MAIN MANAGEMENT, LLC

Q2 2019 MARKET RECAP

JUL 10, 2019

TRADE RESOLUTION STILL PENDING

Following a strong first quarter, Q2 2019 continued the positive momentum in April before posting the first negative month of the year in May and then subsequently rebounding in June. As painful as May felt, it was actually right in line with the historical expected drawdown following a first quarter as strong as the one we had this year. The second quarter saw US equity markets move higher on the whole, driven by easy money, fiscal stimulus, and monetary stimulus. The trade war with China is still very much up in the air but investors are holding out hope for a resolution. An escalation would be unpleasant for all parties involved and we have already seen U.S imports from China decline markedly. Nonetheless, the S&P 500 is up nearly 19% in the first half of the year despite all of this uncertainty. Historically, years that have started this strong have seen flat returns in the second half. There remains potential upside should a trade resolution be reached and the macroeconomic data simply is not as bad as people are fearing.

However, concerns about slowing growth remain with Manufacturing PMI numbers slipping to multi-year lows around the globe. The Q1 GDP reading for the US was a strong 3.1%, 26% faster than the average during this expansion, and brought average real annualized GDP growth to almost 3% for the past 8 quarters. Q2 GDP is expected to decelerate to 1.5-2.0%, which is more in line with the long-term forecasted growth rate. That is to say, it is slower, but still expansionary. The labor market remains tight, with low unemployment and more job openings than unemployed persons. Productivity continues to be strong, with Q1 posting the largest year-over-year gain since Q3 2010. The average productivity gain over the past 4 quarters has been 1.7%, which is 54% above the expansion average of 1.1%. Inflation is still low. The economy appears to be fundamentally sound for the most part but is showing signs of wear around the edges.

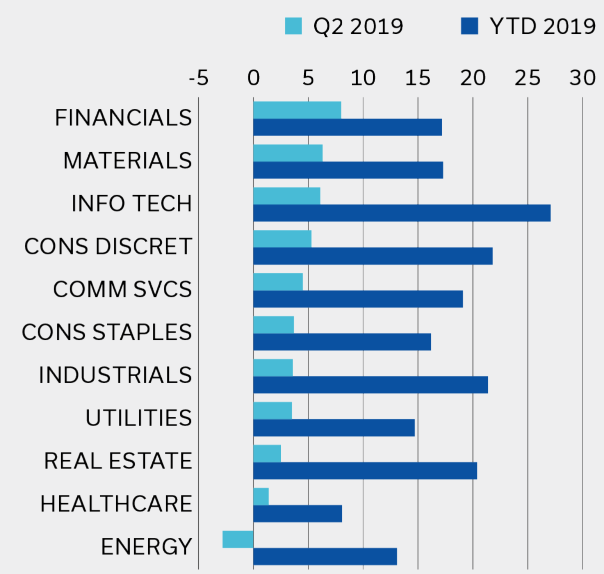
RATE CUTS?

As it was in the first quarter, the Federal Open Market Committee's dovish tone was again one of the bigger developments in Q2. The June meeting continued the dovish trend started in January and March. While the dot plot median remains at 0 cuts for the balance of the year, the markets are pricing in 2 cuts, on average. It's important to remember that as recently as December, the Fed was forecasting 2 rate hikes. The 10 year-3 month Treasury yield spread has been inverted for over a month and continues to garner headlines as a predictor of recession. As was the case when this spread initially inverted back in the first quarter, it is important to remember that inversions are not great recession predictors by themselves. As the curve has been consistently inverted for several weeks now, we note again that the lead time until a recession is typically 55 weeks and that during that time, markets have historically moved higher.

CONTINUED GLOBAL UNCERTAINTY

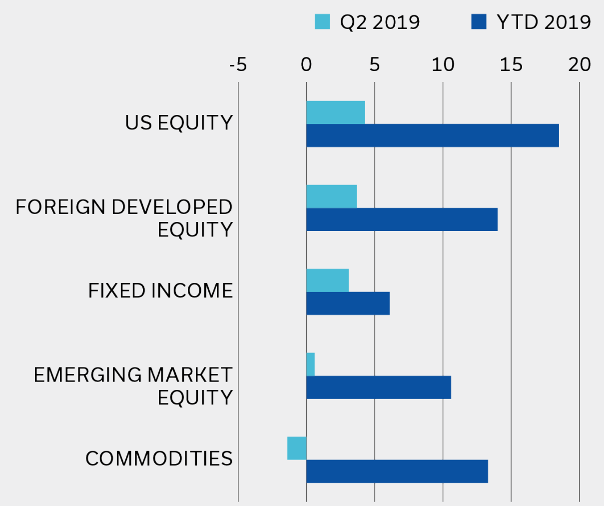
Looking outside the United States, the environment is also

Sector Returns, % return
As of 6/30/19



Source: Morningstar Direct

Asset Class Returns, % return
As of 6/30/19



Source: Morningstar Direct

increasingly uncertain. As economic data has continued to deteriorate, central banks, most notably the ECB, are prepared to take measures to prevent a recession. European GDP is low but positive. Brexit remains localized and appears that it will continue to be. China's stimulus should help things in the second half of the year as it takes hold on the world's second largest economy, and a trade resolution would certainly boost things further. Markets do not like uncertainty and as we said above, it seems as though the worst case scenarios for China are priced in with surprises more likely to be to the upside.

As we move into the back half of 2019, the global economic environment continues to be uncertain. U.S. data is showing signs of slowing but does remain mostly expansionary. With the strong first half in the equity markets, valuations are now slightly above historical levels (P/E of 16.7x current vs 16.2x historical) but are still well below what one would consider over-valued. Outside of the U.S., much hinges on China, a trade settlement with the U.S., and the efficacy of its stimulus. We remain optimistic about seeing positive results which may provide a lift to the global economy later this year.

Sincerely,

Kim David Arthur
CEO and Portfolio Manager

601 California St., Suite 620 | San Francisco, CA 94108 | (415) 217-5800 | info@mainmgt.com | www.mainmgt.com