The Type 2 Investor

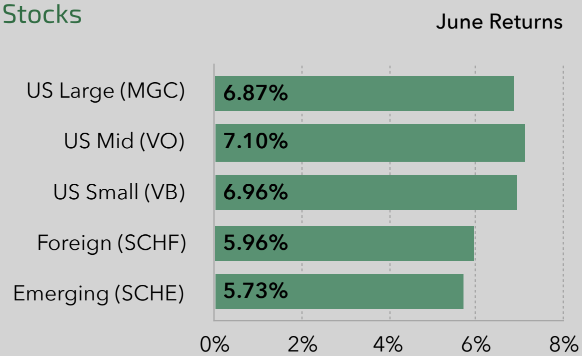
July 14, 2019

June 2019

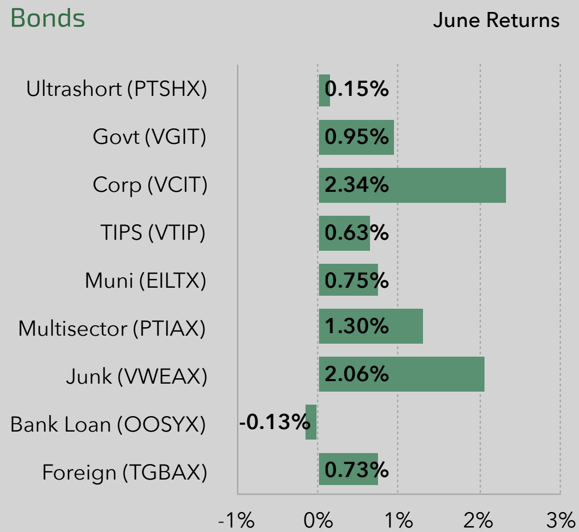
Economic Data

- US payrolls rebounded strongly in June as 224,000 jobs were added; the unemployment rate edged up to 3.7% and wage growth came in below expectations
- Retail sales rebounded in May, up 0.5%, and the previous month was revised upward, as well
- Y/y inflation (CPI) fell to 1.6% in June
- Lower mortgage rates helped existing home sales rebound 2.5% in May

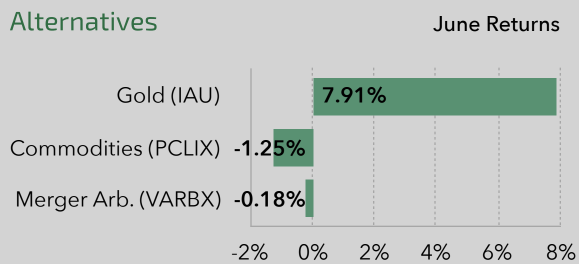
Stocks



Bonds



Alternatives



Performance data provided by Morningstar.

The brain uses two systems to process information. The first type is intuitive but lazy, rapidly forming judgements with no conscious input. The second system is slow, reflective, and is not guided by emotions. It is that second system – type 2 – that we want in control of our investment portfolios.

Powell Patient No More

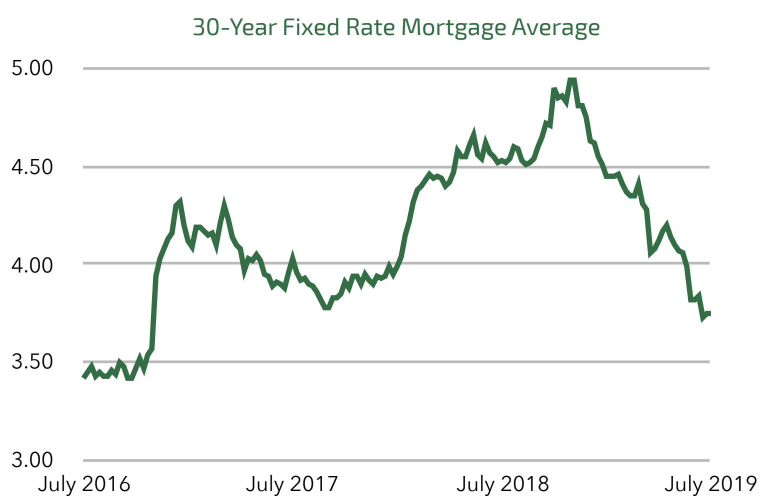
The Fed removed the word "patient" from its June policy statement, in reference to their stance on future adjustments to the federal funds rate. They also noted that economic activity was moderating. The dot plot indicates a 25 bps cut is coming this year, although seven members expect 50 bps in cuts over the next six months. The market was pricing in a near-certainty of two cuts following the statement release, and a 70% chance of three.

More recently, testimony this past week by Federal Reserve Chairman Jerome Powell seems to have made a July rate cut an almost certainty. Uncertainty surrounding trade tensions and concerns about the waning strength of the global economy continue to weigh on the US economic outlook. Low inflation was also cited as a supporting factor for more accommodative policy. The prepared statement was so dovish in tone the question has moved from whether or not we will get a cut, to whether it will be 25 bps or 50.

I feel like more than anything else it's the bond market that is forcing the Fed's hand. We hit an inflection point eight months ago, and the yield on the 10-year Treasury has fallen 1.13% since and has been below the fed funds rate for almost two months now, creating an inverted yield curve. We've talked in the past about how this is a harbinger for recession.

Lower interest rates have pushed even more global debt into negative-yield territory. The amount hit a record $13 trillion, with about 60% of that from Japan. That's roughly double the amount this time last year, and offers a lot of ways one could choose to lose money.

One positive to all this—if you're a home owner—is that mortgage rates have come down substantially, falling 1.19 percentage points since their recent highs in November. This has boosted refinance activity, brought buyers back to the market, and helped to keep home prices elevated. Mortgage rates should stay low for a while. Time will tell whether that's enough to keep prices up.



Source: Freddie Mac

Portfolio Positioning

Stocks have rebounded nicely from a painful May, with the S&P 500 closing above 3,000 for the first time on Friday. It just doesn't feel like the market is doing as well as that might suggest, however. To put things in perspective, that mark is less than 3% above its high from last September. Bonds have been doing much better by comparison over that stretch. Emerging markets have been lagging so far this year, but a rate cut in the US could give emerging market central banks some wiggle room to ease policy without risking capital flight.

Gold has finally broken out to the upside, hitting a six-year high after surging more than 10 percent since the middle of May. The shiny metal has been helped in part by the prospect of lower interest rates reducing the opportunity cost of holding an asset that doesn't produce an income yield.

In other commodities news, trouble in the Strait of Hormuz has helped push oil back above $60. This narrow strip of water, with the UAE and Oman on one shore, and Iran on the other, sees about 30% of the world's supply pass through it, according to Reuters. But lately, oil tankers seem to keep getting attacked on their way through it. And, you know, that's kind of a problem. Unless you're invested in oil. The June return numbers don't reflect it well, but the commodities position (PCLIX) is up 20% from it's Christmas lows.

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Tactical Asset Allocation					
Asset Class	Heavy Under-weight	Under-weight	Neutral	Over-weight	Heavy Over-weight
Fixed Income			●		
Ultrashort					●
US Govt.		●			
TIPS				●	
Multisector			●		
Bank Loans	●				
Foreign Bonds			●		
Equities	●				
Large Cap	●				
Mid Cap	●				
Small Cap	●				
Developed Intl.		●			
Emerging			●		
Alternatives					●
Commodities					●
Hedging					●

Binge Box

Schitt's Creek (Netflix)

The show follows the Roses, a wealthy family of four who find themselves penniless after mismanagement by their accountant results in years of back taxes owed. They are forced to move to the only asset they have left, Schitt's Creek, a fictional town the patriarch (Eugene Levy) bought as a joke for his son's (Dan Levy) birthday. Despite the name, this is actually a pretty intelligent comedy with characters that develop and grow on you. Catherine O'Hara steals the show with the way she brings the matriarch's character to life, including a brilliant accent that is all her own. Annie Murphy also does a great job playing the daughter, particularly her mannerisms. There are now four seasons available to stream on Netflix.

About EmeraldSpark

EmeraldSpark Investments, LLC is a Registered Investment Adviser based in Chicago, IL. We were founded by Ryan P. Layton, CFA in 2015 to provide personalized financial planning and fiduciary investment management services to select clients. Our investment process blends the foundations of Modern Portfolio Theory with the latest research in the field of behavioral finance. We specialize in asset allocation and investment due diligence to help provide our clients with investment strategies personalized to match their specific goals and risk comfort zone.