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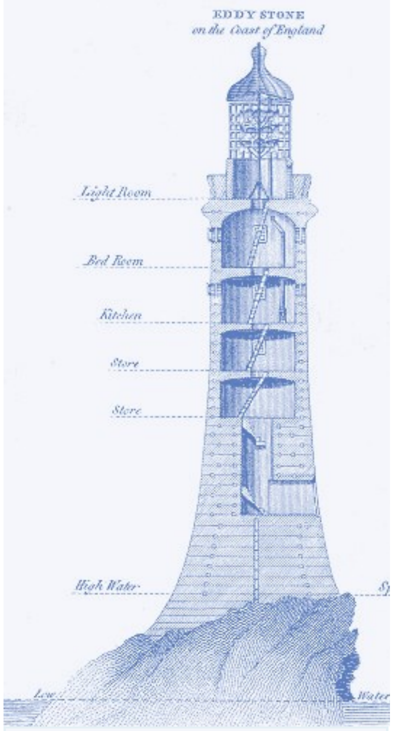
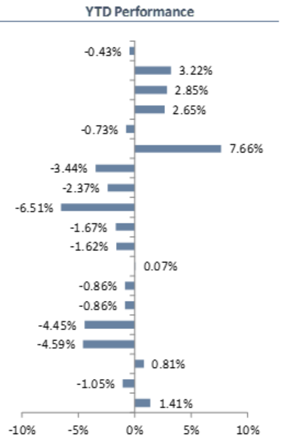


The Waypoint

Volume 1, Issue 7

Mid-Year Market Review

Asset Class Total Returns		1m	3m	12m	YTD
World Equities	***MSCI AC World***	**-0.54%**	**0.61%**	**10.73%**	**-0.43%**
U.S. Equities	***Russell 3000***	**0.65%**	**3.89%**	**14.78%**	**3.22%**
Large Cap	*Russell 1000*	0.65%	3.57%	14.54%	2.85%
Large Cap	*S&P 500*	0.62%	3.43%	14.37%	2.65%
Large Cap	*Dow Jones Industrial*	-0.49%	1.26%	16.31%	-0.73%
Small Cap	*Russell 2000*	0.72%	7.75%	17.57%	7.66%
International Equities	***MSCI AC World Ex U.S.***	**-1.84%**	**-2.24%**	**7.79%**	**-3.44%**
Developed Market Equities	*MSCI EAFE*	-1.19%	-0.80%	7.37%	-2.37%
Emerging Market Equities	*MSCI EM Free*	-4.09%	-7.73%	8.59%	-6.51%
Fixed Income	***Barclays U.S. Universal***	**-0.15%**	**-0.27%**	**-0.28%**	**-1.67%**
U.S. Core Fixed Income	*Barclays U.S. Aggregate*	-0.12%	-0.16%	-0.40%	-1.62%
High Yield	*ML High Yield Master II*	0.33%	1.00%	2.51%	0.07%
Alternatives	***Bloomberg Commodities TR***	**-3.64%**	**-0.07%**	**5.82%**	**-0.86%**
Commodities	*Bloomberg Commodities TR*	-3.64%	-0.07%	5.82%	-0.86%
MLP's	*Alerian MLP*	-1.54%	9.55%	-11.64%	-4.45%
Gold	*GSCI Gold Spot TR*	-3.70%	-5.49%	0.20%	-4.59%
Cash	***ML 90 Day T Bill Index***	**0.17%**	**0.46%**	**1.36%**	**0.81%**
Hedge Funds	*HFRX Global Hedge Fund*	-0.38%	-0.03%	2.27%	-1.05%
Real Estate	*Dow Jones Real Estate*	4.07%	7.78%	5.19%	1.41%



Inside this issue

About "The Waypoint"

This seventh edition of The Waypoint includes data from Oxford Economics, provided by Gina Sanchez, an independent investment consultant who has partnered with Lumina Wealth Management. She is an economist, former portfolio manager and regular contributor on CNBC, as well as a member of the Oxford Global Centre for Economics in London.

Introduction

◊ **The markets are looking past short-term tax stimulus:** In a classic "what have you done for me lately" fashion, the markets are starting to discount lower earnings growth in the future as analyst estimates don't project tax cut stimulus beyond 2018.

◊ **The US continues to garner returns while multiples have contracted dramatically on the international front:** Emerging Markets have taken the brunt of the effects with China dragging down sentiment despite rising oil prices which should be a net positive for the EM equity basket.

◊ **Treasuries outlook clear as mud:** Safe-haven trading has supported yields down to 2.8% while concern for the deficit and the need to issue significantly more Treasuries argue for much higher yields in the medium term.

Market Review: All Eyes on the US

The rare synchronized expansion among major world economies that was cheered on by markets and policymakers may be slowing, with only the near-term prospects for the United States looking significantly better. So, while 2018 may still turn out to be a very good year for overall global economic growth, and certainly for the United States, policies on trade suggest trouble is ahead for everyone else in the second half. Euro zone growth has slowed remarkably, posing a challenge to the European Central Bank's plans to soon stop buying bonds.

The International Monetary Fund (IMF) warned that new import tariffs threaten to undermine the global trading system, prompt retaliation by other countries and damage the U.S. economy. The IMF, in a review of U.S. economic policy, also took a much less optimistic view on America's economic growth potential. While U.S. economic growth is expected to be strong this year and next, recent tax and spending measures could cause greater risks from 2020 onwards. A cycle of retaliation on trade is likely to dampen national and international investment, interrupt global and regional supply chains and undermine a global system that has supported U.S. growth and job creation.

Estimates on the impact of tariffs range from a negative 0.2% to 0.4% of US GDP growth by 2020. Tariffs on $50 billion of imports from China were imposed in mid-June, a move that came on top of hefty duties on steel and aluminum imports implemented at the start of the month. The risks come at a time when the Federal Reserve has pushed interest rates into positive territory adjusted for inflation for the first time in over a decade, a move that raises borrowing costs for consumers.

The number of Americans filing for unemployment benefits unexpectedly fell last week, pointing to a further tightening of labor market conditions. Other data showed a moderation in factory activity amid a decline in new orders, likely an indicator of early tariff effects. Despite the pullback, US manufacturing remains solidly expansionary. The labor market, which is underpinning economic growth, likely will pave the way for the Federal Reserve to raise interest rates two more times this year. Last week the U.S. central bank increased borrowing costs for a second time this year and forecasts two more rate hikes by the end of 2018.

The European Central Bank (ECB) announced it will soon bring its asset purchase program to an end and hinted at a first-rate hike in the summer of 2019. Bloomberg Economics' estimate of neutral policy suggests their second hike shouldn't be too far behind. If the stance on policy prompts overheating, the ECB may find it has some catching-up to do.

China's growth this year shows no signs of slowing despite rising tensions with the U.S. over trade and disappointing economic data in May. The median estimate of 60 economists shows the economy will grow 6.5 percent this year. That's exactly what the government is targeting and hasn't changed since mid-January. Economic expansion is seen slowing to 6.3 percent next year and 6.2 percent in 2020, according to a Bloomberg survey. The forecast for economic expansion this quarter was raised on the expectation of higher factory-gate prices and better exports and imports. China's central bank said in mid-June it would cut the amount of cash that some banks must hold as reserves by 50 basis points (bps), to accelerate the pace of debt-for-equity swaps and spur lending to smaller firms. The reserve reduction, the third by the central bank this year, had been widely anticipated by investors amid concerns over market liquidity and a potential economic drag from a trade dispute with the United States. China's policymakers have been pushing for debt-for-equity swaps since late 2016 to ease pressure on firms struggling with their debts.

Going Forward: Long Run Inevitable, Short Run Unforecastable

Inevitable is the near-term slowdown of the most recent economic expansion, which will extend the recovery in the US just long enough to pass the rest of the world. Second, the medium-term evolution of the US population from a majority non-Hispanic white population to a plurality, also termed "majority-minority," for the total population by 2043 and for children by 2019, according to the 2016 US Census Bureau. Finally, the long-term reality that sustainability matters will play a role in determining the long-term trend growth trajectories. This leaves event risk, the most challenging to forecast, as the primary risk on the table as we head toward the inevitable. It is in this environment that we must invest and in doing so, we must keep a close pulse on the near-term directional pull.

The Near Term Economic Slowdown

Now almost a decade since the Financial Crisis, we are nine years into one of the longest and largest bull runs in US history. Early in the crisis, the policy aimed at stemming the pain from balance sheet repair, shifting the weight of the problem from the household to the government with corporations simply maintaining their indebtedness on average. However, the current administration has embarked on an active mission to move demand forward through tax incentives, debt and deregulation. While the markets celebrated these goals immediately post-election, the impacts are proving to be short term. Equity earnings growth came in at 23.9% for the S&P 500 for Q1 2018 and are projected to rise to an even more stupendous growth rate of 30.8% for Q2 2018. These are not sustainable growth numbers. Small Cap stocks, the long-time favorite this year will only gain a quarter advantage, peaking out in Q3 at an expected 34% EPS growth rate.

However these are one-time gains rather than results from continuous operations, suggesting that the longer-term estimates of 7-9% EPS growth are the norm not the exception and will ultimately be the direction that gravity pulls. Add to that the uncertainty around trade tariffs, which are expected to be at the very least inflationary and at the most demand destructive to disposable income. Multiples are already starting to look past the peaks and discount a less exuberant future. Corporate high yield has been on a risk roller-coaster with spreads landing toward the top of the range for the year.

That said, economic expectations remain positive, the labor market continues to tick stronger and the Fed looks determined to normalize. While these are short term policy measures, they will put the US ahead of Europe, the UK, Japan, China and the rest of Emerging Markets. US equity markets, and small caps in particular have dominated, but value stocks are poised for a comeback, which feels signals defensiveness. Within bond markets, Treasuries posted positive, albeit small, gains while high yield has done reasonably well. Investment grade credit suffered the most as risk premiums have deteriorated. International markets have lagged on all fronts, both equity and bonds. Emerging Markets were hit the hardest in both equity and fixed income, as the US dollar demonstrated continued strength and sparked concerns over global liquidity. We could easily see further US outperformance, but with a change in the tenor of the markets to a more defensive stance.

Geopolitical Concerns

We continue to see oil on two fronts. First from a supply perspective, very few countries have the ability to bring supply on line quickly enough to counter the effects of the Iranian nuclear sanctions as well as the Venezuelan crisis. Saudi has increased output dramatically along with the US, though neither is fast enough. Combine that with the continued proxy wars in the Middle East and we could very easily envision a short-term spike in oil prices beyond the $80 per barrel level that OPEC generally deems as "demand destructive." However, we don't anticipate oil prices remaining elevated. We still see oil in the range of $72 to $74 per barrel in the long run and expect that to continue toward those levels.

Thank you for reading The Waypoint from Lumina Wealth Management. If any specific financial topics pique your interest, or you want to hear our thoughts on a global or domestic event, please contact us.

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