we do know for sure is the market does not like uncertainty.

The problem is we seem to be mired in a significant amount of uncertainty at the moment. Around the financial campfire, we are beginning to hear the "R word" (recession) being thrown around – even by some large institutions - which is a rare occurrence. As of the end of May, the markets remain below their Jan

Exhibit 2. Source Bloomberg as of May 31, 2019

2018 highs. In general, the markets have gone nowhere over the last 18 months and it feels like we are going to continue this "roller coaster" ride for a little while longer.

As we take time to update and review the chart showing the divergence between the S&P 500 and 10-year US Treasury yield that we have shared in previous *Monthly Market Commentary*, we continue to notice a similar level of divergence. Exhibit 2. That may not seem interesting until you consider that the S&P 500 shed over 6% in May. One would expect the divergence gap between these two indices to tighten or narrow with such a significant S&P 500 move. However, the gap remains relatively unchanged month-over-month. One issue perhaps causing the divergence to remain pronounced, could be that the 10-year UST yield also dropped significantly in May. As we have stated in previous writings, historically this type of market divergence gap closes with the equity markets falling. Mainly because the bond market tends to be a more accurate predictive gauge of an economy's overall heath. So perhaps the market is telling us all we need to know – but don't want to hear?

Which highlights a very big question… how much lower will the S&P 500 have to go to finally catch the 10-year UST yield?

We recently observed a similar situation within our favorite chart highlighting the Semiconductor Index (SOX) vs Korean Semiconductor Exports. The SOX had a 15% decline yet remains nowhere close to historical parity with the Korean Semiconductor Export level. How much further can it drop before Korean semi-

Fundamental Global Macroeconomic Backdrop (cont.)

conductor exports turnaround, especially in the face of an escalating US trade war with China?

Exhibit 3.

We think between the weakening of the US and global economic conditions, trade wars, and the myriad of Trump related issues, that the market may be in for a bumpy ride. However, depending on how some of these things get resolved, it could be an opportunity to participate in a real recovery or we may have an extended down period that could turn into a recession. *We are preparing to hear a pronounced uptick in Fed Speak in June, as Fed officials will discuss cutting the benchmark rate from its current roost at 2.25-2.50%.* We are going out on a limb (tongue firmly in cheek) to predict that after taking six weeks off of tweeting about the markets, President Trump will renew his love affair with twitter. And on the slight – but not out of the realm of possibility - chance that the Fed does lower the Fed Funds rate in June, we should all be prepared for an avalanche of "I told you so" tweets directed at Fed Chair Powell.

As investors try to adjust to the conflicting news, we would expect to continue to see swings in both directions until we get a China Trade Deal and/or Fed

Exhibit 3. Source MI2 Partners, Bloomberg as of May 31, 2019

Action and/or the markets move towards the underlying economic data.

A quick comment on the trade front…

As it relates to the proposed Mexico tariffs, we tend to not put much stock into the reality. Mainly because Trump is conducting this exercise for immigration – not trade - reasons. Much can be done in the form of posturing and lip service when it comes to immigration. And we believe that Mexico would be able to, and motivated to enact adequate reforms quickly and quietly, rather than dragging things out and running the risk of being on the receiving end of extremely viable tariff threats. We will remain vigilant to see if this chatter begins to escalate or perhaps spins in a different direction than we expect, but we tend to believe Mexico / US tensions will be settled in fairly short order.

Since last month's commentary, we have seen both China and the US start to dig in and prepare for a protracted trade war. The question becomes will Trump or China be able to handle both the economic pain and political pain for the long-term? Trump has the economic leverage, but he is fighting a controlled economy. China has the political leverage, because if the US economy continues to weaken it might be enough to foil a Trump second term. Therefore, it may just come down to who blinks first.

As this complex negotiation plays out, we should probably expect market volatility driven by renewed optimism followed by disappointment when an agreement isn't able to be reached. China has become a world power on the back of one-sided economic deals, and they will not relinquish that power without a fight. *If the new Trump tariffs are implemented and China responds aggressively, we can expect a very volatile market.*

The end of the month should provide a better vantage, as XI and Trump will be together at the G20… just before Trump's $300 billion tariff increase is scheduled to begin.

ReDefine Wealth Management

Global Equities

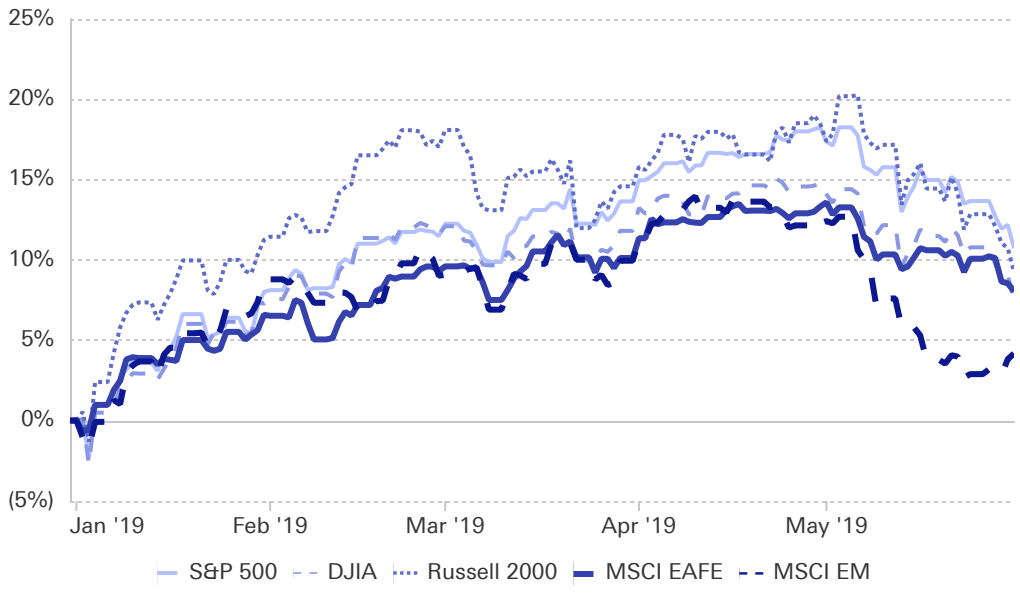
May was a very interesting month in the global markets - especially for equities. For the month, every single equity market that we follow - four global equity markets and nine country specific equity markets - where down for the month of May. Emerging Markets lead the way for the global equity markets down -7.22%, while the NASDAQ lead the country specific equity charge by shedding -7.79% for the month *(total return in USD between May 1 - May 31, 2019).*

We had been speculating that the markets were perhaps over extended in relation to the technical and fundamental numbers. So fortunately, we did not feel blindsided by May's volatility and downward pressures. However we begin June anew - as with every month - attempting to see around corners in search of alpha for our clients' portfolios.

We are caught up in a very bumpy period for equity prices globally. The battle between worsening economic data and China Trade War versus jawboning from the White House and the Fed's continued threats of a big rate cut can swing stocks on a daily basis.

We are maintaining a cautious approach to equities until we get some clarity on both the economy and trade fronts. We remain positioned in US equities only until we see the US Dollar rollover and start its longer trend down. At that point, we will most likely position aggressively toward emerging markets and potentially investments within the materials sector.

Year-to-Date Global Equity Performance



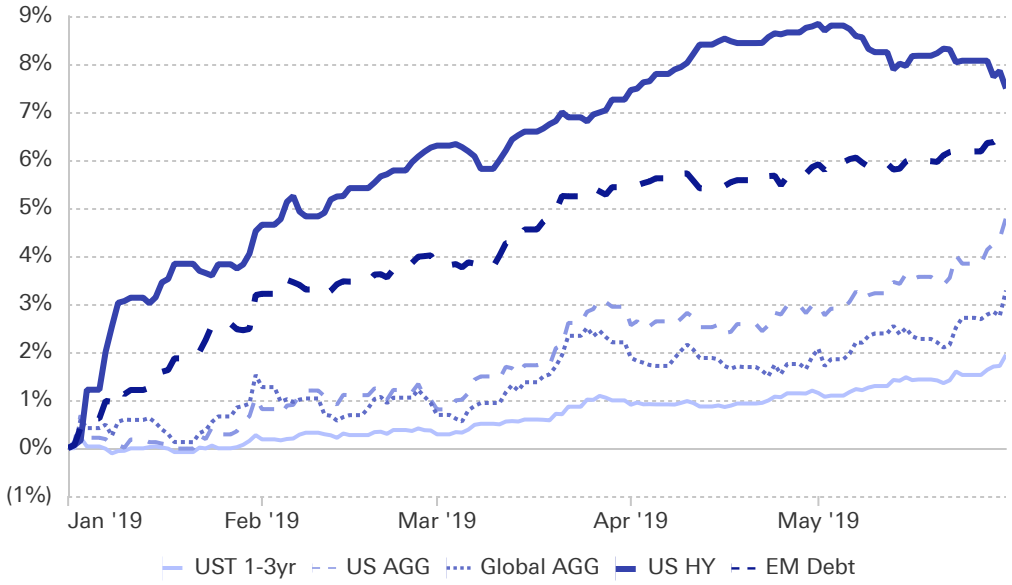
	1 MO.	YTD	2018
S&P 500 Index (TR)	(6.35%)	10.73%	(4.38%)
Dow Jones Industrial Average (TR)	(6.32%)	7.54%	(3.48%)
Russell 2000 Index (TR)	(7.78%)	9.26%	(11.01%)
MSCI EAFE Index (TR)	(4.66%)	8.05%	(13.36%)
MSCI Emerging Market Equity Index (TR)	(7.22%)	4.18%	(14.24%)

Global Fixed Income

Bonds continue to rally as the underlying economic data weakens. Again, this is of concern, especially as it relates to stocks. Historically, US Treasury yields and S&P 500 Equity prices typically don't diverge to the current degree unless we are looking at a very weak economy over the next 12-18 month horizon. Time will separate the winners from the losers within the global fixed income asset class; however, we remain of the belief that there is value in certain sectors of US fixed income.

Currently, as earnings and economic data continue to weaken, we feel strongly that there will be a negative impact on high yield bond prices in the near future. So we would avoid high yield at the current levels.

Year-to-Date Global Fixed Income Performance



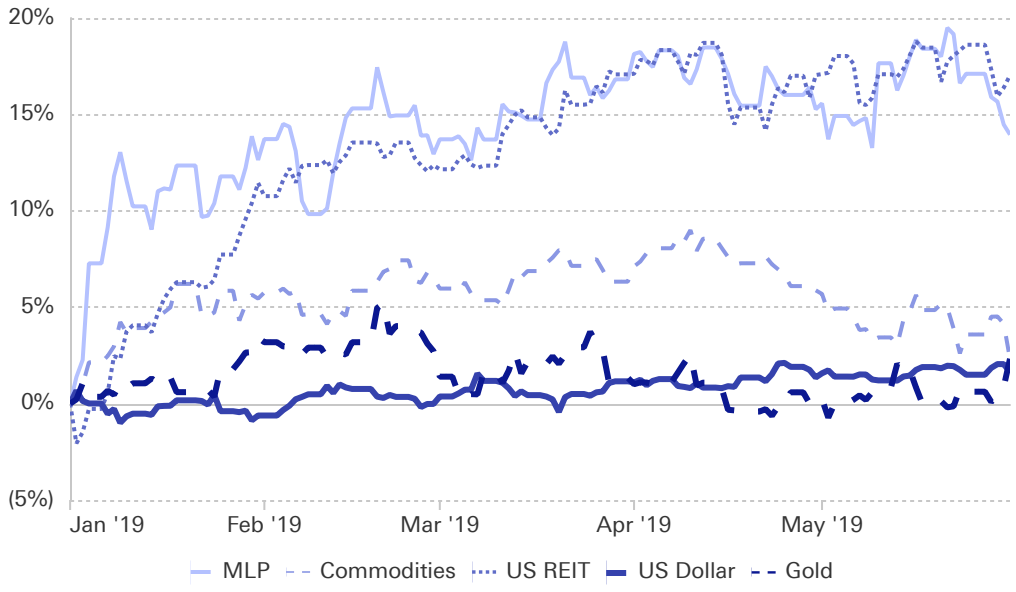
	1 MO.	YTD	2018
US 1-3 YR Treasury Index (TR)	0.74%	1.94%	1.56%
US Aggregate Bond Index (TR)	1.78%	4.80%	0.01%
Global Aggregate Bond Index (TR)	1.35%	3.28%	(1.20%)
US Corporate High Yield Bond Index (TR)	(1.19%)	7.49%	(2.08%)
Emerging Market Bond Index (TR)	0.62%	6.50%	(2.46%)

Global Real Assets

Commodities have been bouncing wildly up and down continuously as the sector tries to get a handle on global economies. Oil and gas have been beaten down of late, dragging the Bloomberg Commodities Index down over 3.3% in May *(total return between May 1st – 31st, 2019)*. Precious metals have been a mixed bag with Gold leading metals higher, while Silver and Platinum have been retreating. Real Estate, which has been the real outlier and overall best performer within the Real Assets sector this year, showed its first signs of weakness as it finished May off slightly. That stated, we are concerned about Real Estate getting close to the end of its cycle and would hesitate to be a buyer here as the housing data mentioned above might indicate.

As we have stated in previous *Commentary*, we would be looking to add into this space as the US dollar begins to weaken. We maintain the belief that commodities will offer the best value in the markets at that time, however we will remain patient and wait for the right time to take a more significant allocation.

Year-to-Date Global Real Asset Performance



	1 MO.	YTD	2018
Alerian MLP Index (TR)	(1.14%)	13.95%	(12.42%)
Bloomberg Commodity Index (TR)	(3.36%)	2.31%	(11.25%)
Dow Jones US REIT Index (TR)	(0.01%)	17.03%	(4.03%)
US Dollar Index (TR)	0.28%	1.64%	4.40%
GSCI Gold Index (TR)	1.98%	2.33%	(2.14%)

Conclusion

As we have stated since the beginning of the year, it is our opinion that the 2019 rally has been a *"Bear Market Rally"* or stated another way… a *"Dirty Rally"*. We hold this opinion because it is not supported by rosy corporate data or even positive economic numbers.

We tend to believe the equity markets are overvalued at these levels, especially when considering the underlying economic data. We continue to believe that the risk of the economic numbers not improving swiftly enough to justify the current valuations is very strong and the probability of another sharp equity correction is quickly becoming heightened. That said, we feel confident in our overall portfolio allocations - specifically our allocations to high quality, lower duration US fixed income - as well as our allocations to market volatility trades and increasing allocations to cash & cash equivalents.

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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