June 2019 Monthly Market Update

May Benchmark Returns	MTD	QTD	YTD
EQUITY BENCHMARKS			
Vanguard 500 Index	-6.4%	-2.6%	10.7%
iShares Russell 1000 ETF	-6.3%	-2.6%	10.9%
iShares Russell 1000 Value ETF	-6.4%	-3.2%	8.3%
iShares Russell 1000 Growth ETF	-6.3%	-2.1%	13.5%
iShares Russell 2000 ETF	-7.9%	-4.7%	9.2%
Vanguard REIT	0.1%	0.0%	17.3%
iShares MSCI ACWI ETF	-6.1%	-2.9%	9.2%
Vanguard FTSE Developed Markets ETF	-5.2%	-2.5%	7.8%
Vanguard FTSE Europe ETF	-5.7%	-2.0%	8.7%
Vanguard FTSE Emerging Markets ETF	-6.4%	-4.4%	6.9%
FIXED-INCOME BENCHMARKS			
Vanguard Total Bond Market Index	1.8%	1.9%	4.8%
Vanguard Intermediate-Term Tax-Exempt	1.4%	1.7%	4.3%
iShares TIPS Bond ETF	1.8%	2.0%	5.3%
ICE BofA Merrill Lynch U.S. High Yield Cash Pay Index	-1.3%	0.1%	7.5%
S&P/LSTA Leveraged Loan Index	-0.2%	1.4%	5.5%
ALTERNATIVE BENCHMARKS			
HFRX Global Hedge Fund Index	-0.7%	-0.0%	2.6%
Bloomberg Commodity Index	-3.4%	-3.8%	2.3%
SG Trend Index	-2.5%	1.6%	4.6%
3-Month LIBOR	0.2%	0.5%	1.2%

Concerns around a trade war between the U.S. and China took center stage again last month, as a sudden breakdown in trade talks and escalating tariffs and threats between the two countries rattled markets. U.S. stocks fell more than 6% in May. The risk-averse environment boosted Treasury bond prices and sunk yields—the 10-year Treasury yield dropped from 2.51% to 2.14% by month end. The Treasury curve inverted again during May (10-year yield minus 3-month yield) and remained so for the second half of the month, raising (and reflecting) renewed fears of a recession on the horizon.

This recap is a stark contrast to last month's market update. As a reminder, the first four months of 2019 marked the best start for U.S. stocks in 30 years. Even after May's sharp decline, the S&P 500 was still up over 10% for the year. But it's a good reminder that market headlines are often never as good or bad as they seem. Uncertainty is a constant presence and volatility can return to markets at the drop of a tweet. If you own equities, you need to be prepared to ride through their drops. It's the shorter-term price you pay to earn their higher expected returns over the longer-term.

Foreign equity markets also fell in May. Emerging-market equities dropped a similar amount as U.S. large-cap stocks (the Vanguard FTSE Emerging Markets ETF was down 6.4%). Developed international stocks were down slightly less. Vanguard FTSE Developed Markets ETF lost 5.2%. European equities (Vanguard FTSE Europe ETF) dropped 5.7% in May.

Bond markets held up during the month, providing beneficial diversification relative to stocks in our balanced portfolios. The flight to safety lifted high-quality bond prices, as the U.S. core bond index gained 1.8% in May. More credit-sensitive areas of the fixed-income markets fell modestly: floating-rate loans dipped 0.2% and high-yield bonds dropped 1.3%.

While the Federal Reserve continues to signal a "patient" monetary policy stance, the fed funds futures market is predicting the Fed will cut rates this year. One month ago, the fed futures market was putting

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roughly a 50% probability that the Fed would cut rates at least once this year. By the end of May, the probability had jumped to 98% of at least one cut, and a greater than 80% probability of two or more cuts.

The abrupt U-turn in U.S.-China relations, which goes beyond just trade disputes, as well as new tariff threats against Mexico, Europe, and others, has increased the *shorter-term* risk of a global growth slowdown and a U.S. recession. The financial markets reflected this increased likelihood in May. But this outcome is by no means a certainty. Looking out over the next 12 months, there is still a reasonable "global recovery" scenario, in which we'd expect a reversal of May's performance trends. Over the past 10 years, we have seen the dramatic impact that government and central bank policy, in particular, can have on the financial markets—sometimes changing the market narrative on a dime. These narratives can then become self-fulfilling, feeding on themselves both on the upside and the downside.

We have made minor portfolio tweaks this year and we continue to actively revisit and re-assess our risk exposures and return expectations across a range of shorter-term (12-month) and medium-term (5-10 year) scenarios. As always, there are multiple risk and return trade-offs to consider and balance within the context of each portfolio's overall risk objective. This includes stress-testing our balanced portfolios for a severe recessionary bear market, an event that we think is unfortunately likely within the next five years given the weakness and late stage of the economic cycle coupled with very high valuations for U.S. stocks. We are still in-process with our assessment and will continue to work on it over the coming months to see if and what additional portfolio changes are necessary.

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