United Methodist Frontier Foundation
New York • Connecticut

Second Quarter 2018 Investment Highlights

- Overall, the equity market recouped its losses in the aftermath of cross asset volatility routs, trade conflicts, and concerns over slower growth and higher inflation, but was not able to surpass its previous highs in January due to renewed escalation of trade tensions in late June.

- Escalating trade war rhetoric has kept hitting the headlines, but then subsequently followed by details showing less drastic actions, leading investors to "Sell-on-the Rumor and Buy-on the-Fact" as stock markets flip-flop between uptick and downtick. We maintain our view that the odds of a full blown worldwide trade war remain low.

- Compared to Europe, which is mute of expansive fiscal policies, the U.S. is seeing its major growth engines simultaneously at work: solid consumption backed by a strong labor market; robust business investment supported by tax cuts; strong housing markets; and expansionary government spending further fueling domestic demands. Small-cap's relative strength to the market also reflects the strength of domestic demand in the U.S.

- Indicators of volatility for both U.S. equity and foreign exchange rates are also reflecting the calm of the markets, and the fact that trade conflicts have so far spared "Main Street" despite being the major catalysts for Wall Street this year.

- Economic indicators imply that European Union core inflation has remained benign and is expected to increase only gradually as wage growth has been trailing the trend of a diminishing output gap.

- China has become more advanced with managing its financial stability with an establishment of a super financial regulatory body, and unemployment indicators continued to trend lower reflecting China's continuous transition from an old economy built on excessive investment in industrial manufacturing capacities to the new economy driven by innovation and consumption.

- Amid a broad-based correction, Emerging Market equities as a whole saw its worst decline since 2015 in the second quarter and Emerging Market debt also saw its worst first half in history.

- After years of easing, global central banks are on a broad-based wave of tightening actions (albeit at different stages of their cycles); the underlying risks for financial markets are boiling under the combination of uneven economic growth trajectories in various economies and concurrent liquidity tightening.

- The yield curve in both the short end and long end of the U.S. treasury market persisted in its downward trend but has not yet inverted, signaling aging of the current business cycle instead of recession. We continue to anticipate a flattening yield curve as the Fed proceeds with its current rate hike cycle although rising money-market rates have made it harder for the Fed to maintain control over their key policy benchmark.

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Please refer to the full Investment Manager Memo for supporting details.