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MONTHLY MARKET COMMENTARY | JULY 2019

Trade Talks Trip on New Tariffs

Monthly Snapshot

- Developed-market stocks crept higher in July, while emerging markets slid amid continued signs of slowing global economic growth. Government bond rates declined across all maturities in the U.K. and eurozone during the month.
- Top-level U.S. negotiators wrapped up recently-resumed trade talks with China at the end of July. President Donald Trump announced that the U.S. will impose 10% tariffs on $300 billion of Chinese goods beginning in September.
- Major central banks continue to have investors' backs, as they promise to (or already have) cut interest rates and provide other forms of monetary accommodation.

Developed-market stocks crept higher in July, while emerging markets slid amid continued signs of slowing global economic growth. Regionally, the Middle East delivered some of the best country-level returns—Turkey and the United Arab Emirates were the month's top performers; Israel and Qatar also registered among the best returns—while Europe and Asia lagged the rest of the world.

Second-quarter earnings for companies in the S&P 500 Index appeared on track for the second consecutive quarter of year-over-year declines, which hasn't happened since early 2016.

The shortest-maturity U.S. Treasury rates fell in July, while short-to-intermediate-term rates increased, reducing (but not eliminating) the yield-curve inversion that has persisted since the spring. Government bond rates declined across all maturities in the U.K. and eurozone during the month.

Top-level U.S. negotiators wrapped up recently-resumed trade talks with China at the end of July. President Donald Trump announced on August 1 that the U.S. will impose 10% tariffs on $300 billion of Chinese goods beginning in September, essentially covering all remaining yet-to-be-tariffed imports. China responded that it will retaliate if the tariffs are enacted, but the uneven trade relationship leaves a limited pool of U.S. exports for China to tariff (although China allowed the yuan, its currency, to depreciate in early August as a countermeasure). In late July, President Trump and Congress struck a two-year budget deal to raise U.S. discretionary spending; this was expected given sufficient bipartisan support for the deal.

Boris Johnson began serving as U.K. Prime Minister and leader of the Conservative Party toward the end of July, using his new platform to double down on his campaign promise to depart the EU—with or without a Brexit deal—on October 31. He signaled that if the EU wants to avoid a no-deal departure, the Irish "backstop" (part of the deal struck between former Prime Minister Theresa May and the EU) would need to be dropped before any substantive renegotiation could commence. EU negotiators, for their part, have expressed no plans to renegotiate the withdrawal agreement struck with Johnson's predecessor.

Key Measures: July 2019

EQUITY		
Dow Jones Industrial Average	1.12%	↑
S&P 500 Index	1.44%	↑
NASDAQ Composite Index	2.15%	↑
MSCI ACWI Index (Net)	0.29%	↑
BOND		
Bloomberg Barclays Global Aggregate Index	-0.28%	↓
VOLATILITY		
Chicago Board Options Exchange Volatility Index PRIOR MONTH: **15.08**	16.12	↑
OIL		
WTI Cushing crude oil prices PRIOR MONTH: **$58.47**	$58.58	↑
CURRENCIES		
Sterling vs. U.S. dollar	$1.22	↓
Euro vs. U.S. dollar	$1.11	↓
U.S. dollar vs. yen	¥108.58	↑

Sources: Bloomberg, FactSet, Lipper

In mid-July, European Parliament approved Ursula von der Leyen—long-time cabinet member in German Chancellor Angela Merkel's government—to succeed Jean-Claude Juncker as president of the European Commission beginning in November. Earlier in the month, David Sassoli, an Italian member of European Parliament, was elected and immediately began to serve as president of the EU's legislative body. The European Council selected Belgian Prime Minister Charles Michel to succeed Donald Tusk as its next president later this year; it also appointed Christine Lagarde, chairman and managing director of the International Monetary Fund, to follow Mario Draghi as president of the European Central Bank (ECB) before year end.

Trade relations between Japan and South Korea began to deteriorate in July, when Japan tightened exports on input materials critical to South Korea's technology hardware industry. By the beginning of August, each country downgraded the trade-relationship status of the other in an effort to impose hurdles that could put pressure on commerce.

Central Banks

- The Federal Open Market Committee (FOMC) voted during its late-July meeting to cut to the federal-funds rate 0.25%, as was widely anticipated, but signaled in its announcement that the cut should be interpreted as a mid-cycle adjustment rather than the beginning of an easing cycle. The dovish turn also involved an early conclusion to its balance-sheet reduction program, which was originally scheduled to end in September. These accommodative actions came amid below-target inflation and uncertainty about trade developments.
- The Bank of England's Monetary Policy Committee held no meeting during July. Its announcement on August 1 kept policy unchanged and retained a Brexit-contingent preference for tighter policy.
- The ECB made no immediate changes during its late-July meeting. However, it announced a willingness to consider pushing benchmark rates further into negative territory and a need to explore options that could lead to a new asset-purchase program.
- The Bank of Japan announced no monetary policy changes following its meeting at the end of July.

Economic Data

- U.S. manufacturing conditions eased firmly into modest expansion territory during July, while services sector activity accelerated to slow-but-healthier levels. The U.S. unemployment rate held firm at 3.7%, near a 50-year low, and the labor-force participation rate increased to 63% as U.S. employers continued to hire workers at a moderate pace.

U.S. economic growth measured an annualized 2.1% during the second quarter, down from 3.1% in the first quarter.

- U.K. manufacturing conditions contracted at the same pace in July as it did in the prior month, while activity in the services sector remained at a standstill. The claimant-count unemployment rate increased from 3.1% to 3.2% in June; during the March-to-May period, average year-over-year earnings expanded from 3.1% to 3.4% and the unemployment rate held at 3.8%.
- Eurozone manufacturing contracted further during July, clocking its sixth straight month of recession. Services sector activity continued to expand at a moderate pace. Labor-market conditions were unchanged in June, with the unemployment rate holding steady at 7.5%. Eurozone economic growth was halved during the second quarter to a pace of 0.2%, causing the year-over-year rate to slow from 1.2% to 1.1%.

Portfolio Review

The U.S. equity-market rally continued in July at a much milder pace, and large-company stocks returned to outpacing small-company stocks. Our core U.S. large-cap strategy produced a positive return but lagged its benchmark as a result of underweights to information technology and communication services; overweights to the healthcare and energy sectors detracted to a lesser degree. Our core U.S. small-cap strategy performed well due to stock selection within industrials, information technology and healthcare; an overweight to information technology contributed as well. Our international equity strategy was held back in a challenging environment for developed-market stocks outside of the U.S. Selection in healthcare and the consumer sectors detracted; selection within industrials and financials was beneficial, as was an underweight to materials. At the country level, an allocation to South Korea, selection in Switzerland, and

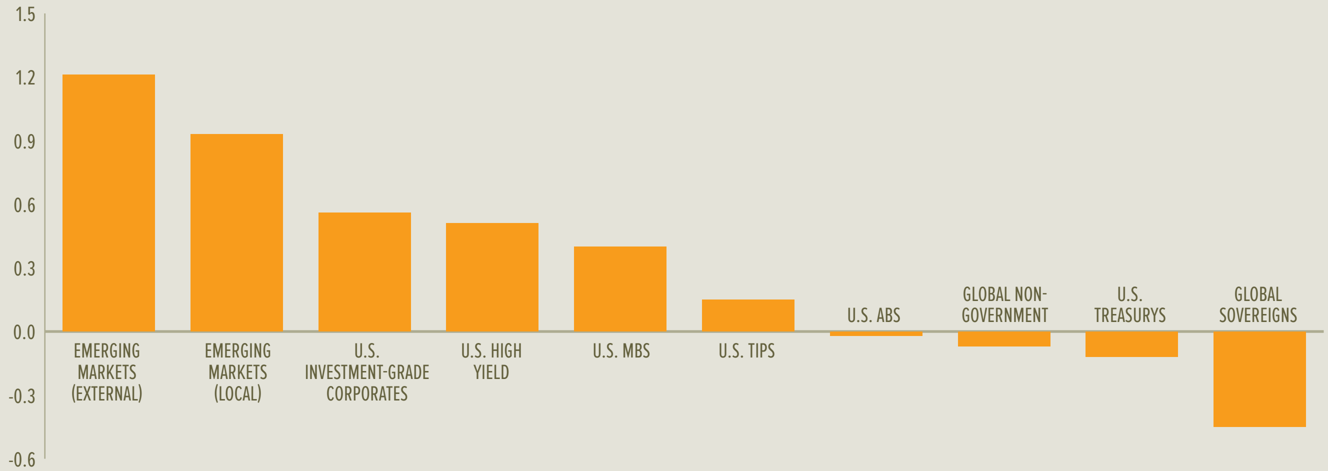
Major Index Performance in July 2019 (Percent Return)

Sources: FactSet, Lipper

overall positioning in Japan hurt relative returns; selection in the U.K. and underweights to Hong Kong and France helped. Our emerging-market equity strategy matched the benchmark's decline during July. Its overall positioning in information technology, selection in consumer discretionary and healthcare, and an underweight to materials contributed, while selection in communication services and financials detracted. Regionally, overall positioning in Brazil and selection in Taiwan and South Korea were beneficial, while selection in China weighed on performance.

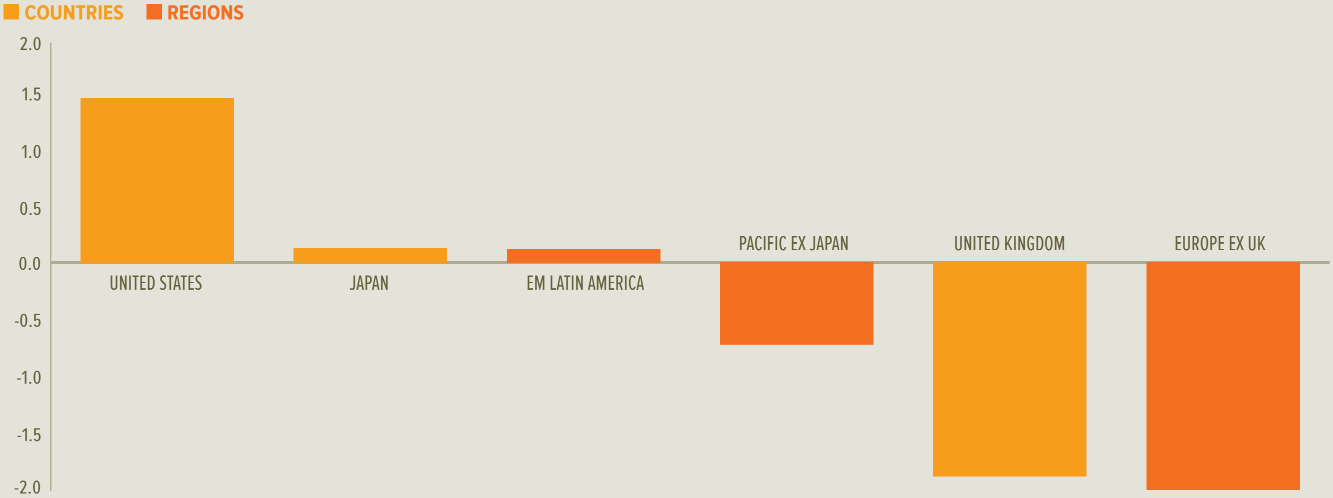
Our core fixed-income strategy was in line with its benchmark's modest gain during July as U.S. investment-grade non-government fixed-income sectors outperformed comparable U.S. Treasurys. An overweight to the long end of the yield curve was additive, as was a slight overweight to corporate credit despite being concentrated in underperforming financials. Securitized sectors generally outperformed, but our exposure to student loans weighed on the strategy's allocation to asset-backed securities (ABS); an emphasis on higher quality within commercial mortgage-backed securities (CMBS) also held back relative performance. An overweight to agency mortgage-backed securities (MBS) contributed, earning a boost from holdings in lower-coupon MBS. An underweight to the non-corporate sector and taxable municipals detracted as both sectors outperformed. Our high-yield strategy closely tracked the benchmark's moderately positive performance in July. The strategy benefited from an allocation to collateralized loan obligations (CLOs) along with selection within retail and healthcare; selection in media and services detracted, as did its overall positioning in banking. Our emerging-market debt strategy also essentially matched the positive performance of its benchmark. An overweight to Ukraine contributed, while an overweight to Venezuela detracted.

Fixed-Income Performance in July 2019 (Percent Return)



Sources: FactSet, Lipper. See "Corresponding Indexes for Fixed-Income Performance Exhibit" in the Index Descriptions section for more information.

Regional Equity Performance in July 2019 (Percent Return)



Sources: FactSet, Lipper. See "Corresponding Indexes for Regional Equity Performance Exhibit" in the Index Descriptions section for more information.

Manager Positioning and Opportunities

U.S. economic activity has continued to increase, but there are indications that the strongest growth may be in the past. Trade tensions have persisted unabated, and the outlook for global growth has fallen to the weakest level in a decade. Our core U.S. large-cap strategy continued to underweight some of the largest-capitalization stocks in favor of better valuations further down the capitalization spectrum; an underweight to utilities also remained due to the sector's interest-rate sensitivity, high-debt balance sheets and low returns on capital. Our core U.S. small-cap strategy maintained an emphasis on cyclical value despite the difficulties these securities faced in July. It also prioritized stability-oriented stocks at the expense of momentum-oriented stocks. Our international developed-market strategy retained overweights to technology and communications services (given their long-term structural tailwinds) and to financials (particularly insurers), energy and healthcare. The strategy maintained an underweight to telecommunications and utilities on their defensive low-growth characteristics. Our emerging-market equity strategy emphasized long-term global growth themes through overweights to technology and industrials. Underweights to financials and real estate were driven by cautious exposure to the Chinese economy. Regionally, the strategy was overweight Brazil and underweight Asia (particularly China, Taiwan and Malaysia).

Our core fixed-income strategy continued to add exposure in the front end of the yield curve and maintained an overweight to the long end of the yield curve. Duration positioning was modestly longer during July, but continued drifting closer to neutral. A modest overweight to the corporate sector remained concentrated in banking; the strategy selectively added in the new-issue market given recent high-issuance volumes. The strategy maintained overweights to ABS and CMBS (due to their competitive risk-adjusted yields) and an allocation to non-agency MBS; it increased an overweight to agency MBS. Our high-yield strategy retained an allocation

Tariff tensions and worries about global growth have put only a modest dent in the confidence of American businesses so far, but it certainly looks as if the U.S.-China trade relationship is getting frostier.

to CLOs and overweights to leisure and media. Energy was the largest underweight, followed by banking, telecommunications and financial services. Our emerging-market debt strategy was overweight to local-currency assets. The biggest country overweights were to Argentina, Egypt and China, while the most significant underweights were to the Philippines, Hungary and Peru.

SEI's View

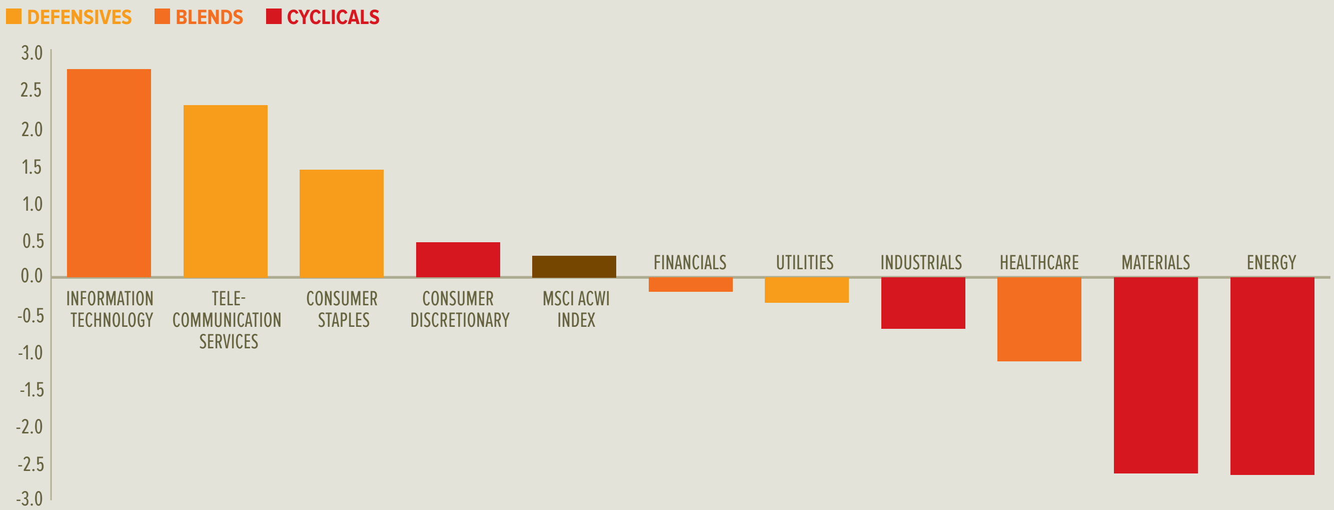
July marked the tenth anniversary of the U.S. economic expansion. The bull market in the S&P 500 Index reached its tenth birthday in March, and appeared to celebrate these achievements by moving into new-high territory through late July. But there now seems to be anxiety that the equity bull market is on its last legs, the victim of a slowing global economy, the lagged impact of last year's U.S. interest-rate increases and, perhaps most importantly, a worsening trade war between the U.S. and China.

To be sure, the U.S. economy is hardly firing on all cylinders. There's a good chance that capital spending will continue to ease in the months ahead, but we're not forecasting a major downturn. Corporate cash generation continues to run slightly ahead of capital expenditures. The main point to remember: It's not unusual for capital expenditures to run well in excess of cash flow, especially toward the end of the economic up-cycle. And that's not happening yet.

We need to see a severe deterioration in financial and leading economic indicators before climbing onto the recession train. Even after the past two years of multiple Fed rate increases, there are still few signs of a build-up in financial stress.

The big unknown, of course, is how the evolving tariff war between China and the U.S. will affect U.S. economic growth and global trade in the months ahead. Tariff tensions and worries about global growth have put

Global Equity Sector Performance in July 2019 (Percent Return)



Sources: FactSet, Lipper. MSCI ACWI Index Components (as defined by SEI).

only a modest dent in the confidence of American businesses so far, but it certainly looks as if the U.S.-China trade relationship is getting frostier.

It is our view at SEI that the U.S. economy should be able to weather this storm. An all-out tariff war between the two largest economies in the world will certainly disrupt supply chains and likely lead to higher prices for a broad range of consumer goods. Still, we think it helps to keep the problem in perspective. Even if the U.S. imposes a 25% tariff on all Chinese imports, total duties will amount to roughly 0.5% of U.S. gross domestic product, according to our calculations of data provided by the U.S. International Trade Commission.

It is not our intention to minimize the importance of the shift in U.S. trade policy toward protectionism. The speed and ease with which supply chains can be relocated to other countries will be a critical factor, either exacerbating or tempering the tariff impact on consumers and companies in both the U.S. and China. An escalation of the trade wars by the U.S. against other countries would prove far more dangerous for the near-term growth prospects in the U.S. than if trade were disrupted only with China.

We have been thinking that the U.S. would avoid waging multiple tariff wars as it concentrated its firepower on China. But our persistent optimism may not hold. Tariffs on German and Japanese autos are still a possibility later this year.

In all, we think the U.S. economy will show resiliency in the face of what is admittedly a stiff headwind. Household income growth has continued to advance at a good pace. The decline in U.S. interest rates that began late last year should certainly help consumers.

The market-implied rate (based on federal-funds futures contracts as of August 1) projects a federal-funds rate of 1.65% by the close of 2019, according to the CME Group, consistent with two additional 25 basis-point cuts. Although the forecasts of FOMC members have been more cautious, they are moving in the direction of the markets. The recent decline in bond yields to levels last seen in 2016 ranks as one of the biggest surprises of the year. We find it hard to justify these moves. In our view, recession is not likely without a severe policy mistake, such as fighting a tariff war on multiple fronts.

When one considers all the headwinds facing emerging economies—a significant slowdown in Chinese economic growth, ongoing trade tensions between the U.S. and China, weak commodity pricing, and a still-resilient U.S. dollar—it's surprising that emerging stock markets have appreciated at all this year.

Europe currently faces a variety of idiosyncratic challenges, both economic and political, that makes it hard for even contrarian investors to get terribly enthusiastic about the near term. Economically, the downward trajectory is similar to that of the 2011-to-2012 period amid the region's periphery debt crisis. This time, however, Germany's industrial economy is fully participating in the slowdown.

Unconventional monetary policy in the form of negative European interest rates, quantitative easing and term lending facilities do not carry a lot of punch nowadays.

It's not just the region's heavy exposure to manufacturing and international trade that makes German industrialists glum. There is also a worrisome vacuum of political leadership. Chancellor Angela Merkel is on her way out, and a politically distracted Germany is a concerning issue given the country's central importance in the eurozone and EU.

At the supra-national level, Christine Lagarde will succeed Mario Draghi as president of the ECB and is expected to maintain the dovish policies of her predecessor. But unconventional monetary policy in the form of negative European interest rates, quantitative easing and term lending facilities do not carry a lot of punch nowadays. An aggressive easing of fiscal policy makes sense, but that strategy is a non-starter in the eurozone. Once again, the structural flaws of the eurozone are coming to the fore.

And then there's the looming cloud of Brexit. Although it has been delayed until October 31, there is little sign that the breathing space will be put to good use. It's hard to see how Boris Johnson's ascension to the role of prime minister improves the chances of an orderly exit.

Although economic growth is sluggish, the U.K. economy is not exactly cratering as the deadline approaches. In fact, the U.K. unemployment rate fell to a multi-decade low. The eurozone also recorded steady labor-market improvement; the jobless rate itself remained far higher, owing to structural factors.

That said, we can't help but think Brexit (if it indeed occurs) will prove to be a highly disruptive event for the U.K. and the EU. Roughly half of the U.K.'s trade in goods, both imports and exports, is with the EU.

We think there is still life in the economic expansion, both in the U.S. and globally. If we're right, that means corporate profits should continue to expand and push global stock markets to higher levels in the months ahead. This may seem like a bold statement at a time when the world seems increasingly unpredictable and the economic data point to slowing growth. Yet we simply do not yet see the economic imbalances or nosebleed equity-market valuations that normally bring on recessions and an associated contraction in earnings and stock prices. It is also clear that central banks have investors' backs as monetary policymakers promise to (or already have) cut interest rates in various parts of the world and provide additional liquidity to their banking systems in both developed and emerging countries.

Glossary of Financial Terms

Dovish: Dovish refers to the views of a policy advisor (for example, at the Bank of England) that are positive on inflation and its economic impact, and thus tends to favor lower interest rates.

Federal-funds rate: The federal-funds rate is the interest rate at which a depository institution lends immediately-available funds (balances at the U.S. Federal Reserve) to another depository institution overnight in the U.S.

Quantitative easing: Quantitative easing refers to expansionary efforts by a central bank to help increase the supply of money in the economy.

Index and Benchmark Descriptions

All indexes are quoted in gross performance unless otherwise indicated.

The Bloomberg Barclays 1-10 Year U.S. TIPS Index measures the performance of inflation-protected public obligations of the U.S. Treasury that have a remaining maturity of 1 to 10 years.

The Bloomberg Barclays U.S. Asset Backed Securities (ABS) Index measures the performance of ABS with the following collateral types: credit and charge card, auto and utility loans. All securities have an average life of at least one year.

The Bloomberg Barclays Global Aggregate Bond Index (formerly Lehman Brothers Global Aggregate Index), an unmanaged market-capitalization-weighted benchmark, tracks the performance of investment-grade fixed-income securities denominated in 13 currencies. The Index reflects reinvestment of all distributions and changes in market prices.

The Bloomberg Barclays Global Aggregate ex-Treasury Index is an unmanaged market index representative of the total-return performance of ex-Treasury major world bond markets.

The Bloomberg Barclays Global Treasury Bond Index is composed of those securities included in the Bloomberg Barclays Global Aggregate Bond Index that are Treasury securities.

The Bloomberg Barclays U.S. Corporate Investment Grade Index is a broad-based benchmark that measures the investment-grade, fixed-rate, taxable corporate bond market.

The Bloomberg Barclays U.S. Mortgage Backed Securities (MBS) Index measures the performance of investment-grade, fixed-rate, mortgage-backed, pass-through securities of Government National Mortgage Association (GNMA), Federal National Mortgage Association (FNMA) and Freddie Mac (FHLMC).

The Bloomberg Barclays U.S. Treasury Index is an unmanaged index composed of U.S. Treasurys.

The BofA Merrill Lynch U.S. High Yield Constrained Index contains all securities in The BofA Merrill Lynch U.S. High Yield Index but caps exposure to individual issuers at 2%.

The BofA Merrill Lynch U.S. High Yield Index tracks the performance of below-investment-grade, U.S. dollar-denominated corporate bonds publicly issued in the U.S. domestic market.

The Chicago Board Options Exchange Volatility Index (VIX) tracks the expected volatility in the S&P 500 Index over the next 30 days. A higher number indicates greater volatility.

The Dow Jones Industrial Average is a widely followed market indicator based on a price-weighted average of 30 blue-chip New York Stock Exchange stocks that are selected by editors of *The Wall Street Journal.*

The FTSE All-Share Index represents 98% to 99% of U.K. equity market capitalization. The Index aggregates the FTSE 100, FTSE 250 and FTSE Small Cap Indexes.

The ICE BofAML USD 3-Month Deposit Offered Rate Constant Maturity Index is based on the assumed purchase of a synthetic instrument having three months to maturity and with a coupon equal to the closing quote for 3-month LIBOR. That issue is sold the following day (priced at a yield equal to the current day closing 3-month LIBOR rate) and is rolled into a new 3-month instrument. The index, therefore, will always have a constant maturity equal to exactly three months.

The JPMorgan EMBI Global Diversified Index tracks the performance of external debt instruments (including U.S. dollar-denominated and other external-currency-denominated Brady bonds, loans, eurobonds and local-market instruments) in the emerging markets.

JPMorgan GBI-EM Global Diversified Index tracks the performance of debt instruments issued in domestic currencies by emerging-market governments.

The MSCI ACWI Index is a market-capitalization-weighted index composed of over 2,000 companies, representing the market structure of 48 developed- and emerging-market countries in North and South America, Europe, Africa and the Pacific Rim. The Index is calculated with net dividends reinvested in U.S. dollars.

The MSCI ACWI ex-USA Index includes both developed- and emerging-market countries, excluding the U.S.

The MSCI Emerging Markets Index is a free float-adjusted market-capitalization-weighted index designed to measure the performance of global emerging-market equities.

The MSCI Emerging Markets Latin America Index captures large- and mid-cap representation across five emerging-market countries in Latin America.

The MSCI EMU (European Economic and Monetary Union) Index is a free float-adjusted market-capitalization-weighted index that is designed to measure the equity market performance of countries within EMU. The Index consists of the following 10 developed-market country indexes: Austria, Belgium, Finland, France, Germany, Ireland, Italy, Netherlands, Portugal and Spain. The MSCI EMU Index captures large- and mid-cap representation across the developed-market countries in the EMU.

The MSCI Europe ex-UK Index is a free float-adjusted market-capitalization-weighted index that captures large- and mid-cap representation across 14 developed markets countries in Europe (Austria, Belgium, Denmark, Finland, France, Germany, Ireland, Italy, the Netherlands, Norway, Portugal, Spain, Sweden and Switzerland). The Index covers approximately 85% of the free float-adjusted market capitalization across European developed markets, excluding the U.K.

The MSCI Pacific ex Japan Index captures large- and mid-cap representation across four of five developed-market countries in the Pacific region (excluding Japan).

The MSCI Japan Index is designed to measure the performance of the large- and mid-capitalization stocks in Japan.

The MSCI World Index is a free float-adjusted market-capitalization-weighted index designed to measure the equity market performance of developed markets. The Index consists of the following 23 developed-market country indexes: Australia, Austria, Belgium, Canada, Denmark, Finland, France, Germany, Hong Kong, Ireland, Israel, Italy, Japan, Netherlands, New Zealand, Norway, Portugal, Singapore, Spain, Sweden, Switzerland, the U.K. and the U.S.

The MSCI World ex-USA Index is a free float-adjusted market-capitalization-weighted index that is designed to measure the equity market performance of developed markets, excluding the U.S.

The NASDAQ Composite Index is a market-value-weighted index of all common stocks listed on the National Association of Securities Dealers Automated Quotations (NASDAQ) system.

The Shenzhen Stock Exchange Composite Index tracks performance of A share stocks (which are denominated in renminbi, the local currency) and B share stocks (which are denominated in Hong Kong dollars, an offshore currency) on China's Shenzhen Stock Exchange.

The S&P 500 Index is a capitalization-weighted index made up of 500 widely held U.S. large-cap companies. The S&P 500 Index is an unmanaged, market-capitalization-weighted index comprising 500 of the largest publicly traded U.S. companies and is considered representative of the broad U.S. stock market.

The TOPIX, also known as the Tokyo Stock Price Index, is a capitalization-weighted index of all companies listed on the First Section of the Tokyo Stock Exchange. The Index is supplemented by the subindexes of the 33 industry sectors. The Index calculation excludes temporary issues and preferred stocks, and has a base value of 100 as of January 4, 1968.

Corresponding Indexes for Fixed-Income Performance Exhibit

U.S. High Yield	BofA Merrill Lynch U.S. High Yield Master II Constrained Index
Global Sovereigns	Bloomberg Barclays Global Treasury Bond Index
Global Non-Government	Bloomberg Barclays Global Aggregate ex-Treasury Index
Emerging Markets (Local)	JPMorgan GBI-EM Global Diversified Index
Emerging Markets (External)	JPMorgan EMBI Global Diversified Index
U.S. Mortgage-Backed Securities (MBS)	Bloomberg Barclays U.S. Mortgage Backed Securities Index
U.S. Asset-Backed Securities (ABS)	Bloomberg Barclays U.S. Asset-Backed Securities Index
U.S. Treasurys	Bloomberg Barclays U.S. Treasury Index
U.S. Treasury Inflation-Protected Securities (TIPS)	Bloomberg Barclays 1-10 Year U.S. TIPS Index
U.S. Investment-Grade Corporates	Bloomberg Barclays U.S. Corporate Investment Grade Index

Corresponding Indexes for Regional Equity Performance Exhibit

United States	S&P 500 Index
United Kingdom	FTSE All-Share Index
Pacific ex Japan	MSCI Pacific ex Japan Index (Net)
Japan	TOPIX, also known as the Tokyo Stock Price Index
Europe ex UK	MSCI Europe ex UK Index (Net)
EM Latin America	MSCI Emerging Markets Latin America Index (Net)

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