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The Waypoint

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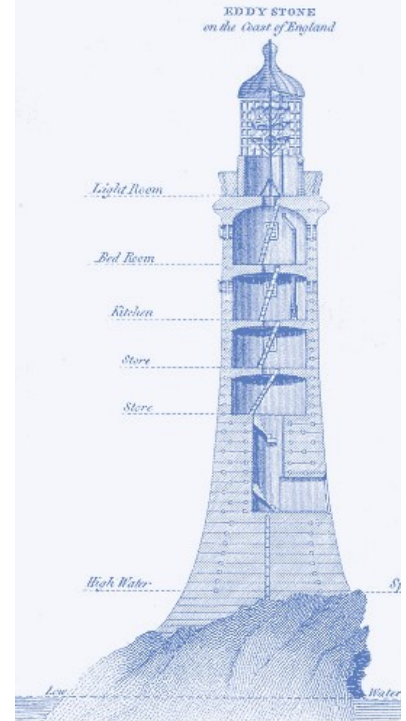
Lumina Welcomes Rachel Moore

We are excited to introduce you to our newest team member, Rachel Moore! Rachel is an alumni of the UNCW Cameron School of Business. During her time at UNCW, she earned a Business degree with a concentration in International Business as well as a minor in Spanish. Originally from Greensboro, she now considers Wilmington home. In addition to her new position as account administrator with Lumina Wealth Management, she also has a new addition at home- Ryder the Goldendoodle! Rachel is looking forward to meeting and working closely with our wonderful clients. She brings positive energy, is very eager to familiarize herself with our business and is an integral part of the team here at Lumina!

Also, we would like to share with you a special report that compares the economies of Wilmington, Charleston and Savannah with the rest of the United States. This report was a project of our 2018 Summer Intern, Alexanne Penton. Alexanne's project gives us some interesting insights into our economy and the economies of similar cities. We hope you will take a few minutes to view this report on our website: www.luminawm.com.

August 2018 Market Update

- **As economic momentum pushes ahead at a strong pace, it seems that not even trading tensions can stand in the way of continued market strength:** However, the momentum is now waning, and the underlying current is turning decidedly defensive.
- **Higher energy and tariff-related metals prices are creeping into inflation readings:** The markets are looking to the Fed to contain inflation, but not overshoot, a fine line to walk.
- **US markets are discounting escalating risks of global trade conflict, mid-term elections and Fed policy missteps:** All invite short term volatility to US equity markets that bear monitoring. Far more attractively priced EAFE and EM markets emerge as a potentially better option to watch.



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About "The Waypoint"

This eighth 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.

Market Review: Fast Pace Growth

The U.S. economy grew at the fastest pace in nearly four years in the second quarter as households boosted spending and net exports surprised positively. Gross domestic product rose 4.1%, with consumer spending rising 4.0%, contributing 2.7% to the growth rate. Net exports contributed 1.1% and a 7.3% increase in business investment contributed 1.0% to overall output. Output expanded 3.1% in the first half of 2018, putting the economy on track to hit the administration's target of 3% annual growth.

More jobs were created in June than expected, but steady wage gains pointed to moderate inflation pressures that should keep the Federal Reserve on a path of gradual interest rate increases this year. An increase in consumer spending and tighter labor market were key topics at last month's FOMC meeting, which produced a 25-basis-point rate hike and a rise in quarterly forecasts from one to two more hikes this year. The Fed also removed language indicating that rates would remain low for some time.

U.S. stocks rose early in July, giving the Dow and S&P 500 their biggest gains in more than a month. Bank shares jumped ahead of earnings reports, while industrial, energy and consumer discretionary shares rose sharply. Overall, US equity markets followed the strong economic results, despite the brewing trade conflict between the United States and China, which could slow hiring, especially in the manufacturing sector. The U.S. and China imposed reciprocal duties on $34 billion worth of the other's imports. Wall Street responded positively late in the month as President Trump secured concessions from the European Union on trade, despite a disappointing quarterly report from Facebook that slammed its stock and threatened to put the brakes on a tech rally.

The International Monetary Fund left its global economic growth forecast unchanged at 3.9% for both 2018 and 2019. IMF projections take into account only tariffs currently in force, so larger actions are not included. Forecasts for the United States and China were both unchanged, with U.S. growth pegged at 2.9% in 2018 and 2.7% in 2019. China's growth forecast was at 6.6% in 2018 and 6.4% in 2019. The IMF warned world economic leaders on July 21 that the recent wave of trade tariffs being discussed would significantly harm global growth. Further, the IMF declared in late July that the U.S. dollar is over-valued, while China's yuan is in line with fundamentals. Nearly half of global current account balances are now excessive, adding to growth risks and trade tensions. The IMF also said excessive current account surpluses and deficits are increasingly concentrated in advanced economies.

The euro fell late in the month as the European Central Bank clung to its easy money policy and signaled no change to its timetable to move away from ultra-low rates or end its bond purchase program. Sterling, already pressured by a strong dollar, fell on the European Union's rejection of key elements of Britain's new trade proposals after it leaves the EU. ECB President Mario Draghi indicated he was confident regional inflation would reach the ECB's 2% target; however, rising tariffs and trade barriers would hurt Euro growth.

China's economic expansion slowed in line with expectations, signaling broadly stable output as trade conflict with the U.S. intensifies. Gross domestic product increased 6.7% in the second quarter, which was the slowest pace since 2016 and in line with the 6.8% pace in the previous quarter. While investment growth and industrial output slowed, steady growth heading into the second half of the year provides support to the potentially negative effects of trade barriers with the U.S. and to continuing multi-year efforts to control debt and clean-up the financial system. The world's second-largest economy is expected to slow this year, with the government's growth target at 6.5%.

All of this is entirely separate news from what has been going on in Turkey. Cross border bank holdings are low, trade flows are miniscule (trade tariffs hurt them way more than their tariffs can hurt us) and portfolio exposure is only 0.5% of the MSCI Emerging Market Equity Index. If you look across markets, this has been a fairly isolated event. Turkish equity markets have sunk and the only other EM market that has sunk in a similar fashion is China, which has more to do with Tencent Holdings missing earnings than Turkey. The Lira is down, but no other currency has responded in kind except for risk driven modest dips. Sovereign Credit Default Swaps (CDS) have spiked for Turkey and Russia but have remained within reasonable bands for the rest of EM. While short-term interest rates in Turkey have spiked to 22.9%, no other EM is showing that kind of liquidity dry up. There are no real avenues for contagion and therefore, no contagion has occurred. One element of this clash with Turkey to consider is their strategic military significance. They are the base from which we battle ISIS and to lose that would be a blow to the US military. This could put the balance of geopolitical off kilter.

Going Forward: Canary In the Coal Mine

Economic peaks and troughs are notoriously hard to call, though given the extra fuel added to the latest economic expansion in the form of tax stimulus; it is not too risky a proposition to suggest that 4.1% year over year growth is probably not a sustainable pace. While we may continue to get similarly strong numbers in the near term, it is unlikely they will maintain throughout 2019. And, to be sure, economic forecasts are calling for a cooling of the current global expansion. However, that cooling is expected to be moderate rather than recessionary, which still leaves room for continued growth, particularly in the Emerging Markets.

Falling Volatility

Trade fear and uncertainty have eased, and winners and losers have generally been identified. US market leadership is rebounding and, interestingly, EAFE and EM equity markets, where damage may not be immediately concerning, are following suit. However, compression in volatility may only be the calm before the storm. Namely, increasing inflation and underappreciated risks in the Middle East, including the potential for a significant oil supply disruption, could cause further spikes in oil prices and bring about an equity correction. In addition, market confidence in the Fed's ability to manage accommodation wind-down may wane if any evidence of runaway inflation or overshoot emerges. The risk of Fed policy misstep looms large and it is worth noting that present volatility levels do not fully reflect the current risk environment.

Subtle Shifts in the Market

While the markets are rebounding on strong economic fundamentals, the recent compression in multiples suggests that the markets are reevaluating the forward looking prospects for earnings and finding the prospects less attractive. Markets are becoming more defensive, particularly equity markets. Value is now outperforming growth and defensive sectors such as staples and utilities are beginning to hold their own. We suspect that the shift towards defensive stocks is somewhat consistent with the sluggish movement in the long end of the yield curve, which suggests that the outlook for long term growth is weakening.

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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