RAYMOND JAMES

VOLUME 11 | ISSUE 3 | JULY 2019

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Letter from the Chief Investment Officer

Being in the Right Place at the Right Time

Celebrating the 25-year anniversary of the Academy Award-winning movie Forrest Gump, we revisit many of the movie's themes which remain relevant in today's world. Forrest Gump's mother always said that **"Life was like a box of chocolates."** This memorable observation could just as easily be applied to the financial markets, as you never know what volatility-inducing headline you're going to get next.

President Trump's infamous tweets on trade continue to spark serious disputes between the world's most influential superpowers, as a fickle Federal Reserve (Fed), rising recessionary fears, and the upcoming U.S. presidential election top the list of potential domestic risks. Mix in a global economic slowdown, Brexit uncertainty, Italy's budget crisis, escalating tensions with Iran, and the long-running political crisis in Venezuela, and you have the perfect recipe for a volatile market. While most of these headlines serve as daily noise to give investors both sugar highs (and sugar crashes), we still believe that investors must be prudent with their investments and remain committed to their long-term financial plans.

As Forrest reminds us, **"You've got to put the past behind you before you can move on."** That is exactly what we need to do from an economic perspective. With the U.S. economy poised to notch the longest economic expansion in the history of our country in July (121 months), investors can no longer count on tax cuts, quantitative easing, or early-cycle "bounce back" growth to support the market.

Assuming the trade war does not escalate, our Chief Economist, Dr. Scott Brown, believes this expansion will continue as the Fed is likely to cut short-term interest rates not just once, but twice, before the end of the year. Elevated business and consumer confidence, robust employment conditions, and expectations for healthy consumer spending trends should lead to U.S. Gross Domestic Product (GDP) growth of 1.9% for 2019. While risks have risen, the expectation is that the U.S. economy will not slip into recession over the next 12 months, which is critical in developing our outlook for the capital markets for the next year.

The bond market has us echoing Forrest's question, **"What's normal anyways?"** Given historical precedent, the longevity and strength of the economic expansion, combined with record budget deficits, should have led to higher interest rates. However, this has not been the case. In fact, global interest rates have continued to grind lower and the yield curve remains flat/inverted, depending on the maturities you examine. According to Managing Director of Fixed Income Research, Doug Drabik, central bank bond purchases (particularly in Europe and Japan) have led to more than $13 trillion in negative-yielding sovereign debt. Demographics are also playing a part, as retiring investors transition from risk assets to income-generating securities.

U.S. Treasuries have traditionally been the "safe haven" destination for much of the fixed income world. On a comparative basis, would you prefer a 10-year U.S. Treasury bond yielding 2.01% or a 10-year German bund yielding -0.33%[1]? The answer is obvious, and the excess demand for U.S. Treasuries will likely keep domestic interest rates lower for longer. The likelihood that the Fed will cut rates in order to preserve the economic expansion, combined with unattractive interest rates overseas, has led us to reduce our year-end target for the 10-year Treasury yield to 2.4% (from 2.75%). From a sector perspective, we still prefer emerging market bonds and investment-grade bonds over high yield.

"Run, Forrest, run" could just as easily be "Run, equities, run!" However, to move higher, the equity markets need to shed the "braces" of negativity surrounding trade fears and recessionary concerns. If this does occur, we believe record earnings should continue to propel the equity markets higher. We reiterate our S&P 500 year-end target of 2946. However, should the trade war with China escalate, Managing Director of Equity Portfolio & Technical Strategy, Mike Gibbs, estimates that S&P 500 earnings will fall by ~4%, leading to more uncertainty and downside potential

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[1] Source: Bloomburg as of 06/26/2019

for equities. From a sector standpoint, we prefer Technology, Health Care, Consumer Discretionary, and Communication Services. In addition, assuming the Fed embarks upon an easing cycle, we favor cyclicals over defensives, and growth over value-oriented strategies. We maintain our preference for the U.S. over other developed-market equities such as Europe and Japan. If there is any progress on the trade front between the U.S. and China, emerging markets should stand to benefit.

Unlike Forrest and Jenny, oil prices and the U.S. dollar are not like **"peas and carrots."** In fact, there is typically a negative correlation between commodities and the dollar. Tailwinds that previously supported the dollar continue to fade, particularly as the Fed appears set to cut interest rates before year end. As a result, we forecast the dollar weakening slightly to $1.15 versus the euro before year end. A weaker dollar, fading global oil inventories, and the new International Maritime Organization (IMO) standards set to take effect in January 2020 should support oil prices. Our forecast is that oil will bounce back to $70/barrel before the end of the year.[**]

Forrest Gump is an inspiration to many, as he overcomes significant tribulations in his life through both hard work and good fortune. Admittedly, you need both as a successful investor! He had a way of being in the right place at the right time, as he ended up being part of many of the most iconic events of the twentieth century. That is exactly what we aim to do with our investment strategy views: place your portfolio in the best position to succeed over the long term.

Bubba remarks that **"shrimp is the fruit of the sea,"** as he lists the multitude of cooking methods, pairings, and seasonings that make shrimp so versatile. The same could be said of your portfolio, as there are numerous ways to structure your investments to meet your unique goals and objectives. As volatility is likely to increase, and the return environment becomes more challenging, we encourage you to review your portfolio with your advisor.

Lawrence V. Adam, III, CFA, CIMA®, CFP®
Chief Investment Officer, Private Client Group

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Entrenched: Trade Warfare

Ed Mills, *Managing Director, Washington Policy Analyst,* Equity Research

Trade tensions between the United States and China have been a hallmark of President Trump's time in office and a major market overhang that threatens to initiate a decoupling of the world's largest economies, disrupting supply chains, and potentially hitting company earnings in the process. It has been over two years since the initial face-to-face meeting between President Trump and China's President Xi at Mar-a-Lago, at which time a 100-day plan to address broad economic concerns was put into action.

ARE WE IN A TRADE OR TECH WAR WITH CHINA?

Initial optimism in early 2017 quickly faded as the two sides could not come to an agreement on key market access, intellectual property protection, and technology transfer requirements that remain at the center of talks. The back-and-forth nature of these negotiations is tied to a reality that is gaining greater appreciation: the talks are less about overall trade imbalances, and more about safeguarding future U.S. economic, technological, and military interests. In short, we believe the Trump administration views this as a battle for supremacy. We have noticed more attention on the day-to-day or tweet-by-tweet coverage of the fight (rather than a conversation about why we are in a conflict), the objectives of the Trump administration, and whether China could ever agree to these potential changes. In this article, we will attempt to outline some of the key aspects of this trade war.

"In short, we believe the Trump administration views this as a battle for supremacy."

GAME CHANGER: U.S. TECH CENTRAL TO NATIONAL SECURITY

A government-wide effort to strengthen the defense of U.S. "foundational" technologies began in 2017 under the Trump administration to preserve U.S. leadership in tech that will have future military applications such as advanced robotics, artificial intelligence, and quantum computing. The new approach can be thought of as threefold: enhanced domestic foreign investment reviews, commercial controls on tech exports, and ramped-up criminal prosecutions against the theft of corporate secrets. All three take direct aim at China's efforts to close the gap in technological know-how and begin to challenge the established U.S. tech industry for global superiority. The widely-publicized "Made in China 2025" initiative laid out China's ruling party's plans in this area, establishing domestic and international market share targets for China's firms competing with advanced U.S. tech by 2025 and beyond. In effect, the Trump administration has moved to set defenses against access to U.S. tech that is aimed at directly threatening U.S. dominance in the tech space by a foreign competitor, especially if it could have a military application. More

"The China trade fight is arguably the most popular policy position of the Trump presidency."

broadly, China hardliners in the Trump administration view competition in the tech space as the new ideological frontier to determine the values of the emerging tech landscape – a modern day "Cold War" scenario.

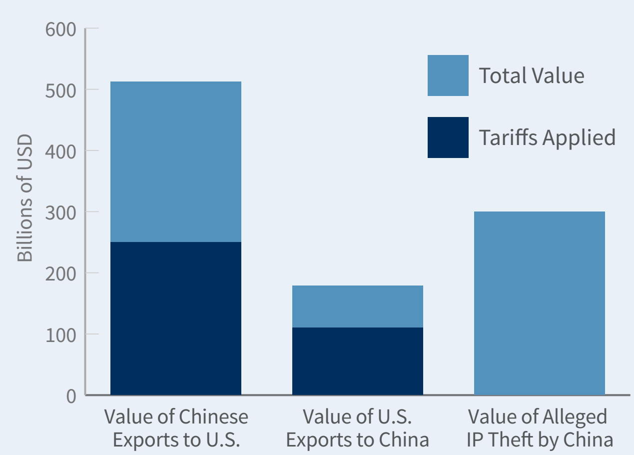
The more direct challenge to China's behavior came in August 2017 with the administration's so-called "Section 301" investigation into "any of China's laws, policies, practices, or actions that may be unreasonable or discriminatory and that may be harming American intellectual property rights, innovation, or technology development." The investigation led to the tariff imposed on $200 billion of Chinese imports directly targeting China's advanced manufacturing industry central to its "Made in China 2025" development goals. The investigation found that China utilizes joint venture requirements (U.S. firms need a Chinese partner to conduct business in China), forced tech transfers (business licenses are only granted to firms who agree to transfer critical intellectual property to their Chinese partner), foreign direct investment (Chinese companies invest in U.S. companies to gain access to new technologies), and unauthorized network intrusions (cyber espionage) to cause direct harm to U.S. industry. U.S. companies seeking to enter China's markets are frequently required to partner with a domestic Chinese partner or detail critical commercial information to government agencies in order to gain licensing approval. These requirements provide crucial access to U.S. tech that can be replicated by Chinese competitors, according to the investigation. The report further details cyber espionage and hacking efforts targeting U.S. companies for theft of trade secrets. A November 2018 follow-up report concluded that China had "failed to make structural changes" and to "adopt U.S. recommendations for reforms" to adequately address U.S. concerns. The tech battle remains a pivotal issue in ongoing talks, and is trending toward escalation for the remainder of 2019.

STAGE SET FOR SIGNIFICANT ECONOMIC RESTRICTIONS TARGETING CHINA

One weapon the Trump administration has floated throughout the trade negotiations is the activation of the International Emergency Economic Powers Act (IEEPA), a set of national security powers that allows for broad restrictions of certain commerce that is deemed a threat to the U.S. In May, President Trump formally invoked IEEPA to secure emerging 5G networks by banning the acquisition of certain foreign-produced equipment that could allow adversaries to exploit vulnerabilities. Although the order does not name China or Chinese companies directly, it alludes to industrial espionage-type threats that the U.S. has described to allies in its push to restrict the use of Chinese 5G equipment around the world. Under the order, the Department of Commerce has until mid-October to establish regulations on specific restrictions. The activation of IEEPA is yet another warning shot at China showing that we could see this battle move from company-to-company restriction (like Huawei) toward a technology-to-technology restriction in the coming months unless negotiators are able to reach agreement on significant changes to China's economic practices.

Tariff Man*

President Trump and his administration have continued to hold a hard line on China, who they accuse of unfair trade practices, non-compliance with the policies of the World Trade Organization, and pervasive theft of American intellectual property (IP). The U.S. Trade Representative has valued the theft of American IP at $300 billion, which has served as its substantiation for tariffs on $250 billion worth of Chinese imports.



Source: U.S. Trade Representative, White House

*Trump's tweet from December 4, 2018: "... I am a Tariff Man. When people or countries come in to raid the great wealth of our Nation, I want them to pay for the privilege of doing so. It will always be the best way to max out our economic power. We are right now taking in $billions in Tariffs. MAKE AMERICA RICH AGAIN."

The Reelection of Least Resistance

Amidst many domestic challenges and political opposition from a divided congress, the Trump administration's hard line on China might be its path of least resistance to reelection.

> "Fighting China in a trade war is easier for Trump to defend than a weak deal, increasing the likelihood that this fight lasts beyond the 2020 election."

PRESIDENTIAL POLITICS AND CLASH OF GOVERNANCE SYSTEMS FURTHER COMPLICATE PATH TO A DEAL

The China trade fight is arguably the most popular policy position of the Trump presidency. Members of Congress may question the style of the negotiations, but few are willing to publicly question the substance of the fight – especially on strengthening protections for U.S. tech. Fighting China in a trade war is easier for Trump to defend than a weak deal, increasing the likelihood that this fight lasts beyond the 2020 election. We believe one of the biggest threats to President Trump's reelection would be a market sell-off or weakening economy. Either could cause the president to soften his stance toward China, but that is not a given and could embolden China to hold out.

Politically, securing a deal in the short term presents advantages for both sides, but opportunity for miscalculation is heightened in the long term. Reaching a deal would provide a market boost in the U.S. and would play well for China's Xi for preserving (for the time being) the relationship with China's largest market. In the longer term, the incentives do not align as well. Xi Jinping's term as China's leader will continue well beyond Trump, but the U.S. may experience a change in administration with the 2020 election. From that perspective, the trade fight may be prolonged if China's leaders decide to "weather the storm" for the time being. A less comprehensive deal or continuously stalled negotiations may result in tariff escalation or other significant economic restrictions. Escalation points could come right in the heat of the 2020 presidential campaign, which can damage Trump's economic message or provide a political incentive to once again increase pressure on China. As we noted earlier, we expect trade relations with China to remain a key theme of the Trump presidency, even in the event of a deal struck sometime in 2019.

KEY TAKEAWAYS:

- U.S./China trade tensions have been a hallmark of President Trump's time in office and a major market overhang that threatens to initiate a decoupling of the world's largest economies, disrupting supply chains, and potentially hitting company earnings in the process.
- China hardliners in the Trump administration view competition in the tech space as the new ideological frontier to determine the values of the emerging tech landscape – a modern day "Cold War" scenario.
- The China trade fight is arguably the most popular policy position of the Trump presidency. We believe one of the biggest threats to President Trump's reelection would be a market sell-off or weakening economy. Either could cause the president to soften his stance toward China, but that is not a given and could embolden China to hold out.
- Politically, securing a deal in the short term presents advantages for both sides, but opportunity for miscalculation is heightened in the long term. Reaching a deal would provide a market boost in the U.S. and would play well for China's Xi for preserving (for the time being) the relationship with China's largest market.

Collateral Consequences: The Economics of Tariffs

Scott J. Brown, Ph.D., *Chief Economist ,* Raymond James

Many of us tend to think of globalization and trade with China as recent phenomena, but that's far from true. Ancient empires interacted with each other, trading spices, silver, and gold. The Silk Road, expanded by the Han dynasty in 114 BCE, brought Chinese goods to India, Persia, Greece, and Rome. By the first century CE, the 1% of Rome and Carthage were dressed in silk.

A Tang shipwreck discovered off the coast of Indonesia in 1998, dated to around 825 CE, contained some 60,000 items, mostly Chinese ceramics. The young United States traded with China after it lost its only source for tea (England) following the Revolutionary War. Trade brought an exchange of goods and cultures, but varied over the centuries as empires came and went.

In studying economics, one learns early about the concept of comparative advantage and the benefits of trade. There are winners and losers (as trade with another country picks up), but both benefit overall.

THE MAKING OF THE MODERN DRAGON

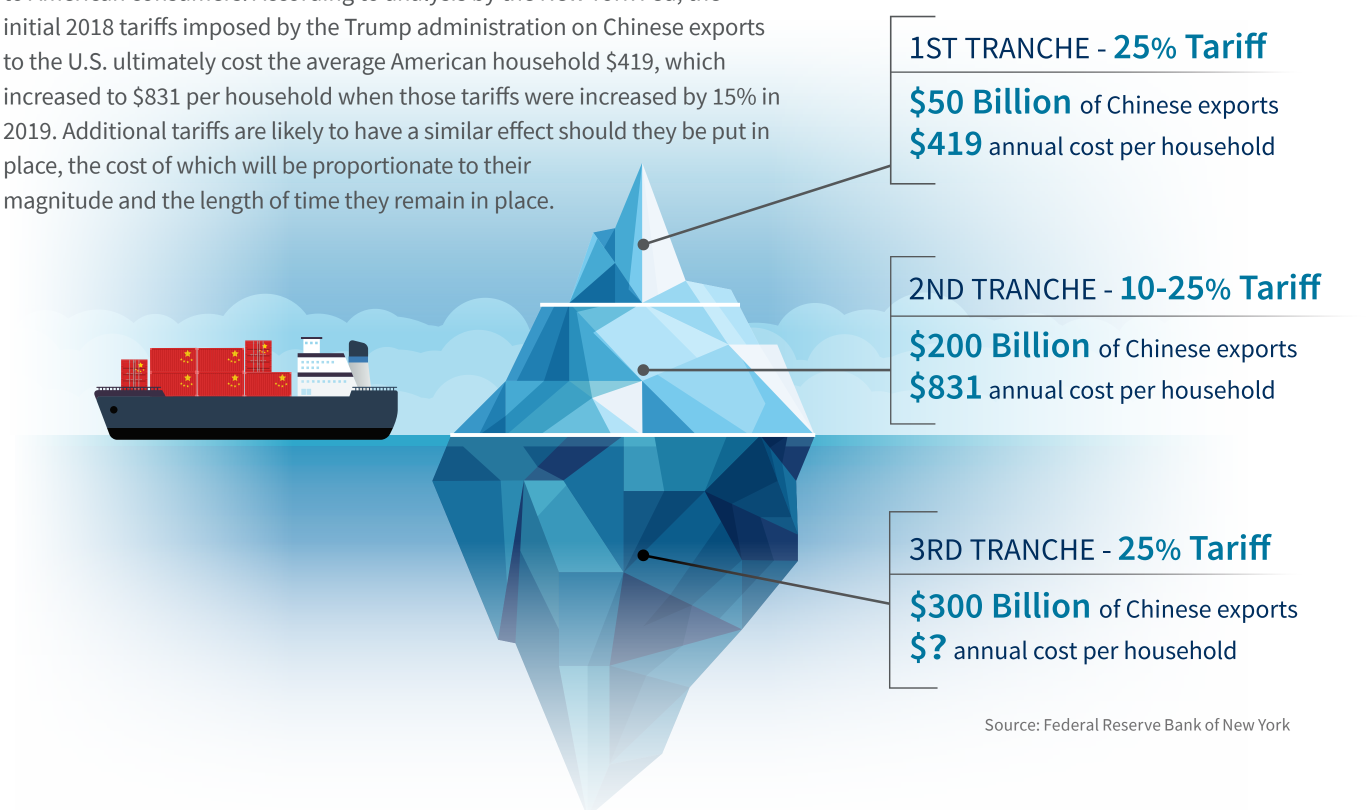
After the Maoist Revolution, China was closed off from the rest of the world until the 1970s, but began to open up in the early 1980s, signing a number of regional trade agreements. The country joined the World Trade Organization (WTO) in late 2001. Expansion of port facilities in China as well as in Los Angeles and Long Beach, California, together with a new, larger class of container vessels, led to a rapid increase in exports to the U.S., although some of this was taking share from other Asian nations.

Although the U.S. refrained from formally classifying China as a currency manipulator, the country was clearly keeping its currency weak against the U.S. dollar in the early 2000s. To do this, China had to amass large amounts of dollar-denominated assets, mostly U.S. Treasury and mortgage-backed securities. In fact, Chinese purchases of U.S. mortgage debt helped to keep mortgage rates low throughout the decade, partly contributing to the housing bubble. China stepped away from the U.S. mortgage market after Fannie Mae and Freddie Mac were placed in conservatorship, leaving the Federal Reserve (Fed) to take up the slack.

The rapid growth in trade with China had a negative impact on U.S. manufacturing employment. In the 1980s, the rule of thumb was that the U.S. would lose one out of ten manufacturing jobs each year, but that lost job would be replaced by a new manufacturing job. Over time, the U.S. shed low-productivity jobs and replaced them with high-productivity jobs, keeping the level of factory employment roughly constant over time even as output grew exponentially. Trade with China ended that, but it's estimated that about half of the manufacturing jobs lost since 2000 were due to technology (mostly robotics). Job losses were devastating for families and communities. As a country, we failed to ease that transition.

What Lies Below

Much as the tip of an iceberg often conceals its deceivingly large size, the impact of past, present, and future tariffs are likely to pose significant costs to American consumers. According to analysis by the New York Fed, the initial 2018 tariffs imposed by the Trump administration on Chinese exports to the U.S. ultimately cost the average American household $419, which increased to $831 per household when those tariffs were increased by 15% in 2019. Additional tariffs are likely to have a similar effect should they be put in place, the cost of which will be proportionate to their magnitude and the length of time they remain in place.



Source: Federal Reserve Bank of New York

A DEFICIT OF UNDERSTANDING

China's foreign trade is not out of line with the rest of the world. The country imports raw materials and exports intermediate and finished goods. Its trade surplus is about 1% of its GDP. The U.S. trade deficit is also manageable, currently about 2.0-2.5% of GDP (it rose to over 6% of GDP in 2005). The reason the U.S. runs a trade deficit is that we consume more than we produce, or equivalently, we don't save enough. Economists think it is foolish to focus on the bilateral trade deficit. After all, I have a significant trade deficit with my grocery store. I buy more from them than they buy from me.

A trading partner's bad behavior can be addressed through the WTO or through coordinated international pressure (if other countries have similar complaints, as they do with technology transfers and intellectual property). Applying tariffs hurts the exporting country, but also damages the economy of the importing country.

A tariff is a tax, but one paid by U.S. consumers and businesses, not by China. Tariffs raise costs, disrupt supply chains, invite retaliation in the form of increased tariffs against U.S. exports, and dampen business fixed investment.

> "There is growing evidence that tariffs are having a negative impact on U.S. economic growth, but to date, they appear unlikely, by themselves, to push the U.S. economy into a recession."

RATCHETING UP TRADE TENSIONS

Tariffs on Chinese goods can be separated broadly into three rounds. The first was a 25% tariff on $50 billion, mostly intermediate industrial inputs and capital equipment. The second was a 10% tariff on an additional $200 billion in Chinese goods, including intermediate goods, such as computer and auto parts, and consumer goods. This tariff was raised to 25% on May 10. The third is a potential 25% tariff on the remaining $300 billion or so in Chinese goods, mostly consumer items.

A U.S. importer need not pay a tariff if there is an alternative, but supply chains are complicated and it takes time to make alternative arrangements. U.S. trade with Vietnam is now rising rapidly.

> “While there is still hope that a trade deal with China can be reached, the worldwide rise of protectionism is a discouraging development as we look ahead to the next decade or so.”

However, the one thing that production in China gives you is scale – and in that, there are no easy offsets. None of this means that production will return to the U.S.

FOCUSING ON THE FALLOUT

The Federal Reserve Bank of New York estimates the 2018 tariffs imposed an annual cost of $419 for a typical household. The May 10 escalation of tariffs imposed an additional annual cost of $831. Together, that amounts to over 2% of average household income. The impact will fall harder on lower-income households, and the damage will increase substantially if the third round of tariffs is imposed. Douglas Irwin, a trade economist at Dartmouth, estimates an average tariff of 3% on Chinese goods before 2018. Last year's tariffs raised that to 12%, and the May 10 escalation brought it to 18%. If Trump imposes a 25% tariff on the remaining $300 billion in Chinese goods, the average tariff will be 29%.

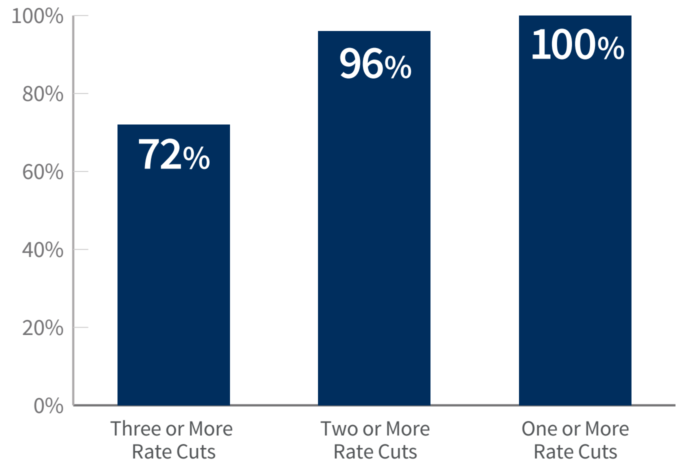
There is growing evidence that tariffs are having a negative impact on U.S. economic growth, but to date, they appear unlikely, by themselves, to push the U.S. economy into a recession. The potential third round of tariffs would have a greater impact.

Some Fed officials may fear the inflationary implications of tariffs. However, that impact would be transitory. The bigger concern should be the drag on growth. Hence, the Fed could lower short-term interest rates by the end of the year. Such an outcome is already anticipated in the federal funds futures market, which is pricing in a 100% chance of one or more rate cuts by the end of this year.

Following two world wars, the countries of Europe felt that war could be prevented by reducing tariffs and other trade barriers. The General Agreement on Tariffs and Trade eventually morphed into the WTO. We had 70 years of peace and cooperation. While there is still hope that a trade deal with China can be reached, the worldwide rise of protectionism is a discouraging development as we look ahead to the next decade or so.

Hike, Hike, Cut

The probability of one or more rate cuts in 2019 by the Federal Reserve has risen dramatically



Source: Bloomberg as of 6/20/19

KEY TAKEAWAYS:

- Tariffs raise costs, disrupt supply chains, invite retaliation in the form of increased tariffs against U.S. exports, and dampen business fixed investment.
- There is growing evidence that tariffs are having a negative impact on U.S. economic growth, but to date, they appear unlikely, by themselves, to push the U.S. economy into a recession. The potential third round of tariffs would have a greater impact.
- The Fed could lower short-term interest rates by the end of the year. Such an outcome is already anticipated in the federal funds futures market, which is pricing in a 100% chance of one or more rate cuts by the end of this year.

Caught in the Crossfire: Market Momentum

J. Michael Gibbs, *Managing Director,* Equity Portfolio & Technical Strategy
Joey Madere, CFA, *Senior Portfolio Analyst,* Equity Portfolio & Technical Strategy

The S&P 500 rose 26% from its December lows by the end of April, with positive trade negotiation developments, a pivot to a neutral stance by the Federal Reserve (Fed), better economic readings, and lower interest rates restoring investor confidence. However, a fallout between the U.S. and China rekindled trade tensions, triggering a 7.65% pullback in equities in May. The S&P 500 recovered, rallying to a new all-time high on a dovish Fed message at the June meeting and news that Trump and Xi plan to meet at the G20.

U.S./CHINA TRADE TENSIONS RE-ESCALATE

Since the May 5 tweet by President Trump, the U.S. has increased tariffs on $200 billion worth of Chinese goods to 25% (from 10% previously) and threatened to place another 25% in tariffs on the remaining $300 billion worth of Chinese exports to the U.S. Additionally, the dispute has escalated to the use of non-tariff barriers (i.e., U.S. ban on Huawei equipment). Heightened trade tensions come amidst a global backdrop that has softened dramatically over the past 12 months, particularly on the manufacturing side of the economy. While the U.S. economy has held up much better than many other places in the world, it too is experiencing softening manufacturing trends. In response, central banks around the world have shifted to a more dovish tone, talking up monetary policy support if the economic outlook continues to deteriorate. Trade conflicts are top of mind for central bankers and investors alike, and all will be monitoring developments at the G20 meeting in Japan where Presidents Trump and Xi are set to meet. Regarding U.S./ China trade, although both sides appear entrenched, our base case remains that cooler heads will prevail at some point, and something will eventually get done. The last meeting between the two presidents (in December 2018) led to a three-month delay on a tariff hike, and the current state of talks makes a similar result the most likely outcome (according to Washington Policy Analyst Ed Mills). We believe the market in general is trading as if the next tranche of tariffs gets delayed, and this is our view of what will likely transpire. That being said, an escalation in tensions would likely be the catalyst for a market pullback in the short term.

> "From a global perspective, the U.S. equity market has held up better than most areas around the world."

FUNDAMENTAL OUTLOOK

S&P 500 sales growth is expected to reach the 5% level for 2019. Earnings growth expectations of nearly 4% are below the long-term average of ~6%, however the moderating trend is not alarming after 20% growth in 2018. Rising wages, tariffs, and slowing economic growth are applying pressure to margins which have declined by

Trading Tweets

As shown by the chart below, the U.S. stock market (as measured by the S&P 500) has reacted significantly at times to President Trump's tariff announcements via Twitter.

Source: Bloomberg

~6% since tariffs went into effect in September 2018. Lower margin estimates pushed consensus on S&P 500 2019 earnings down to $166.77 and near the $166 level we have maintained for months.

The outcome of trade negotiations will impact the next directional move for earnings estimates. Should the trade battle result in 25% tariffs on all trade between the U.S. and China, our estimate declines to $163 (we apply a 4% hit over 12 months pro-rated for six months left in 2019). On the flip side, positive trade resolution (and improving economic and fundamental momentum) will likely allow estimates to move higher, possibly reaching the $169 incorporated in our bull case scenario.

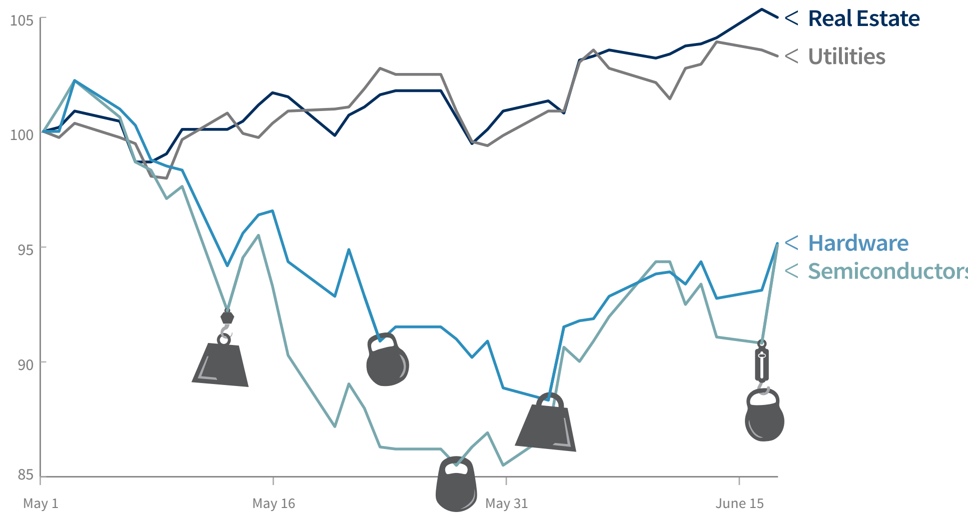
The current S&P 500 P/E of 17.5x is not unreasonable, given low inflation and interest rates, as well as the dovish message from the Fed. However, with the U.S./China trade deal unknown (as of this writing on 6/24), it may not adequately discount the risk either. Our base case year-end S&P 500 expectation remains 2946 (17.75x $166 EPS) for now. It is our belief that the two sides will do enough to soothe investors over the path of negotiations; and with the Fed likely to lower rates, a case can be made for a higher valuation target.

In our bear case scenario, we see an S&P 500 level in the mid 2400s (15x $163) if the trade battle lingers and higher tariffs transpire, putting downward pressure on economic growth and earnings trends (with Fed cuts providing support). The 15x P/E multiple used is in

Source: Raymond James Equity Portfolio & Technical Strategy

Tariff Sensitivity

Some market sectors have proven to be more sensitive to tariffs and trade tensions than others. Due to their significant exposure to trade, semiconductors and computer hardware have fared poorly since the beginning of May. On the other hand, Real Estate and Utilities have remained rather insulated due to their defensive, U.S.-centric business models.



Source: Bloomberg; 100 = May 1 Value

line with the valuation seen at market lows over the past five years. We place a low probability on that outcome, however the risk is still there for now. In our bull case scenario of 3211 (19x $169), a trade deal must transpire and tariffs must be eliminated on both sides. This would boost sentiment, economic momentum, and earnings growth. The 19x P/E assumption is in line with the market's peak trailing 12-month P/E last September, as well as the historical median when inflation is in the 2-2.25% range. Given softening manufacturing trends and an increasing possibility for lingering trade issues, we also place a low probability on this outcome for now.

PORTFOLIO POSITIONING

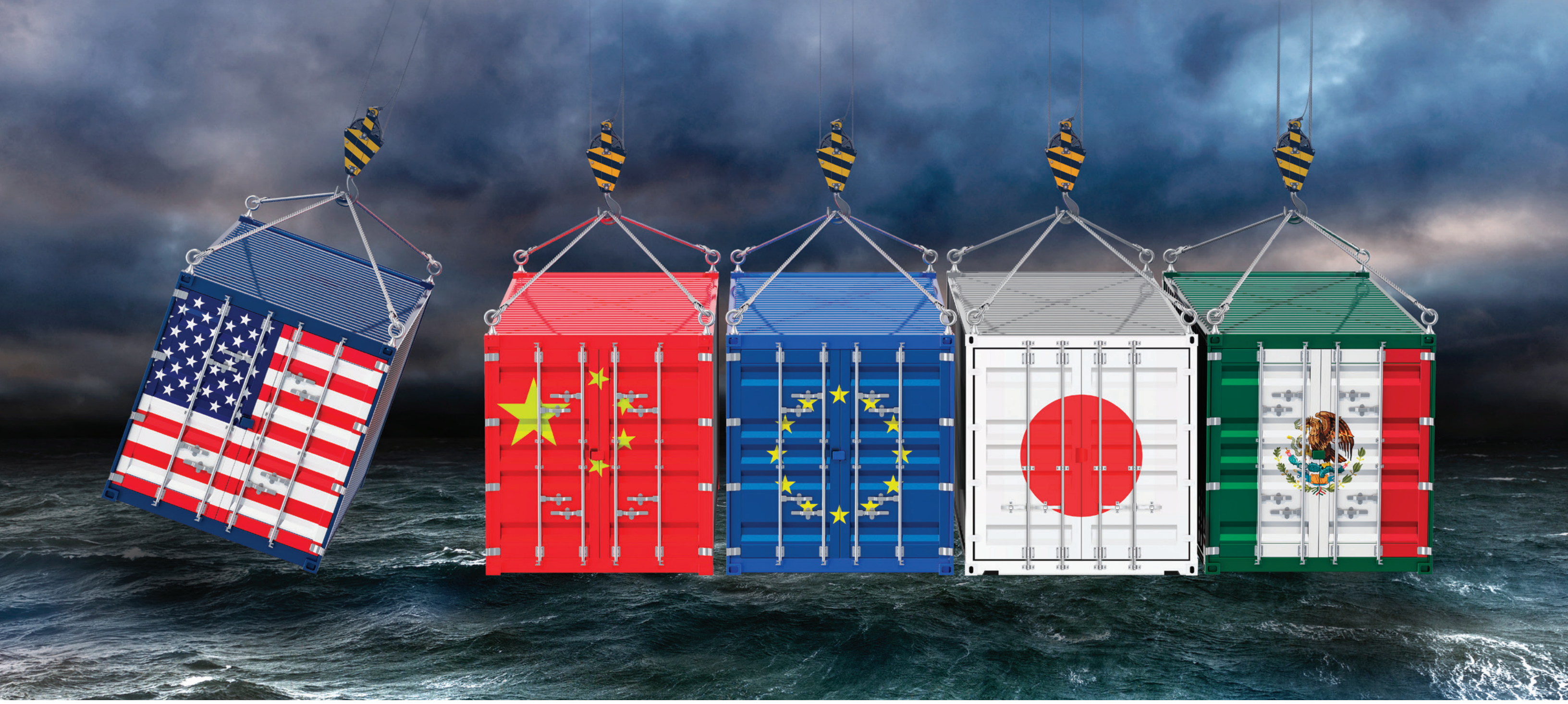
From a global perspective, the U.S. equity market has held up better than most areas around the world (and is also exhibiting better fundamentals). Relative strength for the U.S. (vs. the world) broke out to new highs through the volatility. Therefore, we favor the U.S. over other regions, with a bias toward large-cap growth companies. Next favored are emerging markets given the Fed's dovish message, which may cause weakness in the U.S. dollar.

SECTOR ANALYSIS

Some market sectors have proven to be more sensitive to tariffs and trade tensions than others. Semiconductors and hardware areas of the Technology sector, Materials, the multi-line retail area (of Consumer Discretionary), and specific transportation subsectors (of Industrials), stand out as several groups most influenced by trade negotiations with China. On the flip side, companies with more U.S.-centric business models, along with defensive sectors such as Utilities and Real Estate are benefiting from lower rates and have performed best since early May. At the subsector level, there can be significant deviations between global exposure from one stock to the next, and this is important to consider when positioning your portfolios (based on your risk tolerance) in the current environment. We favor companies with more U.S. revenues since trade is unlikely to go away anytime soon with President Trump making it a campaign topic.

KEY TAKEAWAYS:

- Regarding China/U.S., it is our belief that the two sides will do enough to soothe equity markets over the path of trade negotiations. However, with a belief that a "deal" may be challenging to reach in the near term, our base case year-end S&P 500 expectation remains 2946 (17.75x $166 EPS) for now.
- From a global perspective, the U.S. equity market has held up better than most areas around the world (and is also exhibiting better fundamentals). Relative strength for the U.S. (vs. the world) broke out to new highs through the volatility. We continue to favor U.S. equities (over non-U.S.) with a bias toward large-cap growth. Emerging markets stand to benefit as the U.S. dollar is likely to weaken if the Fed follows through with rate cuts.
- Additionally, we favor companies with more U.S. revenues (since trade is unlikely to go away anytime soon with President Trump making it a campaign topic).



Beyond Borders and Bilateralism: The Import of Trade

Chris Bailey, *European Strategist,* Raymond James Investment Services Ltd.*

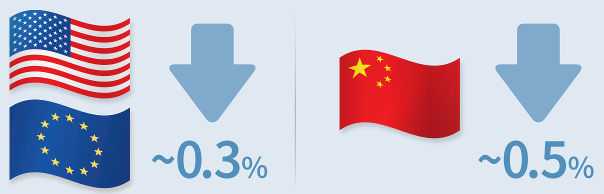
There is no word more dangerous (in finance) than 'extrapolation' and anyone but the most neophyte of investors has grown up with a backdrop of progressively liberal global trade rules. The General Agreement on Tariffs and Trades (GATT) in 1947 led to the creation of the World Trade Organization (WTO) in 1995. The WTO, which boasts a membership of 164 countries, may now preside over services and intellectual property, as well as more traditional manufactured goods, but new challenges have arisen in recent quarters. The threat of trade wars typically tops any investor's list of current global risks.

COOPERATION IS CRUCIAL

Any fledgling economics student knows economic growth is made up of consumption, investment, government spending, and a net trade (exports minus imports) contribution. Trade angst that leads to less interaction between economies, in most circumstances, leads statically to lower economic growth as supply chains are interrupted and more expensive alternatives are less cost-efficient. A few studies in recent months have attempted to quantify the impact of new tariff actions from countries such as the U.S. and China. These studies have suggested an economic growth level reduction of around 0.3% in 2020 for both the U.S. and the pan-European economy compared to the previous status quo of no new tariff implementation. The suggested negative impact on Chinese economic growth levels is a little higher at over 0.5%, but in the wider scheme of things, this is a nudging down of economic growth rates, not an immediate precursor to economic recession.

> "We must become more comfortable with probability and uncertainty."
> – Nate Silver

Impact of Tariffs on Economic Growth

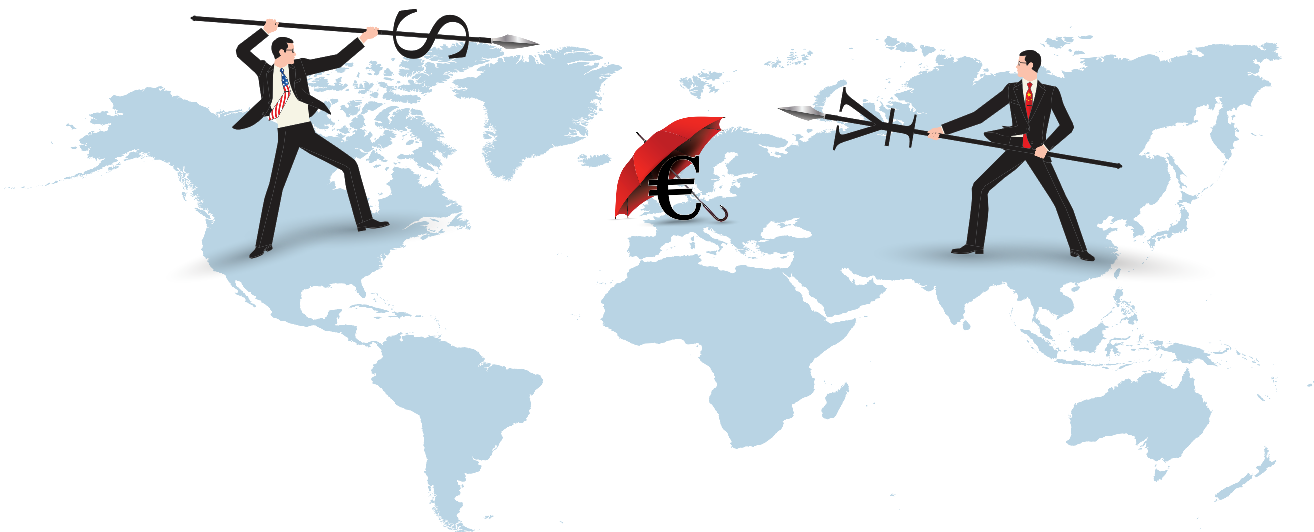


Source: Bloomberg

*An affiliate of Raymond James & Associates, Inc., and Raymond James Financial Services, Inc.

The Art of the Trade War

In the protracted trade war between the U.S. and China, each has its own sources of ammunition. On the one hand, the U.S. has exceptional leverage over China with the tariffs it can apply on China's significantly higher exports relative to the U.S. On the other hand, China can counter such measures with fiscal stimulus and the depreciation of its currency. Suffice to say, each side can dig in. Meanwhile, the EU, Japan, and other developed markets have been caught in the crossfire.



Trade policy, however, tends not to have quantifiable, static effects on its own. The lengthy period of progressive trade liberalization following World War II led to an increasingly complex and inter-related global economy which benefited from the application of the law of comparative advantage. And as is the nature of economic systems leaning towards capitalism, the incentives and informational insights created from the positive benefits of trade create new and dynamic benefits that allow economic growth to advance further. Unfortunately, any regression in such trends threatens a negative reversal in this mirror image of trade. And the transmission mechanism for this? Retaliatory tariffs.

> "Trade policy, however, tends not to have quantifiable, static effects on its own."

PYRRHIC PROBABILITIES

Any student of world trade trends over time knows that the 'tit-for-tat' retaliatory tariff measures, apparent during much of the 1930s, both deepened and prolonged the economic depression at that time. Certainly, such insights from economic history remain highly applicable to today's global economy and may actually occur more quickly and more powerfully due to higher levels of trade, interdependence, and integrated supply chains. Such outcomes bode particularly poorly for economies that have placed emphasis on export success and typically being important parts of the global supply chains for corporations and governments around the world. The three best examples of this today are China, Germany, and Japan.

Starting with China, global investors became accustomed to the Middle Kingdom dominating at-the-margin consumption growth statistics. With an urbanizing and wealthier population of over one billion, this should not be surprising; however much of the heavy lifting in the thematic development of the Chinese economy over the past generation has been undertaken by its ever-stronger capability as a producer of intermediate goods for export. China may no longer be the cheapest country to manufacture many goods, but a sharp slowdown in the country's exports due to trade war angst threatens much more than just a reduction in the country's economic growth level. In a static sense, slower economic growth rates can be offset by more stimulus efforts and this has been apparent over the past few months with a loosening in both monetary and fiscal policy, which has helped keep headline economic growth rates close to quoted targets. However, such a focus threatens progress with the country's all-critical domestic reform and change programme, which is attempting to improve the efficiency, dynamism, and longer-term growth potential of the Chinese economy by reforming the banking sector and reducing excesses in areas such as local government debt levels and an over-reliance on the property sector. With the maintenance of stability (and no need to worry about reelection), an overriding objective of the Chinese government, a risky but politically nationalistic dynamic push back, would be a continuation of recent policy of tariff and technological 'tit-for-tat' retaliation,

> “Any progress in the world trade backdrop is likely to lead to a lower value of the dollar which should help reduce inflamed trade tensions.”

and quite possibly the turning down of a tentative deal with the U.S. a few weeks ago. This, however, would slow Chinese economic growth with implications for every country or company selling into the country while inducing material friction into the global trade and diplomatic backdrop.

Another policy option would be to let the Chinese yuan depreciate to help offset higher tariffs and boost price competitiveness at the margin. Currencies, over recent months, have certainly heightened trade tensions, but recent shifts feel more like a reaction to world trade concerns. Any progress in the world trade backdrop is likely to lead to a lower value of the dollar which should help reduce inflamed trade tensions.

THE GERMAN QUESTION

One area that would be negatively impacted by many of the issues noted above is Europe, Germany in particular, the region’s largest economy, whose economic growth has also been assisted over the last couple of generations by export success, especially in a variety of automotive and industrial sectors. Thus far, global trade angst has been focused on the bilateral relationship between the U.S. and China; however, these developments have both static and dynamic risks for all European economies, particularly Germany.

The static implications can already be seen with recent German economic growth levels being closer to those of the struggling Italian economy than those of other leading European economies such as France and Spain. To date, however, there has been little dynamic impact apart from a slight softening in demand from China.

STRESS TESTING ALLIANCES

In a scenario of ‘tit-for-tat’ and retaliation between the U.S. and China, Europe will not be able to stand aside. Already, discussions concerning issues around WTO decision-making and dispute resolution have thrown up divisions, particularly between Europe and the U.S., supplementing some early-stage trade disputes between the two regions. Simultaneously, the European Union leadership, supported by Chancellor Merkel of Germany, has criticized the actions of the populist Italian government in overtly supporting the Chinese ‘Belt and Road’ initiative. More trade frictions create further pressures and incentives for Europe to choose a side, or face new tariffs or sanctions from everyone else.

By contrast, Japanese relations with the U.S. have remained more cordial, despite the potential for trade related disputes in areas such as the automotive sector. The reason for this may be linked to the relatively close defence relationship between the two countries, along with Japan’s instinctive regional caution toward China. Recent manufacturing sector data in the country has shown an impact from the worsening global trade backdrop, at a time when Japanese domestic economic growth dynamism remains muted (as reflected by continued use of quantitative easing policy).

KEY TAKEAWAYS:

- Trade angst that leads to less interaction between economies, in most circumstances, leads statically to lower economic growth as supply chains are interrupted and more expensive alternatives are less cost-efficient.
- China may no longer be the cheapest country to manufacture many goods, but a sharp slowdown in the country’s exports due to trade-war angst threatens much more than just a reduction in the country’s economic growth level.
- More trade frictions create further pressures and incentives for Europe to choose a side, or face new tariffs or sanctions from everyone else.
- Recent manufacturing sector data in Japan has shown an impact from the worsening global trade backdrop, at a time when Japanese domestic economic growth dynamism remains muted.

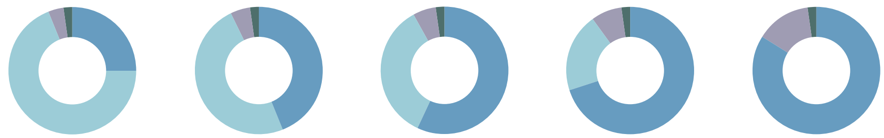
Economic Snapshot

DR. SCOTT BROWN
Chief Economist

The near-term outlook has been mixed, with a healthy consumer sector, but softness in business fixed investment. With the May 10 increase in tariffs on Chinese goods, the drag on U.S. growth has become more noticeable and a further escalation (25% tariffs on the remaining $300 billion or so in Chinese goods) would likely put the economy on the cusp of a recession. The Federal Reserve (Fed) is poised to lower short-term interest rates, if needed. Risks to the growth outlook are weighted to the downside, but much depends on whether we'll see a resolution of trade tensions.

FAVORABLE	EMPLOYMENT	Job markets remain tight. Monthly changes in nonfarm payrolls are volatile, but the underlying trend in job growth has moderated in recent months, partly reflecting labor force constraints.
FAVORABLE	CONSUMER SPENDING	Job gains, wage growth, and consumer confidence remain supportive. Second quarter spending figures appear stronger, but that's not much of a stretch following a weak first quarter.
FAVORABLE	HOUSING AND CONSTRUCTION	Continued strength in the labor market and this year's sharp drop in mortgage rates should support housing activity in the near term. Higher building costs and affordability remain key issues.
NEUTRAL	GROWTH	Economic activity has been mixed, but generally slower, with an increased drag from tariffs. Risks to the growth outlook are weighted to the downside, but depend on a resolution of trade tensions.
NEUTRAL	BUSINESS INVESTMENT	Slower global growth and trade policy uncertainty are negative factors. Orders and shipments of capital equipment remain on a soft track in recent months.
NEUTRAL	MANUFACTURING	Slower global growth has dampened export growth, while trade policy has disrupted supply chains and raised production costs. Factory output has contracted, but that doesn't mean a recession in the overall economy.
NEUTRAL	INFLATION	Inflation can be too low as well as too high and the sub-2% trend in the PCE Price Index is a significant concern for the Fed. Despite tariffs, pipeline pressures have moderated. Firms have had mixed success in raising prices.
NEUTRAL	MONETARY POLICY	The Fed is poised to lower short-term interest rates, if needed, and the proximity to the zero-lower-bound means that officials should be more aggressive in lowering short-term interest rates than they would otherwise.
NEUTRAL	LONG-TERM INTEREST RATES	Long-term interest rates have fallen outside of the U.S., putting downward pressure on U.S. bond yields. Inflation is expected to remain low and the risks to growth are weighted to the downside.
NEUTRAL	FISCAL POLICY	The impact of tax cuts has faded in 2019. The federal budget deficit has increased, but not put much upward pressure on bond yields. State and local government fiscal policy is pro-cyclical, a negative force in a recession.
NEUTRAL	THE DOLLAR	In the short term, exchange rates are driven by monetary policy. Market expectations of a Fed ease are negative for the greenback, but monetary policy is also seen as easing elsewhere.
NEUTRAL	REST OF THE WORLD	The global economic outlook has deteriorated further, with increased concerns regarding China, Europe, and the UK. Trade tensions between the U.S. and China aren't helping.

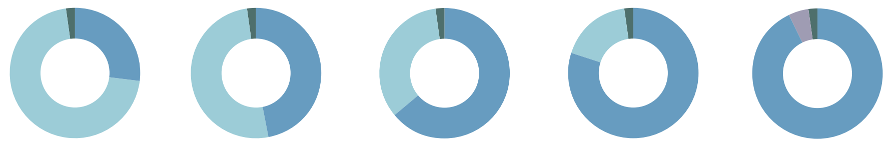
High-Net-Worth & Ultra-High-Net-Worth Models



CURRENT POSITIONING	CONSERVATIVE	MODERATE CONSERVATIVE	MODERATE	MODERATE GROWTH	GROWTH
TOTAL EQUITY	**25%**	**44%**	**57%**	**70%**	**84%**
Total U.S. Equity	15%	27%	34%	42%	50%
Large Cap	12%	21%	23%	30%	35%
Mid Cap	3%	4%	7%	7%	9%
Small Cap	0%	2%	4%	5%	6%
Total Non-U.S. Equity	10%	17%	23%	28%	34%
Non-U.S. Developed Market Equity	8%	14%	19%	23%	28%
Emerging Market Equity	2%	3%	4%	5%	6%
TOTAL FIXED INCOME	**69%**	**49%**	**35%**	**20%**	**0%**
Core Fixed Income	61%	43%	32%	20%	0%
Investment-Grade Intermediate Maturity	51%	35%	25%	14%	0%
Investment-Grade Short Maturity	10%	8%	7%	6%	0%
Plus Fixed Income	8%	6%	3%	0%	0%
Non-Investment Grade FI (High Yield)	3%	2%	0%	0%	0%
Non-U.S. Fixed Income	0%	0%	0%	0%	0%
Emerging Market Debt (Local+USD)	5%	4%	3%	0%	0%
ALTERNATIVE INVESTMENTS	**4%**	**5%**	**6%**	**8%**	**14%**
CASH & CASH ALTERNATIVES	**2%**	**2%**	**2%**	**2%**	**2%**

Refer to pages 22 and 23 for asset class and model definitions.

Strategic Asset Allocation Models

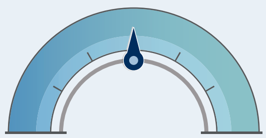


CURRENT POSITIONING	CONSERVATIVE	MODERATE CONSERVATIVE	MODERATE	MODERATE GROWTH	GROWTH
EQUITY	**27%**	**47%**	**64%**	**80%**	**93%**
U.S. Large Cap Blend	15%	17%	21%	26%	29%
U.S. Large Cap Growth	0%	4%	6%	8%	9%
U.S. Large Cap Value	0%	4%	6%	8%	9%
U.S. Mid Cap Equity	2%	5%	7%	8%	10%
U.S. Small Cap Equity	1%	3%	4%	6%	6%
Non-U.S. Developed Market Equity	9%	14%	16%	20%	25%
Non-U.S. Emerging Market Equity	0%	0%	4%	4%	5%
FIXED INCOME	**71%**	**51%**	**34%**	**18%**	**0%**
Investment Grade Intermediate Maturity Fixed Income	56%	42%	28%	15%	0%
Investment Grade Short Maturity Fixed Income	7%	5%	6%	3%	0%
Non-Investment Grade Fixed Income	3%	2%	0%	0%	0%
Multi-Sector Fixed Income	5%	2%	0%	0%	0%
ALTERNATIVE INVESTMENTS/ MANAGED FUTURES	**0%**	**0%**	**0%**	**0%**	**5%**
CASH & CASH ALTERNATIVES	**2%**	**2%**	**2%**	**2%**	**2%**

Tactical Asset Allocation Outlook

For investors who choose to be more active in their portfolios and make adjustments based on a shorter-term outlook, the tactical asset allocation outlook below reflects the Raymond James Investment Strategy Committee's recommendations for current positioning. Your advisor can help you interpret each recommendation relative to your individual asset allocation policy, risk tolerance, and investment objectives.

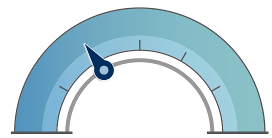
EQUITY



FIXED INCOME

As we enter the latter stages of the economic cycle, our positioning has turned more neutral. With equities trading at historical averages and bond yields at the lower-end of the cyclical range, asset classes, in general, are not inexpensive. As a result, we are Neutral and will look for market corrections to alter our positioning. Volatility is expected to increase which should lead to more opportunities.

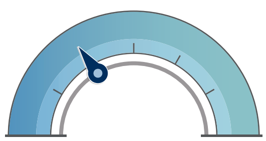
U.S. EQUITY



NON-U.S. EQUITY

While valuations may slightly favor international equities, we continue to favor U.S. equities based on better earnings growth, profit growth, better sector dynamics, and less political risk. Europe has political challenges with Brexit, Italy, and France and Japan has a VAT tax going into effect in October. Pockets of opportunity do exist in EM, particularly in Asia, especially if progress is made with the U.S./China trade discussions. Active management is highly recommended.

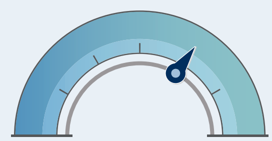
U.S. LARGE-CAP EQUITY



U.S. SMALL-CAP EQUITY

Given that we are in the later stages of the economic cycle and our expectation of increased volatility moving forward, we favor large cap over small cap given its lower beta characteristics. However, our preference is not as pronounced as in recent quarters as small-cap valuations are toward the lower end of historical valuations relative to large cap and small-cap earnings are expected to outpace large cap in both 2019 and 2020.

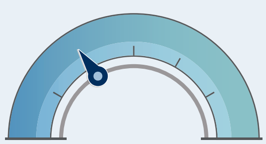
NON-U.S. DEVELOPED MARKET EQUITY



EMERGING MARKET EQUITY

We favor EM over non-U.S. developed equity markets based on more attractive valuations, better earnings growth, and more exposure to cyclical sectors. Additionally, USD stabilization as the Fed eases tends to favor EM given the negative correlation between the two asset classes. Progress in the U.S./China trade negotiations could serve as a catalyst for outperformance.

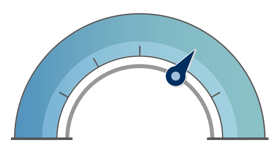
CYCLICALS



DEFENSIVES

Over the past two years, growth has outperformed value by ~20%, the largest two-year rolling outperformance on record, making cyclicals more expensive relative to defensives historically. While this may pose a headwind, we continue to favor cyclicals due to stronger earnings growth (expected to outpace value in both 2019 and 2020) and favorable sector dynamics (cyclicals are more heavily weighted in our favored sectors such as tech).

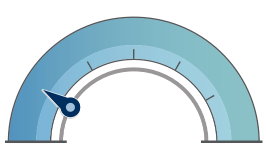
LONG-MATURITY FIXED INCOME



SHORT-MATURITY FIXED INCOME

We prefer having a slightly shorter-duration in fixed income with the expectation that yields will rise modestly over the next 12 months. However, the potential reinvestment risk in shorter-maturity bonds caution us against becoming too short from a duration perspective. Some duration is necessary for diversification benefits during equity market downturns.

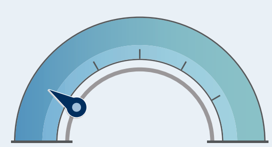
INVESTMENT GRADE FIXED INCOME



NON-INVESTMENT GRADE FIXED INCOME

We favor investment-grade bonds over high yield even though both have become expensive from a historical perspective. In a market that continues to search for yield, both should remain well supported. However, potential downgrades in HY leave us more cautious here.

U.S. DOLLAR FIXED INCOME



NON-U.S. DOLLAR FIXED INCOME

We favor U.S. debt over foreign debt due to better quality, liquidity, and higher yields. The potential for more aggressive global monetary policy should keep interest rates lower for longer. Our conviction has lessened as the 11-year dollar bull market comes to end. Any weakness in the dollar would add to international bond returns.

Alternative Investments Snapshot

ALTERNATIVE INVESTMENTS	Alternative investments experienced mixed results in Q2. The risk-on, risk-off, risk-on quarter was somewhat challenging for many strategies. In general, greater volatility and dispersion should create opportunity but sustained one-way moves may lead funds to move in a similar direction to the broader markets. Many funds were up modestly, but underperformed traditional assets.
EQUITY LONG/SHORT	Following a strong equity-market rally in the first quarter, the second quarter has seen a material pickup in volatility. The long/short equity space has not been immune to these market moves. Q2 started much like Q1 with equity long/short strategies extending gains for the year as corporate earnings and favorable economic trends were supportive for equities. Markets reversed course in May as trade tensions and an inverted yield curve raised recession concerns, causing volatility to pick up and equities to sell off. After bottoming in early June, equity markets have reversed course again. As these strategies are not market neutral, long/short equity funds will move to a degree with broader equity markets. That being said, the dispersion between crowded longs and shorts continues to build and managers have been increasing their gross exposures as the environment for generating alpha appears more robust. Average gross exposures have historically tracked closely to expected volatility and this continues to be the case. While gross leverage has been building, average net exposures have remained steady since last fall, highlighting the cautious directional sentiment of portfolio managers.
MULTI-MANAGER/ MULTI-STRATEGY	Multi-Manager/Multi-Strategy performance will be dictated by the underlying strategies. Diversified, multi-strategy funds would have had a tough time generating interesting returns given the one-way markets each month of the quarter. Those funds with a focus on equity strategies would have been up in April, down in May, and up in June but with substantially less volatility than the S&P. Finally, credit-focused funds performed well in April but tailed off for the rest of the quarter.
MANAGED FUTURES	Managed Futures strategies continued the trend of positive performance from Q1 into Q2 due to sustained trends in global fixed income. Losses from equity indices and commodities created a bump in the road mid-quarter, as equity and energy price weakness created losses in long positions. However, equities caught a bid before many programs were able to switch positioning, driving positive returns late in the quarter and leading to overall positive performance from these strategies for the quarter.
EVENT-DRIVEN	Event Driven strategies had a strong start to the quarter as equity and credit-related positions rallied, but performance suffered in May. Trade war concerns are weighing on merger activity as corporate executives hold off on large transactions until there is greater clarity. This will likely continue unless there is an unexpected breakthrough at the G20 summit. The pure distressed space is also experiencing a lack of opportunity given low default rates. The PG&E bankruptcy represents one of the few large deals available. Multi-strategy managers are best positioned to take advantage of opportunities that arise in the current environment.
EQUITY MARKET NEUTRAL	Market neutral strategies generally suffered during the quarter. After exhibiting flat to negative performance early on, losses accelerated through mid-quarter despite the low net exposure of most managers. Increased dispersion in equity market returns, normally a tailwind, negatively impacted the value bias of many managers as value names fell further than other factors, such as size and momentum.
GLOBAL MACRO	Generally the alternatives strategy which exhibits the greatest dispersion in returns between managers, Global Macro, exhibited positive performance overall, with strong performance to start and end the quarter bookending a difficult period in May. Of the two broad categories of global macro managers (discretionary and systematic), discretionary managers outperformed, as they were better able to respond to economic weakness and the risk of a short-term rate cut by the Federal Reserve.
CREDIT	Credit funds generally provide income and access to both corporate and consumer debt. In the current environment, marked by rising interest rates and frothy markets, manager execution is increasingly important as pockets of credit have become more or less favorable. Investors have raised concerns within corporate credit as companies have increased leverage while credit quality has declined due to a lack of covenants and less collateral backing loans. In contrast, consumers' balance sheets remain healthy with low unemployment rates, increased savings, and lower debt-to-equity ratios, making several structured credit sectors more interesting.

This report is intended to highlight the dynamics underlying major categories of the alternatives market, with the goal of providing a timely assessment based on current economic and capital market environments. Our goal is to look for trends that can be sustainable for several quarters; yet given the dynamic nature of financial markets, our opinion could change as market conditions dictate.

Investors should only invest in hedge funds, managed futures, distressed credit or other similar strategies if they do not require a liquid investment and can bear the risk of substantial losses. There can be no assurance that any investment will meet its performance objectives or that substantial losses will be avoided.

Sector Snapshot

This report is intended to highlight the dynamics underlying the 11 S&P 500 sectors, with a goal of providing a timely assessment to be used in developing your personal portfolio strategy. Our time horizon for the sector weightings is not meant to be short-term oriented. Our goal is to look for trends that can be sustainable for several quarters; yet given the dynamic nature of financial markets, our opinion could change as market conditions dictate.

Most investors should seek diversity to balance risk versus reward. For this reason, even the least-favored sectors may be appropriate for portfolios seeking a more balanced equity allocation. Those investors seeking a more aggressive investment style may choose to overweight the preferred sectors and entirely avoid the least favored sectors. Investors should consult their financial advisors to formulate a strategy customized to their preferences, needs, and goals.

J. MICHAEL GIBBS
Managing Director of Equity Portfolio & Technical Strategy

These recommendations will be displayed as such:

Overweight: favored areas to look for ideas, as we expect relative outperformance

Equal Weight: expect in-line relative performance

Underweight: unattractive expectations relative to the other sectors; exposure might be needed for diversification

For a complete discussion of the sectors, please ask your financial advisor for a copy of *Portfolio Strategy: Sector Analysis.*

	SECTOR	S&P WEIGHT	TACTICAL COMMENTS
OVERWEIGHT	INFORMATION TECHNOLOGY	21.5%	We are Overweight Info Tech. The Fed's message of pending rate cuts should keep the general market trending higher with the high-beta tech sector leading the way. However, any disappointments in trade negotiations with China will weigh on the sector more than others. 1.7% earnings growth is not bad as individual subsectors (semis -11% EPS growth '19) weigh on the average. Valuation is rich for numerous subsectors; therefore, those carrying premium valuation must sustain earnings growth to justify the valuation.
OVERWEIGHT	HEALTH CARE	14.3%	We remain Overweight. The overall sector is attractive with expected earnings growth in excess of the S&P 500, relative valuation below long-term averages, and technical trends improving. Although certain subsectors may struggle as they will be negatively impacted by drug pricing pressure from Congress, numerous others are, for the most part, insulated from the political attacks and should continue to do well.
OVERWEIGHT	COMMUNICATION SERVICES	10.2%	The sector has seen very stable estimate revisions in 2019. Expected earnings growth in Q2 of 5.8% is highest of all sectors. Also, while 2019 estimated earnings growth is in line with the market at 3.4%, the average stock is expected to have 10.4% earnings growth in 2019. Moreover, sales growth estimates are highest of all sectors for the next two years.
OVERWEIGHT	CONSUMER DISCRETIONARY	10.2%	We are Overweight Cons Discretionary despite less than stellar technical trends (especially the equal-weight index) due to favorable earnings expectations (7.4% growth in 2019) and reasonable valuation for the "average stock" as measured by the equal-weight index. If U.S./China trade tensions subside, relative strength trends for both the equal-weight and cap-weighted indices are likely to improve.
EQUAL WEIGHT	FINANCIALS	12.9%	Since the end of 2017, prices for the sector have been held back due to a tight correlation to the 2-year/10-year Treasury yield spread as it declined. Recently, the spread increased, but the correlation to the banks plummeted. The result? Relative performance weakened. With the Fed likely to cut rates (more than once), the banks may struggle (relative to the overall market). However, with the Fed cutting in an environment of decent economic conditions, the odds increase that longer-dated yields rise and steepen the curve. In such a scenario, banks may respond favorably. For now, we suggest patience.
EQUAL WEIGHT	INDUSTRIALS	9.3%	We remain Equal Weight for Industrials. Although Fed cuts (if/when they happen) may rejuvenate softening trends in manufacturing, the current trend remains soft. Price momentum justifies an Equal Weight opinion also as relative strength has been unimpressive during the rally off the recent market pull-back.
EQUAL WEIGHT	ENERGY	5.0%	U.S. supply growth and concern regarding global demand are currently lessening the upside impact on energy prices associated with unrest in the region (U.S./Iran). However, if tensions flare to heightened conflict, energy bulls will get a reprieve from the misery inflicted by the sector over the past year (-16% price only return).
EQUAL WEIGHT	REAL ESTATE	3.1%	Real Estate continues to advance as bond yields plummet. Although both look extreme, we will remain Equal Weight given our belief a substantial move higher in bond yields is unlikely to develop anytime soon. Fundamental trends are supportive of our opinion.
UNDERWEIGHT	CONSUMER STAPLES	7.3%	Structural issues (sluggish volume, inability to adequately raise prices) across some subsectors (food related) influences our bias to be Underweight. On a relative basis, the sector may lag with the overall market taking a more risk-on position due to the message from the Fed.
UNDERWEIGHT	UTILITIES	3.4%	The expensive valuation for this sector influences our Underweight opinion despite solid expected earnings growth relative to the S&P 500. With the recent wave lower for 10-year bond yields, stabilization (or even a counter-trend bounce) will not be a surprise. With Utilities overbought, they are vulnerable to short-term weakness.
UNDERWEIGHT	MATERIALS	2.7%	This minor contributor to S&P 500 performance (2.7% weighting) is expected to post an earnings decline of 8.9% in 2019, and technical trends are weak. Valuation is attractive, however. If a positive agreement between the U.S. and China develops, the sector will likely benefit. However, our base case expects a prolonged battle on trade.

ASSET CLASS DEFINITIONS

U.S. Mid Cap Equity: Russell Midcap Index: A subset of the Russell 1000 index, the Russell Midcap index measures the performance of the mid-cap segment of the U.S. equity universe. Based on a combination of their market cap and current index membership, includes approximately 800 of the smallest securities which represents approximately 27% of the total market capitalization of the Russell 1000 companies. The index is created to provide a full and unbiased indicator of the mid-cap segment.

U.S. Small Cap Equity: Russell 2000 Index: The Russell 2000 Index measures the performance of the small-cap segment of the U.S. equity universe. The Russell 2000 is a subset of the Russell 3000 Index representing approximately 10% of the total market capitalization of that index. It includes approximately 2000 of the smallest securities based on a combination of their market cap and current index membership.

The Russell 2000 Index is constructed to provide a comprehensive and unbiased small-cap barometer and is completely reconstituted annually to ensure larger stocks do not distort the performance and characteristics of the true small-cap opportunity set.

U.S. Large Cap Blend: The Russell 1000 Index. An index of approximately 1,000 of the largest companies in the U.S. equity market. The Russell 1000 is a subset of the Russell 3000 Index. It represents the top companies by market capitalization. The Russell 1000 typically comprises approximately 90% of the total market capitalization of all listed U.S. stocks. It is considered a bellwether index for large cap investing.

U.S. Large Cap Growth: The Russell 1000 Growth Index. A composite that includes large and mid-cap companies located in the United States that also exhibit a growth probability. The Russell 1000 Growth is published and maintained by FTSE Russell.

U.S. Large Cap Value: The Russell 1000 Value Index. A composite of large and mid-cap companies located in the United States that also exhibit a value probability. The Russell 1000 Value is published and maintained by FTSE Russell.

Non U.S. Developed Market Equity: MSCI EAFE: This index is a free float-adjusted market capitalization index that measures the performance of developed market equities, excluding the U.S. and Canada. It consists of the following 22 developed market country indices: Australia, Austria, Belgium, Denmark, Finland, France, Germany, Greece, Hong Kong, Ireland, Israel, Italy, Japan, the Netherlands, New Zealand, Norway, Portugal, Singapore, Spain, Sweden, Switzerland and the United Kingdom.

Non U.S. Emerging Market Equity: MSCI Emerging Markets Index: A free float-adjusted market capitalization index that is designed to measure equity market performance of emerging markets. As of December 31, 2010, the MSCI Emerging Markets Index consists of the following 21 emerging market country indices: Brazil, Chile, China, Colombia, Czech Republic, Egypt, Hungary, India, Indonesia, Korea, Malaysia, Mexico, Morocco, Peru, Philippines, Poland, Russia, South Africa, Taiwan, Thailand and Turkey.

Investment Grade Long Maturity Fixed Income: Barclays Long US Government/Credit: The long component of the Barclays Capital Government/Credit Index with securities in the maturity range from 10 years or more.

Investment Grade Intermediate Maturity Fixed Income: Barclays US Aggregate Bond Index: This index is a broad fixed income index that includes all issues in the Government/Credit Index and mortgage-backed debt securities. Maturities range from 1 to 30 years with an average maturity of nearly 5 years.

Investment Grade Short Maturity Fixed Income: Barclays Govt/Credit 1-3 Year: The component of the Barclays Capital Government/Credit Index with securities in the maturity range from 1 up to (but not including) 3 years.

Non-Investment Grade Fixed Income (High Yield): Barclays US Corporate High Yield Index: Covers the universe of fixed rate, non-investment grade debt which includes corporate (Industrial, Utility, and Finance both U.S. and non-U.S. corporations) and non-corporate sectors. The index also includes Eurobonds and debt issues from countries designated as emerging markets (sovereign rating of Baa1/BBB+/BBB+ and below using the middle of Moody's, S&P, and Fitch) are excluded, but Canadian and global bonds (SEC registered) of issuers in non-EMG countries are included. Original issue zeroes, step-up coupon structures, 144-As and pay-in-kind bonds (PIKs, as of October 1, 2009) are also included. Must publicly issued, dollar-denominated and non-convertible, fixed rate (may carry a coupon that steps up or changes according to a predetermined schedule, and be rated high-yield (Ba1 or BB+ or lower) by at least two of the following: Moody's. S&P, Fitch. Also, must have an outstanding par value of at least $150 million and regardless of call features have at least one year to final maturity.

Multi-Sector Fixed Income: The index for the multi-sector bond asset class is composed of one-third the Barclays Aggregate US Bond Index, a broad fixed income index that includes all issues in the Government/Credit Index and mortgage-backed debt securities; maturities range from 1 to 30 years with an average maturity of nearly 5 years, one-third the Barclays US Corporate High Yield Index which covers the universe of fixed rate, non-investment grade debt and includes corporate (Industrial, Utility, and Finance both U.S. and non-U.S. corporations) and non-corporate sectors and one-third the J.P. Morgan EMBI Global Diversified Index, an unmanaged index of debt instruments of 50 emerging countries.

The Multi-Sector Fixed Income category also includes nontraditional bond funds. Nontraditional bond funds pursue strategies divergent in one or more ways from conventional practice in the broader bond-fund universe. These funds have more flexibility to invest tactically across a wide swath of individual sectors, including high-yield and foreign debt, and typically with very large allocations. These funds typically have broad freedom to manage interest-rate sensitivity, but attempt to tactically manage those exposures in order to minimize volatility. Funds within this category often will use credit default swaps and other fixed income derivatives to a significant level within their portfolios.

Alternatives Investment: HFRI Fund of Funds Index: The index only contains fund of funds, which invest with multiple managers through funds or managed accounts. It is an equal-weighted index, which includes over 650 domestic and offshore funds that have at least $50 million under management or have been actively trading for at least 12 months. All funds report assets in US Dollar, and Net of All Fees returns which are on a monthly basis.

Cash & Cash Alternatives: Citigroup 3 Month US Treasury Bill: A market value-weighted index of public obligations of the U.S. Treasury with maturities of 3 months.

KEY TERMS

Long/Short Equity: Long/short equity managers typically take both long and short positions in equity markets. The ability to vary market exposure may provide a long/short manager with the opportunity to express either a bullish or bearish view, and to potentially mitigate risk during difficult times.

Global Macro: Hedge funds employing a global macro approach take positions in financial derivatives and other securities on the basis of movements in global financial markets. The strategies are typically based on forecasts and analyses of interest rate trends, movements in the general flow of funds, political changes, government policies, inter- government relations, and other broad systemic factors.

Multi-Strategy: Engage in a broad range of investment strategies, including but not limited to long/short equity, global macro, merger arbitrage, statistical arbitrage, structured credit, and event-driven strategies. The funds have the ability to dynamically shift capital among the various sub-strategies, seeking the greatest perceived risk/reward opportunities at any given time.

Event-Driven: Event-driven managers typically focus on company-specific events. Examples of such events include mergers, acquisitions, bankruptcies, reorganizations, spin-offs and other events that could be considered to offer "catalyst driven" investment opportunities. These managers will primarily trade equities and bonds.

Market Neutral: A hedge fund strategy that seeks to exploit differences in stock prices by being long and short in stocks within the same sector, industry, market capitalization, country, etc. This strategy creates a hedge against market factors.

Managed Futures: Managed futures strategies trade in a variety of global markets, attempting to identify and profit from rising or falling trends that develop in these markets. Markets that are traded often include financials (interest rates, stock indices and currencies), as well as commodities (energy, metals and agriculturals).

INDEX DEFINITIONS

Barclays U.S. Aggregate Bond Index: A broad-based benchmark that measures the investment grade, U.S. dollar-denominated, fixed-rate taxable bond market, including Treasuries, government-related and corporate securities, MBS (agency fixed-rate and hybrid ARM passthroughs), ABS, and CMBS. Securities must be rated investment-grade or higher using the middle rating of Moody's, S&P and Fitch. When a rating from only two agencies is available, the lower is used. Information on this index is available at INDEX-US@BARCLAYS.COM.

DISCLOSURE

All expressions of opinion reflect the judgment of Raymond James & Associates, Inc. and are subject to change. Past performance may not be indicative of future results. There is no assurance any of the trends mentioned will continue or forecasts will occur. The performance mentioned does not include fees and charges which would reduce an investor's return. Dividends are not guaranteed and will fluctuate. Investing involves risk including the possible loss of capital. Asset allocation and diversification do not guarantee a profit nor protect against loss. Investing in certain sectors may involve additional risks and may not be appropriate for all investors.

International investing involves special risks, including currency fluctuations, different financial accounting standards, and possible political and economic volatility. Investing in emerging and frontier markets can be riskier than investing in well-established foreign markets.

Investing in small- and mid-cap stocks generally involves greater risks, and therefore, may not be appropriate for every investor.

There is an inverse relationship between interest rate movements and fixed income prices. Generally, when interest rates rise, fixed income prices fall and when interest rates fall, fixed income prices rise.

U.S. government bonds and Treasury bills are guaranteed by the U.S. government and, if held to maturity, offer a fixed rate of return and guaranteed principal value. U.S. government bonds are issued and guaranteed as to the timely payment of principal and interest by the federal government. Treasury bills are certificates reflecting short-term obligations of the U.S. government.

While interest on municipal bonds is generally exempt from federal income tax, they may be subject to the federal alternative minimum tax, or state or local taxes. In addition, certain municipal bonds (such as Build America Bonds) are issued without a federal tax exemption, which subjects the related interest income to federal income tax. Municipal bonds may be subject to capital gains taxes if sold or redeemed at a profit.

If bonds are sold prior to maturity, the proceeds may be more or less than original cost. A credit rating of a security is not a recommendation to buy, sell or hold securities and may be subject to review, revisions, suspension, reduction or withdrawal at any time by the assigning rating agency.

Commodities and currencies are generally considered speculative because of the significant potential for investment loss. They are volatile investments and should only form a small part of a diversified portfolio. Markets for precious metals and other commodities are likely to be volatile and there may be sharp price fluctuations even during periods when prices overall are rising.

Investing in REITs can be subject to declines in the value of real estate. Economic conditions, property taxes, tax laws and interest rates all present potential risks to real estate investments.

High-yield bonds are not suitable for all investors. The risk of default may increase due to changes in the issuer's credit quality. Price changes may occur due to changes in interest rates and the liquidity of the bond. When appropriate, these bonds should only comprise a modest portion of your portfolio.

Beta compares volatility of a security with an index. Alpha is a measure of performance on a risk-adjusted basis.

The process of rebalancing may result in tax consequences.

Alternative investments involve specific risks that may be greater than those associated with traditional investments and may be offered only to clients who meet specific suitability requirements, including minimum net worth tests. Investors should consider the special risks with alternative investments including limited liquidity, tax considerations, incentive fee structures, potentially speculative investment strategies, and different regulatory and reporting requirements. Investors should only invest in hedge funds, managed futures, distressed credit or other similar strategies if they do not require a liquid investment and can bear the risk of substantial losses. There can be no assurance that any investment will meet its performance objectives or that substantial losses will be avoided.

The companies engaged in business related to a specific sector are subject to fierce competition and their products and services may be subject to rapid obsolescence.

The performance mentioned does not include fees and charges which would reduce an investor's returns. The indexes are unmanaged and an investment cannot be made directly into them. The Dow Jones Industrial Average is an unmanaged index of 30 widely held securities. The NASDAQ Composite Index is an unmanaged index of all stocks traded on the NASDAQ over-the-counter market. The S&P 500 is an unmanaged index of 500 widely held securities. The Shanghai Composite Index tracks the daily price performance of all A-shares and B-shares listed on the Shanghai Stock Exchange.

MODEL DEFINITIONS

Conservative Portfolio: may be appropriate for investors with long-term income distribution needs who are sensitive to short-term losses yet want to achieve some capital appreciation. The equity portion of this portfolio generates capital appreciation, which is appropriate for investors who are sensitive to the effects of market fluctuation but need to sustain purchasing power. This portfolio, which has a higher weighting in bonds than in stocks, seeks to keep investors ahead of the effects of inflation with an eye toward maintaining principal stability.

Moderate Conservative Portfolio: may be appropriate for investors with intermediate-term time horizons who are sensitive to short-term losses yet want to participate in the long-term growth of the financial markets. The portfolio, which has an equal weighting in stocks and bonds, seeks to keep investors well ahead of the effects of inflation with an eye toward maintaining principal stability. The portfolio has return and short-term loss characteristics that may deliver returns lower than that of the broader market with lower levels of risk and volatility.

Moderate Portfolio: may be appropriate for investors with intermediate-term time horizons who are sensitive to short-term losses yet want to participate in the long-term growth of the financial markets. This portfolio, which has a higher weighting in stocks, seeks to keep investors well ahead of the effects of inflation with an eye toward maintaining principal stability. The portfolio has return and short-term loss characteristics that may deliver returns lower than that of the broader equity market with lower levels of risk and volatility.

Moderate Growth Portfolio: may be appropriate for investors with long-term time horizons who are not sensitive to short-term losses and want to participate in the long-term growth of the financial markets. This portfolio, which has a higher weighting in stocks seeks to keep investors well ahead of the effects of inflation with principal stability as a secondary consideration. The portfolio has return and short-term loss characteristics that may deliver returns slightly lower than that of the broader equity market with slightly lower levels of risk and volatility.

Growth Portfolio: may be appropriate for investors with long-term time horizons who are not sensitive to short-term losses and want to participate in the long-term growth of the financial markets. This portfolio, which has 100% in stocks, seeks to keep investors well ahead of the effects of inflation with little regard for maintaining principal stability. The portfolio has return and short-term loss characteristics that may deliver returns comparable to those of the broader equity market with similar levels of risk and volatility.

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