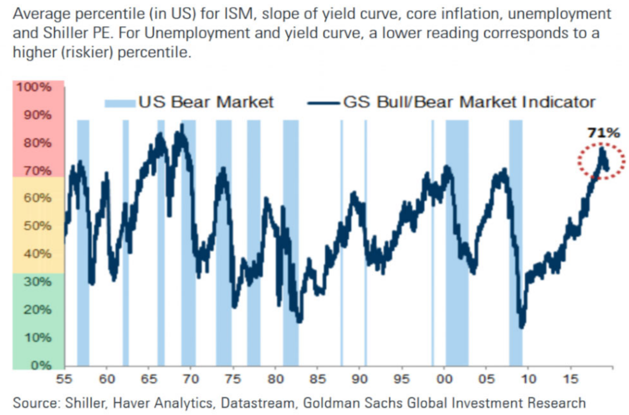
LEGACY WEALTH ADVISORS

Executive Summary

Legacy Update — July 2019

As expected, the global economy continues to slow; a natural result of an aging expansion, disruption to global supply chains from the ongoing China tariff standoff, premature rate tightening by the Fed, and the downside echo of the Q4 pull-forward of demand to avoid the first of several rounds of Q1 tariff increases.

We continue to believe the U.S is facing an earnings recession or growth recession, with a possible 2H re-acceleration now becoming less likely, as the prospects for a 2019 resolution to the trade questions fade. We don't expect a 2020 recession, and yet we will allow that markets may not have our confidence in that outcome.



The Economy

The global economy is likely to slow through the 2H of 2019, and possibly into 2020, with the U.S and China manufacturing alternatives (Vietnam, Hong Kong, Thailand, Mexico, S Korea) remaining stronger than the EU, China, and the remaining emerging market economies. Germany is already on the verge of slipping into a contraction, and several global PMI's are threatening to follow one another below the 50 point threshold.

We continue to see U.S GDP averaging 2% or better for the year, with a possible re-acceleration in Q4, especially if there are hints of a U.S./China deal emerging. That said, we expect trade negotiations to be deliberately "stalled" until China can not tolerate the ongoing growth decay, or until the 2020 political outlook clarifies. As manufacturers repatriate China operations to the U.S. we may see sustained benefits to U.S. capital expenditures and manufacturing employment.

The Fed

The Fed has now moved beyond the "pause" we expected in 1H, and is now hinting at a possible reversal in rate accommodation policy in 2H, with many believing a cut of at least 25bp is likely at the next Fed meeting. We place those odds at 25%, and believe that current conditions do not warrant such a move, and in fact would be a waste of the small amount of easing room they possess.

Inflation remains in line with Fed targets, GDP growth is still reasonably solid at 3% (although expected to ease), wage growth is around 3%, inventories are in line, and the PMI remains above 50. The China trade tariffs have brought disinflation to our shores as we expected, instead of the inflation that many economists and pundits warned about. There is no shortage of lendable funds, and no great demand to borrow that we can see. It is our opinion that the Fed should keep its powder dry.

Politics

We continue to see a widening fracture in the Democrat party, as the Progressive wing tries to drag liberal and centrist Dems ever leftward towards the siren song of Socialism, or "Democratic Socialism" as they say. Trump is proactively fueling the divide with his ever present stream of Twitter grenades, and is attempting to bind the Dem leadership to the Socialists in the minds of Independents and centrist Dems by attacking "The Squad" and highlighting their often anti-American rhetoric.

Trump's approval rating in key Dem voting blocks has soared; doubling among Blacks to nearly 30%, up to 45-50% among Hispanics from 25-30% in 2016, and among high school educated voters, both black and white. Significant job gains in the "Rust Bucket" states, as well as autos, coal, manufacturing and energy have also allowed for some inroads into those traditionally D strongholds as well as labor unions.

The Markets

Markets continue to make new highs as investors ignore the shrill warnings of those who see a recession around every corner. While there are certainly some indicators that are typically present at the beginning of recessions, those indicators are often present in mere slowdowns as well. Inverted yield curves are often associated with recessions, but the lag time can be up to 18 months, so their usefulness as a timing indicator is negligible.

The Goldman Sachs *Bear Market Risk Indicator* above is an another example. While the current showing certainly looks ominous, a closer examination of similar runups going back to the 50's shows many occasions where the *initial* runup was followed by many months, or even years, before a significant bear market occurred. That said, we suggest that markets making new highs in still-slowing economies should warrant a degree of caution.