ECONOMIC HIGHLIGHTS

U.S. New Single-Family Home Sales came in at an annual rate of 689,000 units for May, better-than-expected, and was 10.8% better than April. U.S. Durable Goods orders were down 0.6% for May, with Core Capital Goods down only 0.2%. U.S. Real GDP growth for Q1 2018 was 2.0%, approximately as expected. The GDP Price Index was up 2.2%, a bit more-than-expected. U.S. Personal Income was up 0.4% for May, and the PCE Price Index was up 2.3% year-over-year. Finally, the Chicago Purchasing Managers' Index came in at a blistering 64.1 versus consensus of 60.1.

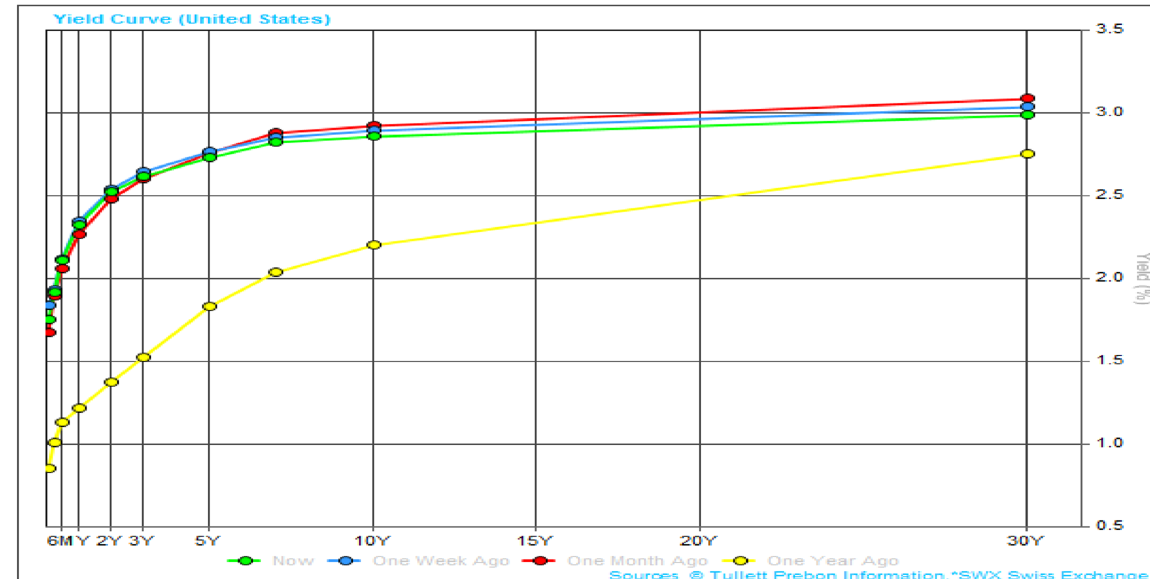
FIXED INCOME

The relentless flattening of the U.S. yield curve could be poised for a breather, as investors look for signs this week that escalating trade disputes will alter the Federal Reserve's plans to lift borrowing costs. Thursday's release of minutes from the central bank's June meeting looms large in a holiday-shortened week, after two Fed presidents warned that trade friction is weighing on businesses and clouding the economic outlook. Friday brings a U.S. deadline to slap $34 billion in tariffs on China, a threat that Beijing has already pledged to retaliate against. The ten-year yield has fallen each of the past three weeks, shrinking its spread over two-year debt to the narrowest since 2007. Any hint that the Fed may pull back from plans to hike twice more this year could slow the curve's march toward inversion. Barring that, the latest monthly job-market reading at the end of the week stands to hammer home that the economy is solid enough to warrant tighter policy. "The minutes will be important because we'll get a further idea about what kind of caution is shaping into the Fed's thinking regarding the effects of any trade war," said Ben Emons, chief economist and head of credit portfolio management at Intellectus Partners. "There is a group that already wants to pause hiking. If the market senses a bigger campaign for that, then traders will lower the probability for a third or fourth hike and that should at least moderate the curve flattening." The ten-year note closed trading last week at 2.86%, down from the 2018 high of 3.13% set in May. The 2- to 10-year yield spread is currently 33 basis points, with the gap between 5- and 30 years at 25 basis points, also close to the smallest spread since 2007. The shape of the curve is drawing scrutiny because inversion has been a reliable indicator of recessions. The curve's contraction gained momentum last month as policymakers lifted rates and raised their projections to a total of four increases for calendar year 2018. The Fed's preferred inflation gauge has been at or above its 2% inflation goal for three consecutive months, which backs the case for more aggressive tightening. For now, traders are pricing in another rate hike in 2018, with some chance of a fourth hike before year end.

CURRENT GENERIC BONDS YIELDS

TREASURIES		AGENCIES		CORPORATES		MUNICIPALS	
3 mo	1.91%	3 mo	1.89%	3 mo	2.38%	3 mo	1.32%
6 mo	2.11%	6 mo	2.05%	6 mo	2.47%	6 mo	1.38%
1 yr	2.31%	1 yr	2.14%	1 yr	2.57%	1 yr	1.46%
2 yr	2.53%	2 yr	2.54%	2 yr	2.84%	2 yr	1.62%
5 yr	2.74%	5 yr	2.80%	5 yr	3.27%	5 yr	2.05%
10 yr	2.86%	10 yr	3.17%	10 yr	3.73%	10 yr	2.65%
30 yr	2.99%	30 yr		30 yr	4.14%	30 yr	3.61%

CHANGE IN TREASURY YIELD CURVE



EQUITY

INDEX RETURNS	LAST WEEK	YTD
Dow Jones Industrials	-1.26%	-0.73%
S&P 500 (Large Cap)	-1.31%	2.65%
S&P 400 (Mid Cap)	-1.85%	3.49%
Russell 2000 (Small Cap)	-2.46%	7.67%
NASDAQ Composite	-2.36%	9.38%
MSCI EAFE (International)	-1.22%	-2.84%
iShares Real Estate	0.82%	1.27%

Rallies on Thursday and Friday were not enough to push the S&P 500 into positive territory, the index closed last week with modest losses. For the week, 7 of the 11 major sector groups closed lower led lower by declines in Consumer Discretionary, Health Care, Financials, and Technology – all of which declined by at least -1%. Gains were relegated to defensive sectors such as Consumer Staples, Real Estate, and Utilities – contributing to a "risk-off" theme for the week.

The impact of the recent trade tensions was highlighted last week by Harley Davidson announcing on Monday that it would shift production overseas to avoid EU tariffs on its motorcycles. The EU raised tariffs on motorcycles to 31% from 6% in response to the Trump administration's metals tariffs, which would have increased the export cost of each bike by about $2,200.

In a report last week, Bespoke wrote that of the seven largest gaps down at the open for the S&P 500 so far this year, all but one was due to headlines related to the threats of a trade war, including two in the last week.

Shares of Nike surged nearly +12% on Friday after better-than-expected sales and earnings, with North America turning positive and gross margins beating expectations. Management also raised the sales outlook for the year.

In corporate action news, shares of Amazon rose on Thursday after the company announced it had reached an agreement to acquire online pharmacy PillPack. Terms of the deal were not disclosed, but earlier reports noted that Wal-Mart was in talks to acquire the company for $1 billion. A number of pharmacy names traded sharply lower on the news including Rite-Aid, Walgreen's, and CVS.

Monday's decline in the Dow Jones Industrial Average pushed the index below its 200-day moving average on a closing basis for the first time in 501 trading days, according to data from Bespoke. The last time the index closed below its 200-day moving average was on June 27, 2016. Since 1952 the current streak of 501 consecutive days is the third longest for the Dow. Rallies on Thursday and Friday were not enough to push the index back above the moving average marking the first weekly close since early 2016.

In recent weeks, U.S. stocks have outpaced international stocks at an accelerating pace – attributed mostly to the recent moves in the U.S. dollar. The S&P 500's relative strength compared to the MSCI World Ex U.S. Index has broken out to new highs and has reached levels not seen in at least 20 years. The S&P 500's performance relative to the MSCI Emerging Market Index has been strong too, but not to the same degree as developed markets.

For the holiday-shortened week ahead there is little meaningful activity on the economic or earnings calendar. The few highlights include the release of the latest FOMC meeting minutes on Thursday and the jobs report on Friday.

The S&P 500 continued to churn essentially sideways last week which did little to the support and resistance levels we are watching. We continue to watch support at 2675 and 2580 – formidable resistance still stands at 2800. The S&P 500 closed last week at 2718.

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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