ECONOMIC HIGHLIGHTS

U.S. New Single-Family Home Sales came in at a 692,000 annualized unit rate versus 677,000 consensus. The PMI Composite Flash Index came in at 55.7 for Services and 56.6 for Manufacturing for May.

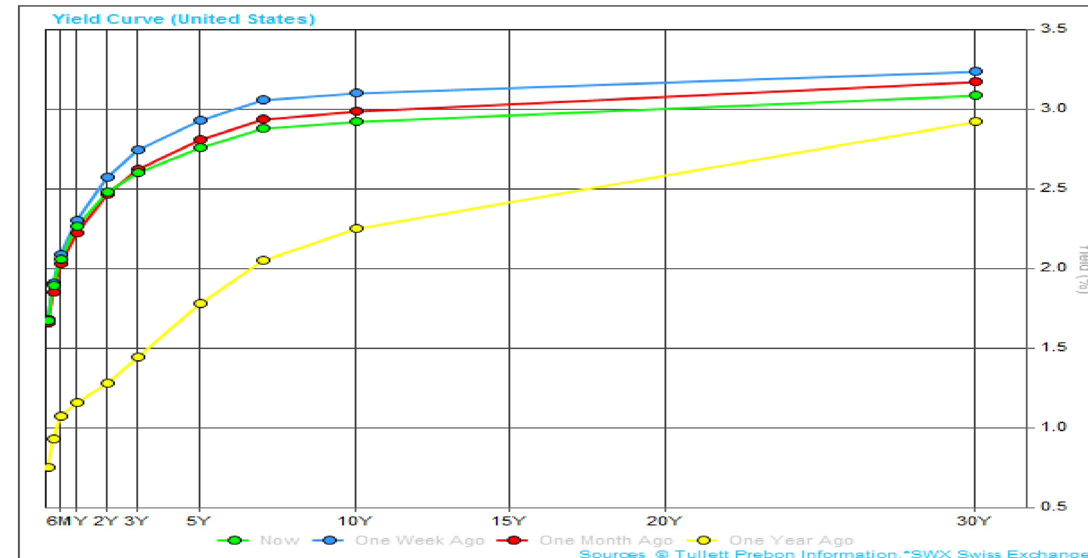
FIXED INCOME

Bond bears looking for a lifeline after the Treasury market's biggest rally in more than a year have a lot to look forward to in a holiday-shortened week. Investors are about to get a reminder that inflation is percolating amid the tightest job market in almost two decades. The mix of data may bring back into focus that the Federal Reserve is probably only weeks away from raising rates again and signaling more increases ahead. The specter of wage pressures and a more aggressive Fed helped drive ten-year yields to an almost seven-year high of 3.13% earlier this month. That was before renewed tension over trade relations and geopolitical concerns spanning both emerging and developed markets spurred a bout of haven buying. Now the market is back to monitoring the same yields that accelerated the bond-market slump when they initially broke just weeks ago. Any sign that a tight job market is boosting wages, and "we'll see yields move higher with the back-end of the curve leading that move," according to Marty Mitchell, an independent fixed-income strategist. "If that happens, then the 3.05% level is the pivot for the ten-year yield as it was previously support." The benchmark ten-year yield sank about 13 basis points last week, its steepest drop since April 2017, closing at 2.93%. Seven days earlier, the yield logged a weekly close above 3% for the first time since 2011. The May surge was enough to trigger some strategists to lift forecasts of where the ten-year yield will close the year. Speculators' net short on ten-year futures contracts remains close to a record, and the same goes for five-year contracts. Putting economic data aside, bond bears point to the government's growing borrowing needs to help justify their stance. A plunge in oil prices last week is adding to forces that may depress yields, on top of the simmering threat of a trade war, turmoil in emerging markets and political risks in Italy and Spain. The yield curve is likely to flatten into Thursday's month-end as investors are set to add duration given the expected extension of the Bloomberg Barclays index, said Dan Mulholland, head of U.S. Treasuries trading at Credit Agricole in New York.

CURRENT GENERIC BONDS YIELDS

TREASURIES		AGENCIES		CORPORATES		MUNICIPALS	
3 mo	1.89%	3 mo	1.94%	3 mo	2.25%	3 mo	1.51%
6 mo	2.06%	6 mo	2.02%	6 mo	2.37%	6 mo	1.57%
1 yr	2.25%	1 yr	2.14%	1 yr	2.46%	1 yr	1.63%
2 yr	2.48%	2 yr	2.49%	2 yr	2.77%	2 yr	1.76%
5 yr	2.77%	5 yr	2.81%	5 yr	3.26%	5 yr	2.11%
10 yr	2.93%	10 yr	3.25%	10 yr	3.75%	10 yr	2.68%
30 yr	3.09%	30 yr		30 yr	4.16%	30 yr	3.63%

CHANGE IN TREASURY YIELD CURVE



EQUITY

INDEX RETURNS	LAST WEEK	YTD
Dow Jones Industrials	0.18%	1.07%
S&P 500 (Large Cap)	0.33%	2.58%
S&P 400 (Mid Cap)	0.21%	30.30%
Russell 2000 (Small Cap)	0.03%	6.44%
NASDAQ Composite	1.09%	8.17%
MSCI EAFE (International)	-1.56%	-0.13%
iShares Real Estate	2.16%	-4.01%

U.S. stocks meandered sideways last week, closing at basically the same level it did the week before. Developed International markets had a rough week, trading sharply lower as the U.S. dollar booked another week of gains.

In these comments last week we noted the recent outperformance of small cap stocks relative to large caps. Bespoke wrote on the topic last week and made note of the fact that most consider the movement of small cap stocks to be a leading indicator for large caps. The fact that small caps typically lead large caps got plenty of attention as small caps broke out to new all-time highs.

One other interesting trend that has emerged recently is the strong performance of the Energy sector. On March 29 at the end of the first quarter, the Energy sector was down -7% - less than 2 months later, the group is up nearly +3.5%. Breadth in the sector is strong with 97% of the stocks in the group trading higher than their 50-day moving averages.

Much of the strong move in the Energy sector can be attributed to the rise in crude oil. Bespoke published a report noting that along with crude oil, gasoline prices have also increased with the national average currently standing at $2.93 a gallon, which is the highest price in over three years. However, the rise has been right in line with historical averages at this time of the year. If the historical pattern plays out, prices at the pump will likely peak around Memorial Day, level out through the summer, and then drift lower to close out the year.

With earnings season all but wrapped up, this past quarter has shaped up to be one of the strongest in several years. According to data from FactSet, with 97% of the companies in the S&P 500 reporting, 78% of the companies have reported a positive earnings per share surprise and 77% have reported a positive sales surprise. If 78% is the final number for the quarter, it will mark the highest percentage since FactSet began tracking this metric in 2008.

The stock market continues to largely ignore the recent political back and forth related to US-North Korea summit, heightened tensions with China regarding trade policy, and the Commerce Department announcing it would undertake an investigation of auto imports. The Commerce Department news followed reports that Trump administration officials have discussed new tariffs of as much as 25% on imported autos.

For the holiday-shortened week ahead we get a few notable earnings releases from the likes of Hewlett-Packard, Dollar General, Dollar Tree, and Dick's Sporting Goods. On the economic front the market sees Consumer Confidence and Case Shiller Index on Tuesday, and PMI numbers later in the week

The sideways move last week for the S&P 500 did little to change the support and resistance levels we are watching. Support levels stand at 2670, 2640, and 2580 – resistance remains at 2800. The index closed last week at 2721.

ASSET ALLOCATION

CURRENT SENTIMENT	
Cash	Neutral
Short Fixed Income	Neutral
Intermediate Fixed Income	Neutral
Inflation-Adjusted Fixed Income	Unfavorable
High Yield Fixed Income	Neutral
International Fixed Income	Neutral
Equity Income	Favorable
Large Cap Equity	Favorable
Mid Cap Equity	Favorable
Small Cap Equity	Neutral
International Equity	Neutral
Emerging Markets Equity	Favorable
Real Estate	Favorable
Commodities	Unfavorable

Below is a summery of our current stance on most asset classes:

Cash - Holding as little as possible given the miniscule yields in money market instruments. Any exposure is for defensive positioning.
Short Term Bonds - Relative to Intermediate Bonds, the reduced duration is preferable given the outlook for higher interest rates.
Intermediate Term Bonds - The current trading range of intermediate bonds warrants a neutral position with limited upside potential. Some opportunities still remain present in spread products.
Inflation-Adjusted Bonds - Low inflation expected in near-term providing zero real return.
High Yield Bonds - Spreads have tightened; however, still remain attractive versus Treasuries.
International Bonds - Emerging market bonds offer good diversification qualities while providing higher yield opportunities relative to domestic fixed income.
Equity Income - High quality and higher-dividend-paying companies remain attractive for long-term investors given their favorable risk-adjusted profile and current yield curves.
Large Cap Stocks - A favorable weighting is recommended. Growth has reemerged as a more favorable style and should be overweighed versus Value.
Mid Cap Stocks - Mid cap exposure along with a value tilt is preferred. Mid cap stocks continue to provide the "sweet spot" of market capitalization - large enough to provide stability, but small enough to be more nimble.
Small Cap Stocks - In broad market corrections, small cap stocks will suffer most with increased volatility. However, a recent divergence of relative strength between small caps and large caps warrants a neutral exposure.
International Stocks - Given most foreign investment is in developed markets and European countries, until sovereign debt concerns are alleviated, an underweight to neutral weight is recommended.
Emerging Market Stocks - Stronger balance sheets, less debt, and better growth potential make emerging markets more fundamentally attractive than developed countries longer-term. Recent relative performance versus developed markets support the stronger fundamental backdrop and positions have been added.
Real Estate - Pricing has stabilized and long-term valuations appear attractive. Real Estate has performed well of late and should continue to be a strong alternative to other asset classes.
Commodities - Global demand should support higher prices if the global recovery remains on track. Although, volatility will be higher and commodities will be susceptible to short-term price shocks, if used in conjunction with other asset classes, risk can be reduced substantially to a diversified portfolio. However, used alone is not recommended as the short-term outlook is not favorable.

Sources of statistical information are Bloomberg and Ned Davis Research.

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