



## Monthly Market Commentary August 2017

### **ECONOMY: US GDP Growth Strongest Since 2015**

#### **Q2 GDP GROWTH GETS STRONGER**

The Commerce Department's second estimate of Q2 U.S. GDP growth came in at an annual rate of 3%. This is up from the initial estimate of 2.6% and Q1 growth of 1.2%. This marks the strongest growth rate for the U.S. economy since Q1 2015. The improvement was driven in large part by strong consumer activity, with purchases of durable goods like automobiles and appliances rising strongly.

#### **HARVEY TO IMPACT GROWTH?**

Hurricane Harvey could be a slight negative for U.S. growth in Q3, but economists say it may ultimately provide a boost to the economy due to the resources needed to rebuild the Houston area. Goldman Sachs economists estimate a very preliminary impact of the storm to be \$30 billion in property damages, making it the ninth largest since World War II in terms of domestic property damage. They estimate that the storm could cost 0.2% of growth in Q3 due to the impact on the energy sector.

#### **UNEMPLOYMENT TICKS HIGHER**

The U.S. unemployment rate unexpectedly rose to 4.4% in August from 4.3% the previous month. The number of unemployed persons increased by 151,000 to 7.1 million. The labor force participation rate was unchanged at 62.9% in August and has shown little movement over the past year.

#### **WAGE GROWTH REMAINS ELUSIVE**

Average hourly earnings in the U.S. rose 0.1% in August from the previous month, below market expectations of 0.2%. It is the smallest increase since March. The year-on-year gain was steady at 2.5%.

#### **BUSINESS CONFIDENCE STRONG**

The Institute for Supply Management's Manufacturing PMI rose to 58.8 in August from 56.3 in July, beating market expectations of 56.5. It is the highest reading since April of 2011, boosted by a rise in production, employment and inventories.

#### **SOUNDS LIKE A BROKEN RECORD**

GDP growth in the 19-member eurozone rose to an annualized rate of 2.2% in the second quarter, up from 1.9% in the prior quarter. Inflation increased 0.2% to 1.5% in August which is closer to the ECB's preferred rate of 2%. The region's unemployment rate stood at 9.1% in July, matching the lowest level on record since February 2009. Broadly improving economic indicators, coupled with increasing financial inflows, have driven up the value of the euro by 13% against the dollar YTD.

#### **POLICY CHANGE ON THE HORIZON?**

The European Central Bank (ECB) will likely decide how and when to reduce its monetary stimulus at its October meeting according to ECB President Mario Draghi. While the U.S. Federal Reserve began raising interest rates at the end of 2015, the ECB has continued to support the eurozone with cash as a way to reduce interest rates, stimulate growth and increase inflation from levels considered to be dangerously low.

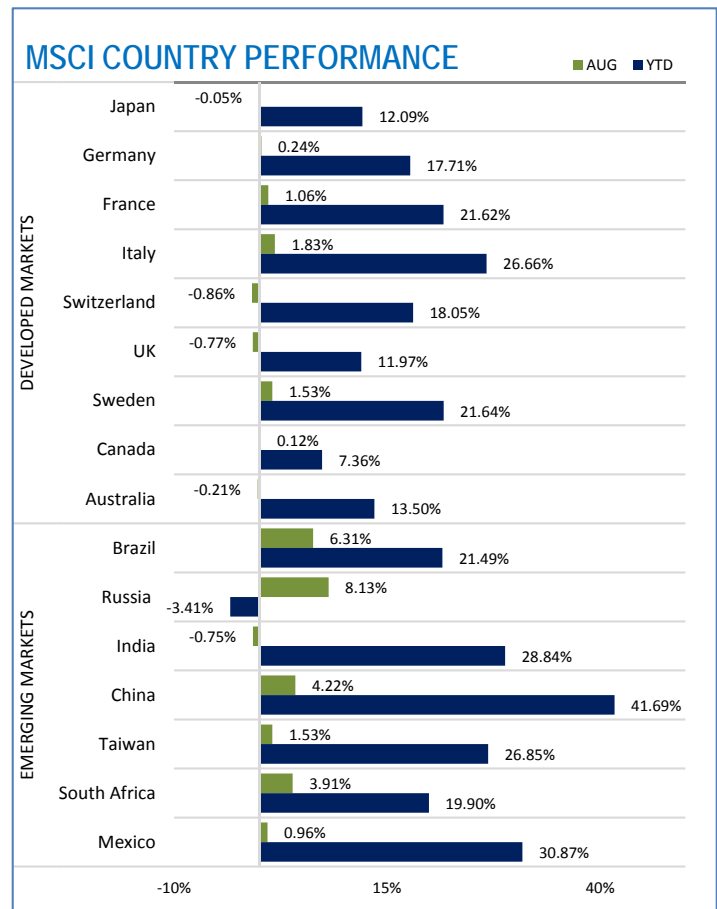
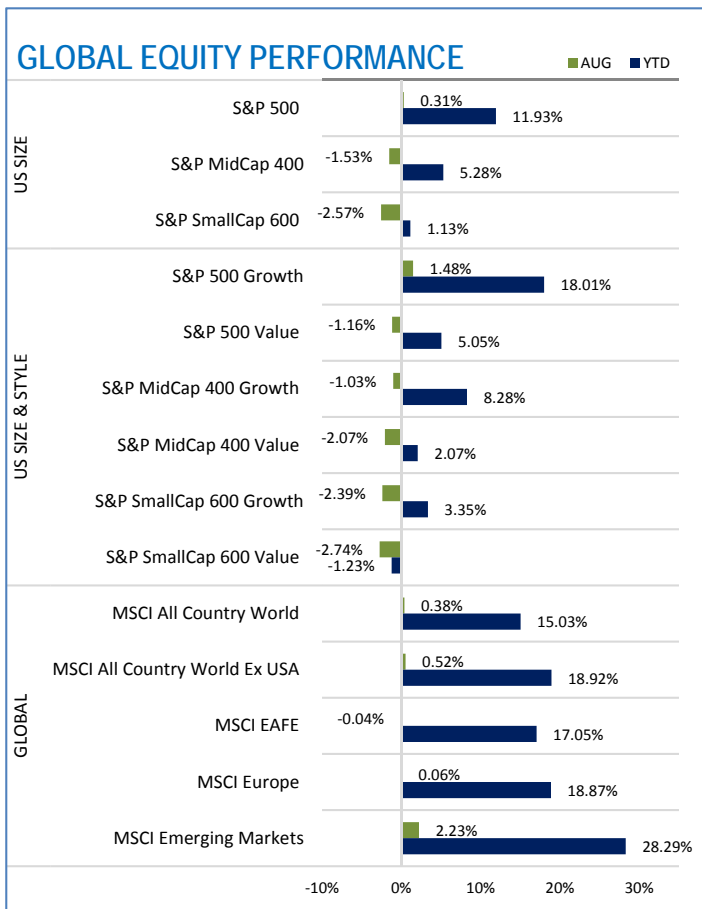
#### **CHINAS SUPPORTS UN**

China has agreed that the United Nations should take more action against North Korea after its latest nuclear test, although it still wanted more dialog to resolve the crisis on the Korean peninsula. This is important as China is by far North Korea's biggest trading partner, accounting for 92% of two-way trade last year.

#### **JAPANESE ECONOMY ROBUST**

Japan's economy expanded at an annualized rate of 4% in Q2, marking the country's sixth consecutive quarterly expansion, and the highest growth rate in more than two years. Domestic demand was strong with private consumption rising 0.9% and business spending growing 2.4% from the previous quarter. These measures were slightly offset by weaker exports, caused in part by the strong yen this year.

# GLOBAL EQUITIES: Markets Flat But Emerging Markets Still Rally



## STOCKS FLAT DURING BUSY MONTH

Despite geopolitical tensions, the struggles of the Trump administration, and Hurricane Harvey, the S&P 500 Index ended August essentially flat. Stocks continue to hit new highs, as the economy, housing, employment, and GDP continue to improve, with low inflation and interest. On August 17th, the S&P 500 recorded its biggest one-day fall since May as the North Korea stand-off and Charlottesville violence were followed by the disbanding of the U.S. administration's business councils and concerns over stretched valuations. And while multiples remain high, Q2 2017 actually beat estimates as earnings set a new record, replacing the old Q3 2014 record.

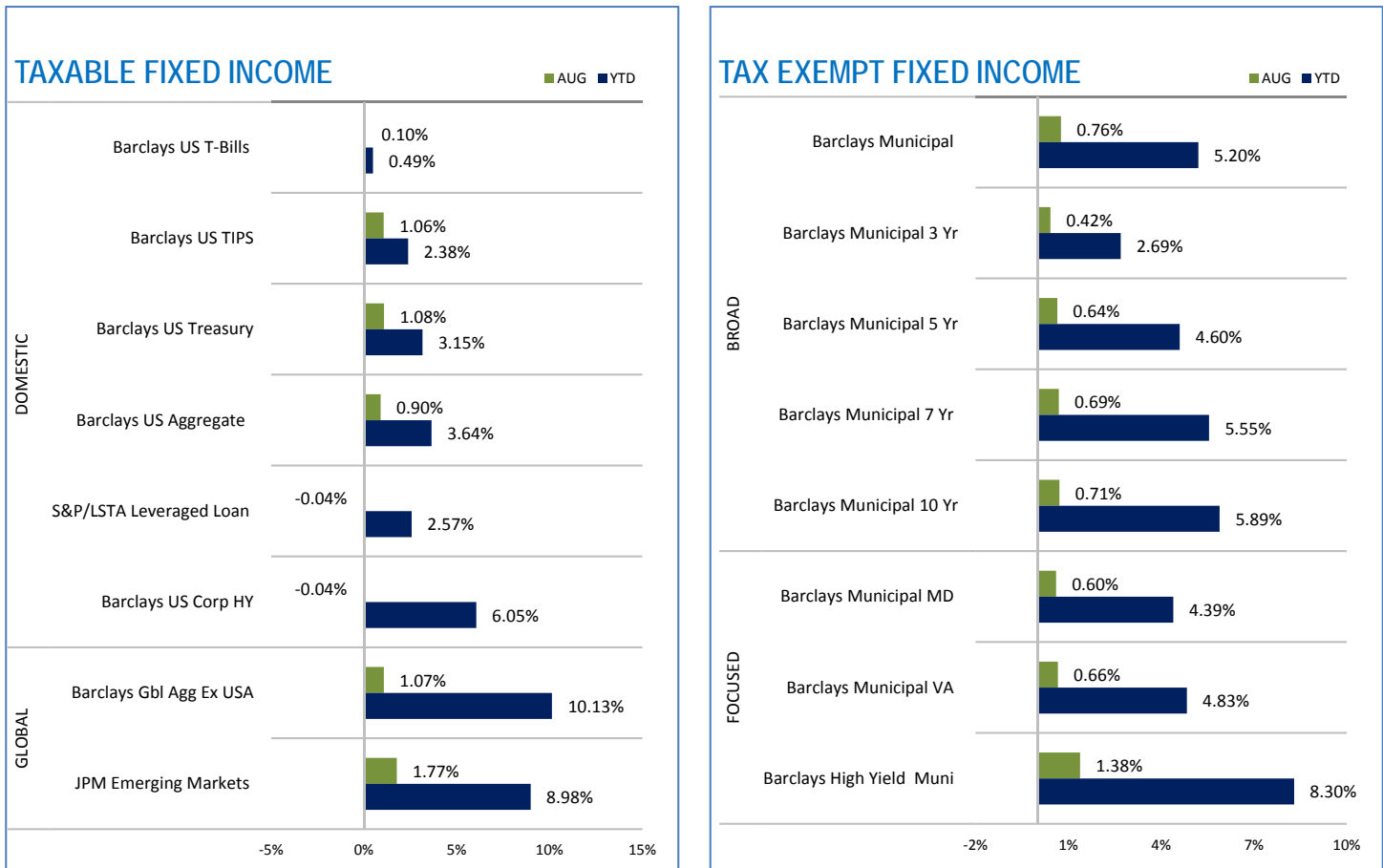
## CURRENCY NOT STOCK GAINS IN EUROPE

European stocks moved sideways in a slow trading month, despite signs of accelerating economic activity, improving corporate earnings growth and steady inflows into eurozone financial assets. The MSCI Europe Index gained 0.06%, while the euro advanced 1% against the U.S. dollar.

## LATIN AMERICA FUELS EM

Emerging markets stocks advanced in August as the MSCI Emerging Markets Index gained 2.23%. Latin America led the gains, drawing support from stronger than expected economic releases, positive political developments and a continued improvement in commodity prices. Brazilian stocks continued to climb after May's sharp selloff and gained 6.31% for the month. The government unveiled a massive plan to sell state assets in the utility and transportation sectors, and voted against a corruption trial for President Michel Temer.

# FIXED INCOME: Geopolitical Risk Benefits Save Haven Assets



## SAFE HAVEN ASSETS GAIN

Yields declined across the Treasury curve as investors sought “safe haven” assets to hedge geopolitical risks in August. The benchmark 10-year U.S. Treasury yield ended August at 2.12%, down from 2.3% in July. Government bonds outperformed corporate bonds and investment grade outperformed high yield. The Barclays U.S. Treasury Index gained 1.08% while the Barclays U.S. Corporate High Yield Index declined 0.04%.

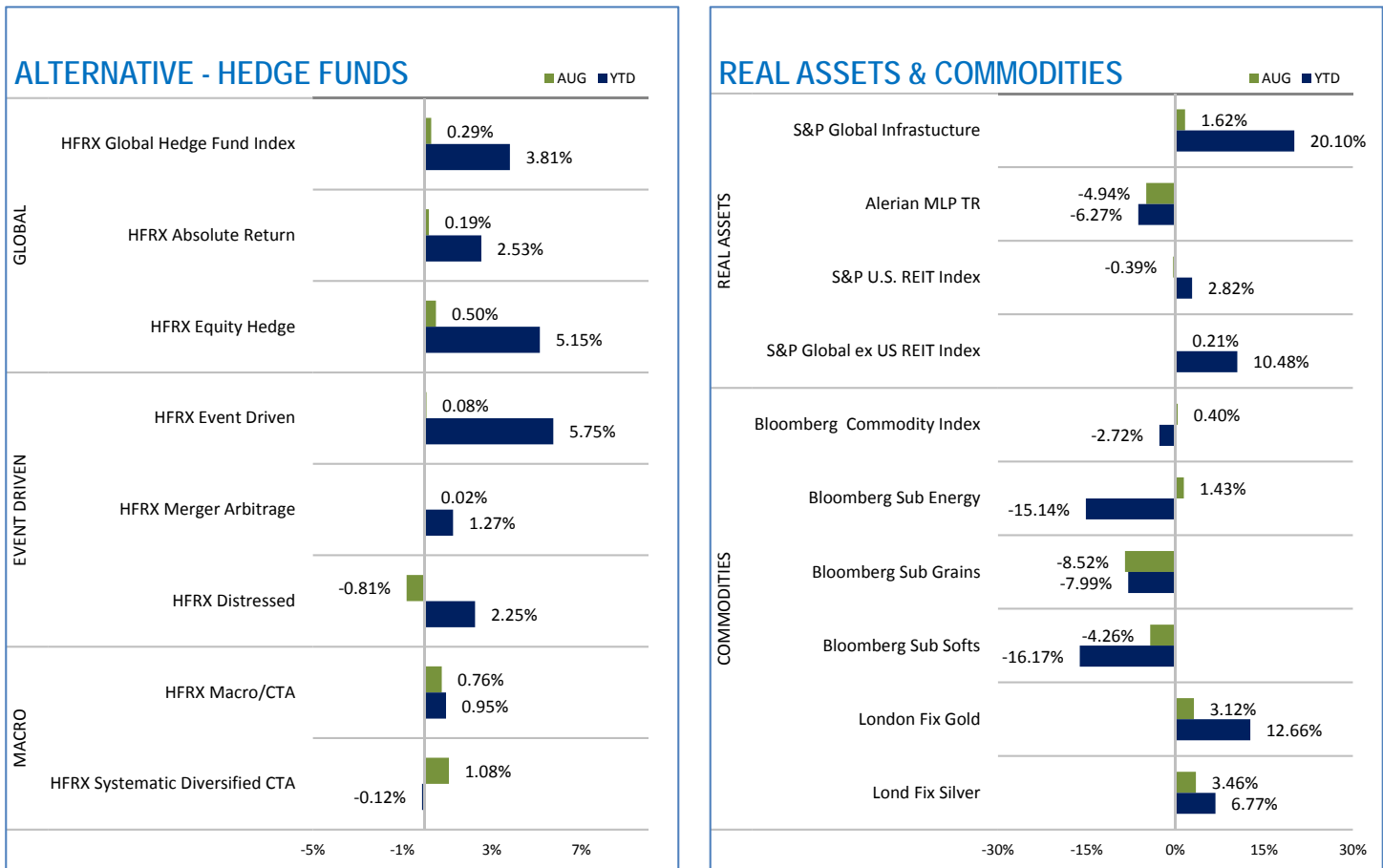
## STRONG EURO SPARKS BOND RALLY

Government bonds rallied across the eurozone as investors speculated that a strengthening euro may prompt the ECB to act more slowly as it seeks to remove accommodative policies. The yield on Germany’s benchmark 10-year note declined by 19 basis points to end the month at 0.29%. Similar maturities in Italy fell 6 basis points to 2.05%.

## MUNICIPAL BONDS PUSH HIGHER

The Barclays Municipal Bond Index increased 0.76% in August, bringing year-to-date performance to 5.20%. Duration and credit once again outperformed as persistently low inflation pushed market expectations for the next Fed rate hike into early or mid-2018. Municipals benefitted from lower supply and the increased demand for of higher quality assets.

# ALTERNATIVES: Harvey Hammers MLPs



## MACRO STRATEGY COMEBACK

Hedge funds generally posted gains in August, with Global Macro strategies leading the pack. The HFRX Macro/CTA Index posted a gain of 0.76% for August from gains in systematic trend-following managers and Emerging Markets strategies, while the HFRX Macro Systematic Index gained 1.08% primarily due to currency volatility.

## HARVEY HITS HOUSTON & MLPs

The Alerian MLP Index was down 10% by mid-August, before recovering to close the month down 4.94%. The index is now down approximately 18% from its February high, and down 6.27% YTD. August's performance can in part be attributed to Hurricane Harvey. It is estimated that 14 Texas oil refineries were closed due to the storm, which represent approximately 17% of U.S. capacity. Pipeline closures and supply/demand disruptions from area marine terminal operations are also affecting the sector.