SECOND QUARTER 2019 REPORT

ENTERPRISE
WEALTH MANAGEMENT
A division of Enterprise Bank

IN THIS ISSUE

Independence Day

Hard to believe, but 2019 is more than halfway over. While the U.S. observes Independence Day on July 4, the Federal Reserve is trying to preserve its own independence. Threats to the Fed's independence have been coming from the White House, by way of President Donald Trump's demands for lower interest rates.

Continued inside

Continued from Cover

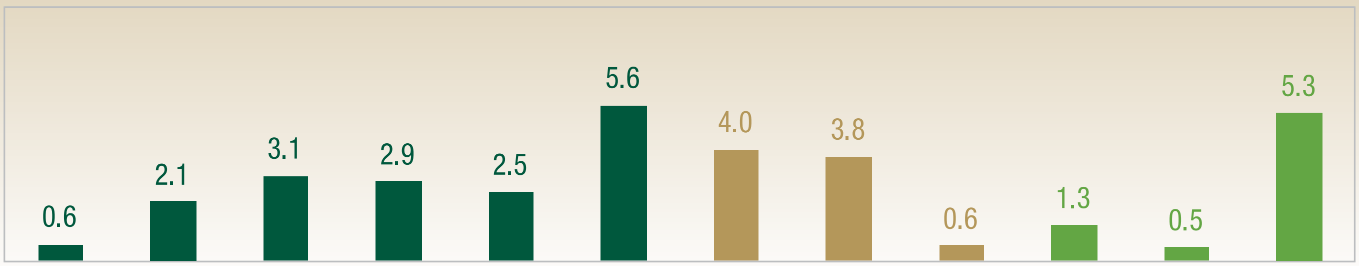
Many view this direct criticism of the Fed as inappropriate, but it increasingly appears the calls for lower rates are warranted. Inflation — at 1.6% — has remained persistently below the Fed's 2% target. With inflation (and inflation expectations) so low and economic growth tepid, the difference between 10-year and three-month Treasury yields is negative — historically a warning sign of recession if the inversion persists.

Up until recently, the Fed has argued the need to head inflation off at the pass. That is, to start (and continue) raising rates in anticipation of inflation's ascent and prevent it from going too high. However, with inflation now trending downward and U.S.-China trade tensions still heightened, the Fed looks set to reverse course. Financial markets are now anticipating anywhere between two and four 0.25% rate cuts from the Fed this year. Further, the Fed seems to be borrowing a page from the orders given to the defenders of Bunker Hill in the U.S. war for independence: Don't fire (raise rates) until you see the whites of their (inflation's) eyes. To the Fed, this means maintaining low interest rates until inflation persistently stays above the 2% target.

As the U.S. celebrates its 243rd birthday, it is also celebrating the 10-year anniversary of the economic expansion. The expansion is the longest in U.S. recorded history, surpassing the one enjoyed through most of the 1990s. With inflation so low and the Fed's accommodative turn, there's reason to believe this expansion can continue into 2020 — and perhaps beyond. That is unless trade tensions materially eat into business and consumer confidence. The Fed's rate cuts can help offset much of the uncertainty, but a full-on trade war would be difficult to combat.

The status of U.S.-China relations has ranged from a severe breakdown in early May, when Trump accused China of reneging on commitments, to renewed hope coming out of the recent G-20 meetings, where yet another cease-fire was announced. So, for now, the only expected fireworks were the ones shot off on July 4. But that could change quickly and everyone — from investors to central bankers — should be prepared.

SECOND QUARTER 2019 TOTAL RETURNS (%)



	RISK CONTROL				RISK ASSETS							
	FIXED INCOME						EQUITIES			REAL ASSETS		
	Cash	Muni	Inv. Grade	TIPS	High Yield	EM Debt	U.S.	Dev. Ex-U.S.	EM	NR	GRE	GLI
YTD	1.2	5.1	6.1	6.2	9.9	8.7	18.8	14.8	10.3	13.8	15.3	20.2

Source: Northern Trust Global Asset Allocation, Bloomberg. NR = Natural Resources; GRE = Global Real Estate; GLI = Global Listed Infrastructure. Indexes are gross of fees and disclosed on last page.

Key Developments

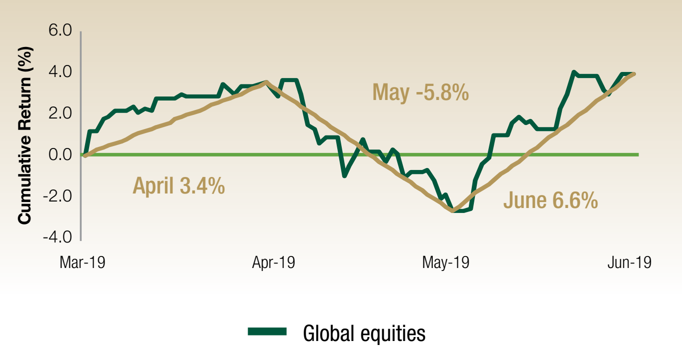
Second Quarter Seesaw

An old investment saying advises "Sell in May and go away [until October]". It got it half right this year. Selling in May would have avoided a 6% drawdown, but not coming back in June would have meant missing out on a big equity market recovery. May's sell-off was driven by renewed trade pressures. The April and June rallies were driven by a properly working interest rate relief valve. We explore each development in the following commentary.

Trade Pressures

Trade developments have driven economic weakness. Solar panel and washing machine tariffs began in early 2018 (1), followed soon after by tariffs on steel and aluminum (2). Then came the direct targeting of China, including 25% tariffs on $50 billion of goods (3) and 10% tariffs on $200 billion (4). In May of this year, the 10% tariffs became 25% tariffs (5) and threats of a 5% tariff (never implemented) were made against Mexico (6).

GLOBAL EQUITY RETURNS BY MONTH



TRADE PRESSURE TIMELINE

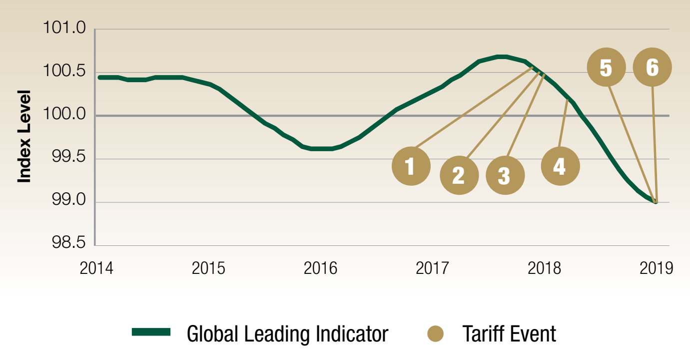
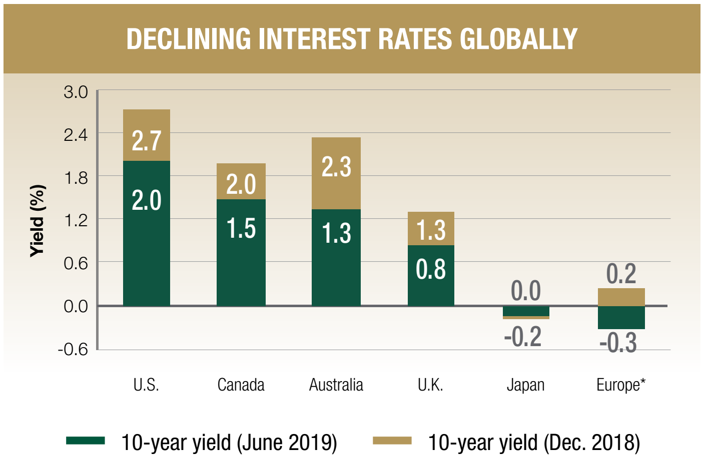


Chart Sources: Northern Trust Investment Strategy, Bloomberg. Indexes are gross of fees. Past returns are no guarantee of future results. Charts are as of December 31, 2018.

Key Developments

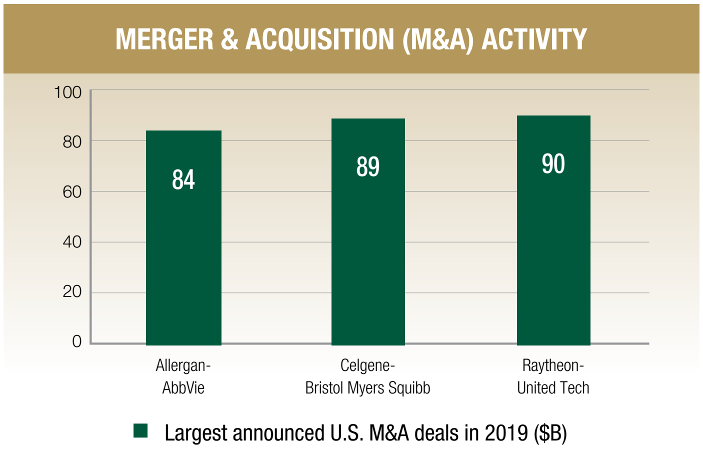
Interest Rate Relief Valve

An interest rate relief valve has diffused some of the trade pressures. Increased central bank dovishness and a continued stuckflation environment have pushed interest rates down around the world in 2019 — with U.S. rates back near where they were prior to the 2016 election and rates in Germany and Japan back in negative territory. Lower rates support economic activity and also allow for higher valuations on risk assets.



Percolating M&A

Merger and acquisition activity has increased recently with major deals announced in the second quarter, including AbbVie's announced acquisition of Allergan and United Technologies-Raytheon (both in June). This joins the Bristol Myers Squibb-Celgene announcement in January. All deals were in excess of $80 billion. Acquisitions often prompt other acquisitions and could support stock valuations in the back half of 2019.

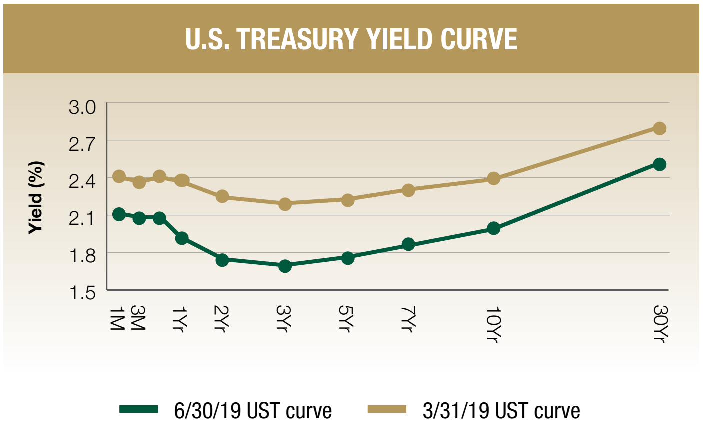


Source: Northern Trust Global Asset Allocation, Bloomberg. *Proxied by Germany.

Market Review

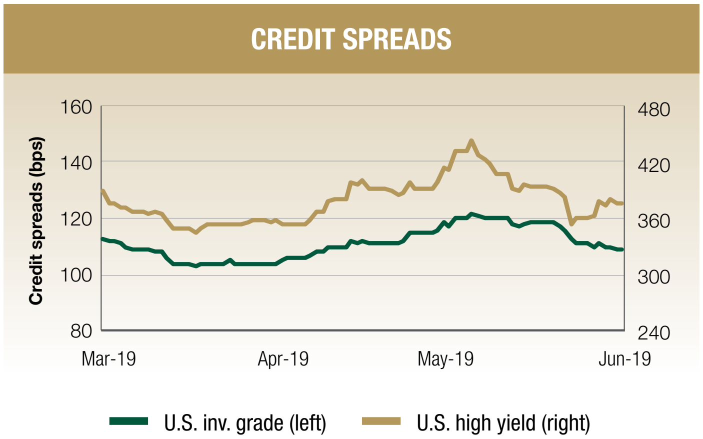
Interest Rates

The U.S. yield curve continued its shift downward as inflation numbers disappointed (core personal consumption expenditures, the Fed's favorite inflation metric, now at 1.6%) and the Fed signaled its willingness to cut interest rates. The 10-year Treasury ended the quarter at 2.0%, while the markets are now fully expecting at least one rate cut this year and a 57% chance of at least three.



Credit Markets

Credit markets followed global equity markets during Q2: tighter through April, wider in May and then tighter again in June. Overall, credit spreads ended the quarter mostly unchanged, representing a tug-of-war between a slower economic growth outlook and the renewed search for yield. In an environment of steady credit spreads and lower interest rates, high yield and investment grade bonds returned 2.5% and 3.1%, respectively.

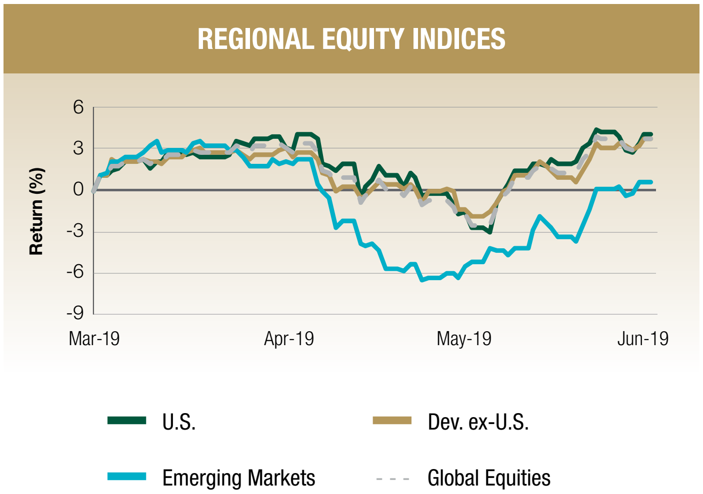


Market Review

Equities

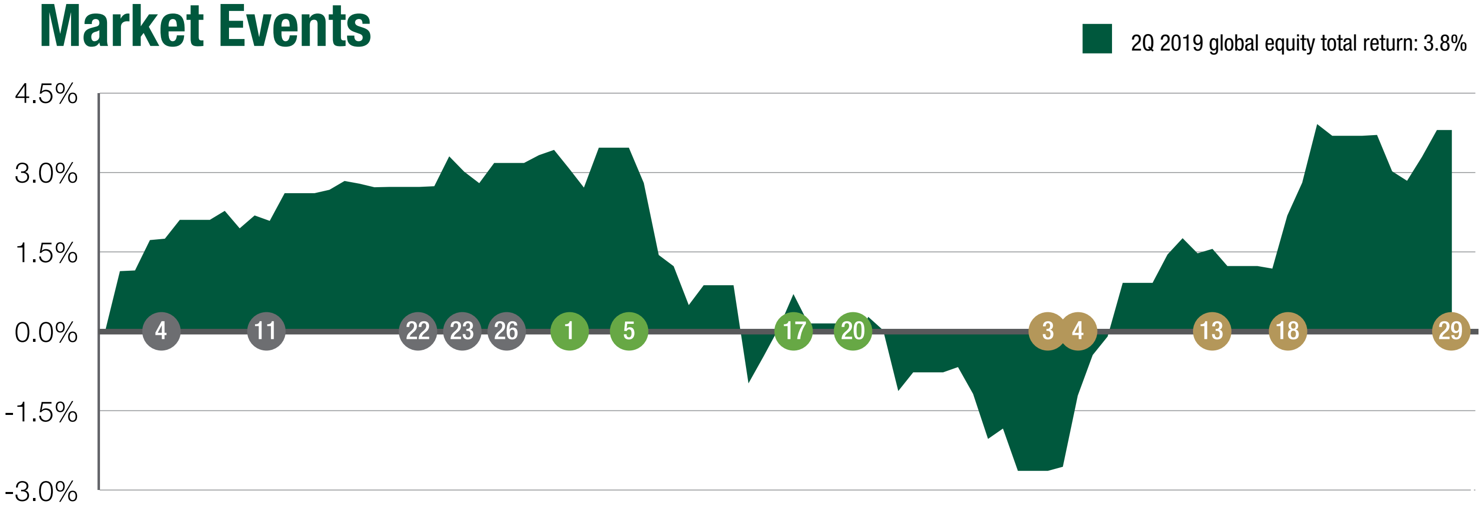
It was a true roller coaster ride for global equities — but one that ultimately ended at higher levels than it began. Developed markets performed best, with U.S. and developed ex-U.S. equities both benefiting from central bank pledges of more accommodation and both returning ~4%. Emerging markets also welcomed easier monetary policy but were hit harder by trade tensions and growth concerns, ending the quarter slightly higher.

Source: Northern Trust Global Asset Allocation, Bloomberg. UST = U.S. Treasury. Indexes are gross of fees.



ENTERPRISE WEALTH MANAGEMENT

Market Events



APRIL	MAY	JUNE
4 China increases purchases of U.S. agricultural products in a positive week for trade negotiations.	1 At odds with market expectations, Fed Chairman Jerome Powell downplays the likelihood of a rate cut any time soon.	3 Technology stocks plunge on heightened concerns over antitrust scrutiny: Google -6%, Amazon -5%, Apple -1%, Facebook -8%.
11 The European Union grants the U.K. a 6-month Brexit extension, allowing the U.K. to leave the EU early if an agreement is reached.	5 President Trump tweets that the U.S. will raise tariffs against China on the upcoming Friday as U.S. officials accuse China of reneging on pledges.	4 Stock prices jump over 2% as Fed Chairman Powell signals an openness to cut rates and Mexican officials note optimism over avoiding U.S. tariffs.
22 Oil prices move higher on news that the U.S. will end waivers that allow countries to buy Iranian oil without facing U.S. sanctions.	17 U.S. ends steel and aluminum tariffs on Canada and Mexico, removing a major barrier to ratifying the countries' new trade pact.	13 Oil prices jump ~4% on reports that Iran attacked and damaged two oil tankers, heightening already escalated tensions with the U.S.
23 A solid start to earnings season drives the S&P 500 above its previous closing high on Sept. 20 to a new record of 2,934.	20 President Trump issues a ban on selling technology equipment to technology company Huawei, escalating trade tensions with China.	18 ECB President Mario Draghi states that the central bank is ready to stimulate the economy through lower policy rates or asset purchases.
28 U.S. gross domestic product report shows first quarter growth surprising to the upside (3.2% vs. consensus expectations of 2.3%).	20 After trailing in the polls, Scott Morrison wins Australia's election for prime minister, sending Australian equity markets up 2%.	29 Risk assets set to rally kicking off Q3 as U.S. and China reach a trade armistice.

Indexes used: Bloomberg Barclays (BBC) 1-3 Month UST (Cash); BBC Municipal (Muni); BBC Aggregate (Inv. Grade); BBC TIPS (TIPS); BBC High Yield 2% Capped (High Yield); JP Morgan GBI-EM Global Diversified (Em. Markets Fixed Income); MSCI U.S. Equities IMI (U.S. Equities); MSCI World ex-U.S. IMI (Dev. ex-U.S. Equities); MSCI Emerging Market Equities (Em. Markets Equities); Morningstar Upstream Natural Resources (Natural Res.); FTSE EPRA/NAREIT Global (Global Real Estate); S&P Global Infrastructure (Global Listed Infra.)

From the Managing Director

Dear Friends and Clients,

I hope you had a wonderful Independence Day and were surrounded by family and friends. I suspect we have all seen countless fireworks shows over the years. I am still in awe of the amazing display of lights and explosions and am never disappointed. Likewise, the global equity markets have put on their own show in the past year, but as I write this, the skies are clearing. The domestic equity markets are again celebrating record heights. The stock market as measured by the S&P 500 rose an impressive 18.5% in the first half of the year and bond markets, too, had notable returns.

The U.S. stock market rewarded investors with the best first half returns since 1997. In addition, the unemployment rate is near the lowest level since 1969, and in July the U.S. reached its longest economic expansion in history. I am reminded of another holiday, Thanksgiving. In this time of national discussion and debate on a variety of topics, this can also be a time to recognize and appreciate the opportunities provided for many during this unprecedented period of growth.

The past ten years since the "Great Recession" have taught the investment industry many things. Individuals and institutions should remember that at times when markets are moving significantly – in either direction – it is best to maintain a long-term perspective and stick with your plan. So, let's not forget New Year's Day. If one of your 2019 resolutions was being more proactive with your finances, it might be an ideal time to revisit your January intentions and contact us to discuss planning, investing or another financial matter. We are always here to help.

Enjoy the beauty of the New England summer, and all our best for a restful and healthy season.

Sincerely,

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Chief Operating Officer, Enterprise Bank

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