QUARTERLY MARKET COMMENTARY: 2019-Q3

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Despite dropping into what we deemed as oversold territory during the month of August, the most recent quarter did close on a positive note. We must admit that as we yearn for clarity over time, we are blindsided by never-ending announcements that continue to drive market volatility. The inability for "the smoke to clear" has kept equity markets within a certain trading range over the last 12-month interval. More recently, equity markets have stayed mostly within our expected range of 26,000 to 27,200 as measured by the Dow Jones Industrial Average (DJIA). When examining the annual point to point returns from 09/30/18 to 09/30/19, U.S. markets are positive 3%+ as measured by both the DJIA and the S&P 500.

We have been monitoring macroeconomic variables very closely with a greater concern on the downside versus expectations on the upside. As fundamentalists with a "buy & hold" approach, we have stayed the course with existing portfolio strategies. As a result, any portfolio adjustments have been minor due to the lack of direction exhibited by domestic equity markets. Our current investment approach to equities can be described as "extremely patient." This is evidenced by our slow rates of reduction in existing cash positions that are earmarked for redeployment to equities.

The 4th quarter had a rough start due to the reporting of weak manufacturing data which has brought the possibility of a recession to the forefront, again. When analyzing such data, we are often trying to answer the question of which came first, the chicken or the egg? Is the weak manufacturing data a result of an existing slowdown in the economy or will it be the driving force behind the reality of a recession? In our attempt to derive a perspective based on reported data, we have shifted our focus to another variable which is having a negative impact on manufacturing. We believe that bottlenecks in supply channels attributed to the trade war/tariffs are playing a major role in slowing down global manufacturing networks.

Looking beyond this factor, we realize that weak manufacturing data will also reflect demand issues. Our hope is the trade war/tariffs are playing a bigger role in this weakness because it is relatively easier to address the bottleneck issue rather than attempting to stimulate the economy in order to increase demand. In this regard, we believe that any rate reduction from the Federal Reserve will not have a direct and immediate positive impact on manufacturing. Therefore, we must direct our attention to the current trade talks which makes this month of October extremely pivotal in our economic outlook for the near future. The duration of anticipated soft data beyond the 3rd and 4th quarter reports will be contingent on these trade talks. The sooner a resolution is achieved, the easier it is to recover from an economic downturn.

Even as we complete this commentary, equity markets are experiencing a rebound based on hopes of some form of trade agreement. Since we have been through this process multiple times, we will refrain from any knee-jerk reactions until certain concrete pieces of evidence emerge. As a pattern of our conservative approach, we have always been comfortable requiring higher levels of certainty prior to making investment decisions.

Evaluating capital market expectations has been extremely challenging this year resulting in many questions from investors/clients. Should you have any questions, please do not hesitate to reach out to your consultant.

This report was written by David Y. Sun, CFA. It is a recap of the market conditions from the previous quarter and is for information purposes only.