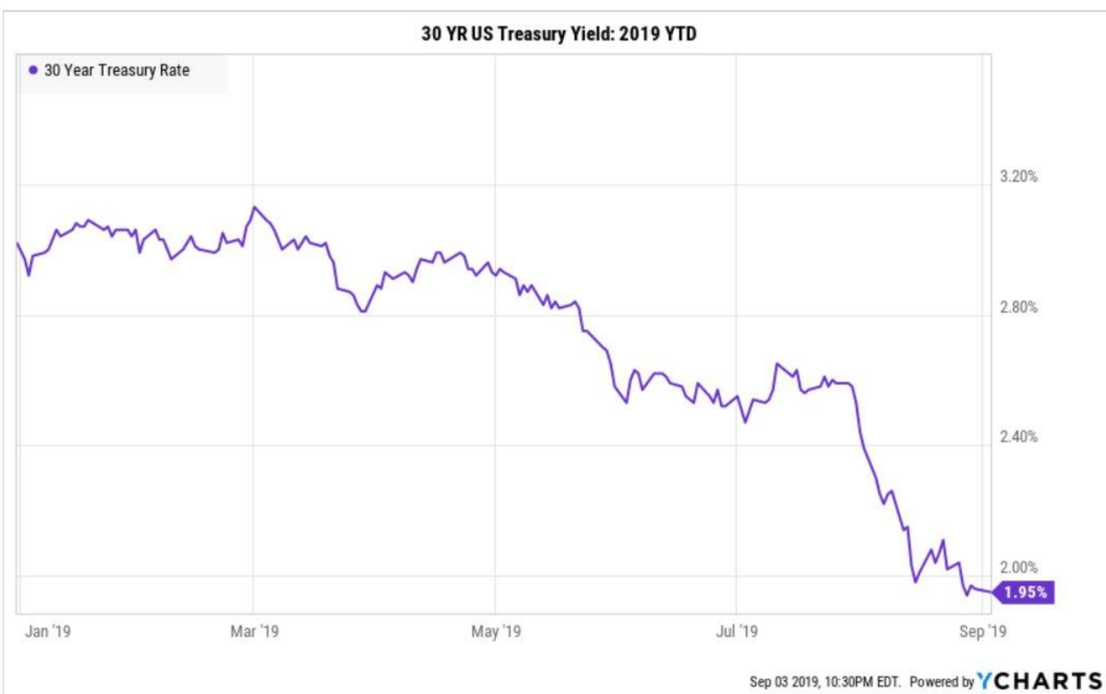
Market Commentary: Election Year Positioning

September 2019

Trade wars and volatility definitely captured the lion's share of attention for the month of August as the wheels pretty much fell off US - China trade negotiations. For all the angst, we sit roughly 3.2% below all-time highs for the S&P 500 as of the end of August after a 1.7% decline for the month.

One market that did move dramatically though was fixed income. Thirty year treasury interest rates dropped below 2% for the first time, hitting all-time lows due to recession concerns associated with trade worries, among other factors. Long term rates dropped roughly 20% from 2.5% in August—a huge move.



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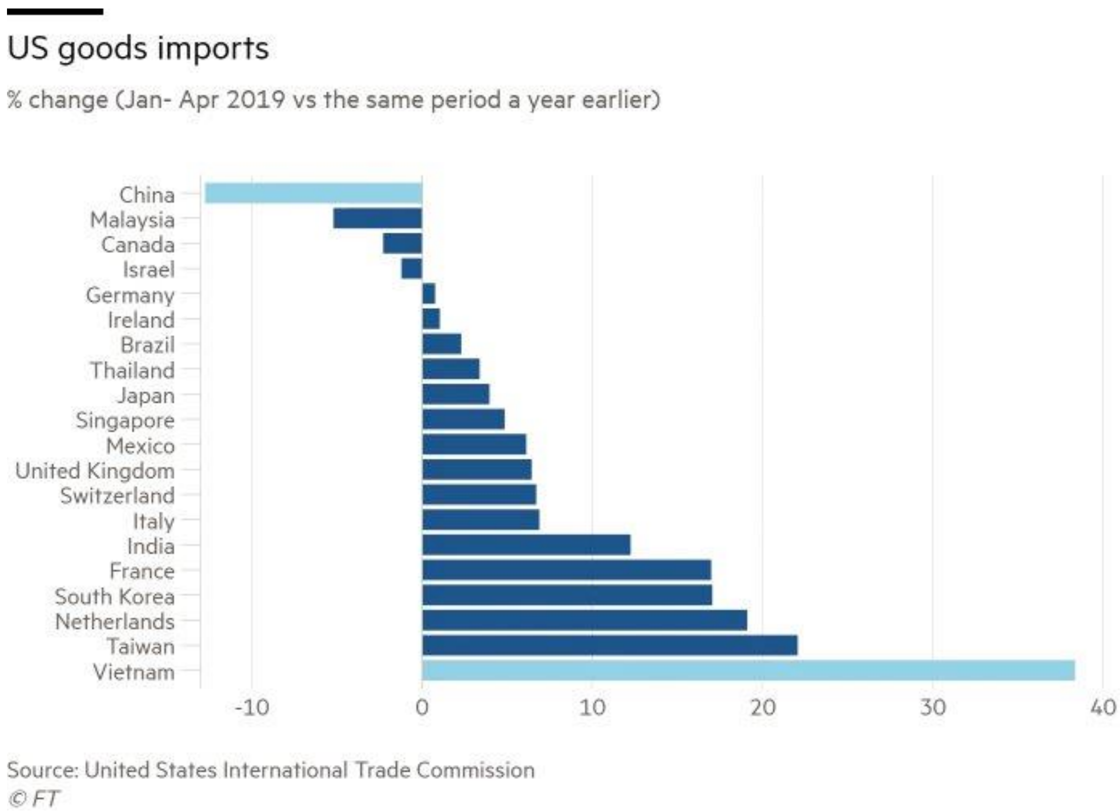
Last month [FAM - 2019 July Market Commentary] we discussed the direct effect of tariffs on Fountainhead as an example of how tariffs work through the system. Lower interest rates assist in counteracting those tariffs, albeit in an indirect way. For example, a segment of our farmers have not coincidentally been negatively affected by the trade war. Our government has decided to subsidize these farmers. It is now cheaper for the government to float these subsidies. More broadly speaking, lower rates reduce a material cost for industry which helps counteract a business slowdown. Finally, whether one points to recession indications or lower long term rates, the pressure continues to pile on the Fed to lower short-term rates, which is a positive for the market.

As we approach the end of 2019 there are two risk items on our radar—themes we have voiced in the past that continue to crystalize in our minds. There is also a day that one can peg as a very important date with a large impact on how quickly certain events evolve. That date is the election. The current administration has materially adjusted the approach of the US towards the global community. The trade war is but one example. A second is global policing and policy.

We had discussed in last month's commentary the fact that a British ship was captured by the Iranians in a busy shipping lane primarily dedicated to the transport of oil. We (the US) made clear that this was a British issue motivating Britain to move navy resources to the region. While the world has always had and will continue to have aggressive actors, the calculation of how we perceive it and act upon it has changed. Therefore, there seems to be a window for further aggressive acts that may introduce further volatility to global markets. It seems a good time for bad (or simply aggressive based on one's view) actors to attempt to achieve an initiative that in the past may have been harder to successfully complete due to global pressure (which has in recent history simply been US pressure with further pressure from US friends). Some ongoing events in no particular order:

- Hong Kong Protests
- Russia protests (scarier and less followed)
- Kashmir
- Japan / Korea
- The list does and will increase

Election Day will also dictate how trade talks with China go, as well as how China may affect the election. As we mentioned in our last note, the election is an Achilles heel that we, given our democratic governance, have to contend with, while China does not. (While I truly believe democracy is far and away the best approach for country and citizen alike, it has its negatives!) In the interim, there is a decently large unwind going on with Vietnam one clear early winner with a 36% year-over-year (YoY) increase in exports to the US. Part of the increase seems to be an attempt to game the tariff system, but part is simply a move of manufacturing.



In summary, we expect current market volatility to continue, if not increase, as we get further into the election cycle due the items reviewed in this month's commentary.

<u>IMPORTANT DISCLOSURE</u>

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