

Economic & Market Commentary

Market Update – August 2019

The summer months concluded with a weak August for equities while bonds and alternatives were generally positive. Both U.S. and international stocks gave back some of the gains made earlier in the year. Bonds were up across the board in August with international bonds the strongest performers. Alternative assets produced mixed returns as managed futures, REITs, and reinsurance were all up for the month while commodities were the lone negative.

Economy

- Inflation (Consumer Price Index) moved slightly higher to +1.8% year-over-year.
- The latest estimate of second quarter Real GDP Growth came in at an annualized +2.0%, down from the previous estimate of +2.1%.
- Unemployment has continued to hold steady at 3.7%.

Stocks

- U.S. stocks were negative across the board with small value stocks (-5.3%) struggling the most.
- International stocks also saw losses in August with emerging markets (-4.9%) the biggest detractor.
- Globally, the UK (-4.7%), South Africa (-8.9%), and Brazil (-9.2%) were among the worst performing markets.

Bonds

- As volatility continued in equity markets, both U.S. short-term (+0.4%) and U.S. intermediate-term (+1.8%) bonds made gains.
- International bonds posted another strong month (+2.6%), continuing its robust year-to-date (+10.5%) performance.

Alternatives

- Managed futures (+3.7%), reinsurance (+0.2%), and global REITs (+2.5%) were all positive while commodities (-2.3%) trended lower.

What's with the Negative Bond Yields?

Investors generally think of bonds as safe investments that provide a stream of income. It may surprise some to learn that more than one quarter of all government bonds issued globally are trading with negative yields. In monetary terms, that is more than \$15 trillion in government debt with a negative yield in addition to more than \$1 trillion in negative yielding corporate debt. This begs two questions:

1. How do negative yield bonds work?
2. Why would investors buy a bond with a negative yield?

It is important to note that negative yielding bonds do not require investors to make periodic payments to the issuer to continue to hold the bond. Rather, the bonds are purchased at a premium to the par value. For example, an investor may pay more than \$100 for a bond with a \$100 par value that issues no coupon payments. If that bond is held until maturity, the investor will only receive the \$100 par value of the bond even though they paid more than \$100 to buy the bond, thus creating a negative yield over the life of the bond.

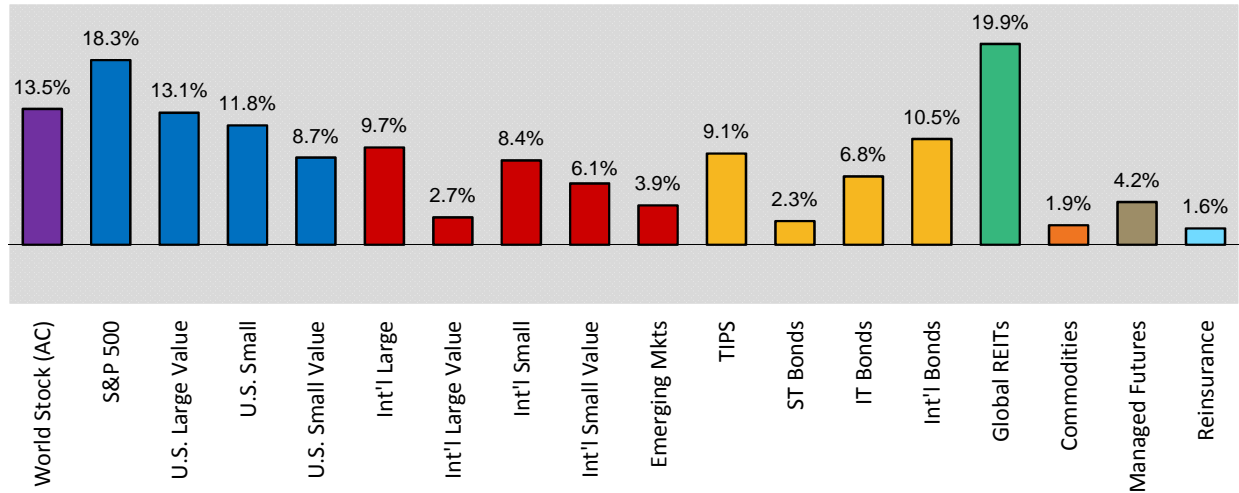
So why might investors choose to buy a bond with a negative yield? Some of the largest holders of negative yielding bonds are institutional investors, such as pension funds and insurers, with specific requirements about the liquidity and risk of the investments they hold. These restrictions essentially mean they are forced to buy large quantities of bonds regardless of the yield.

Another reason investors may purchase negative yielding bonds is because there is still a potential for positive returns. If rates fall, the price of the bond will rise before it matures, which gives the investor an opportunity to sell the bond and achieve a positive return.

Although negative yielding bonds are seemingly counter-intuitive, they are simply a function of economic uncertainty and market forces. The good news is that many U.S. Treasuries and other bonds, while near all-time lows, still have positive yields.

Sources: Nasdaq, Morningstar, Bloomberg

MARKET RETURNS
Year-To-Date as of 8/31/2019



MARKET RETURNS - Longer Term Annualized as of 8/31/2019

	1 Month	YTD	1 Year	3 Years	5 Years	10 Years	15 Years
STOCKS							
S&P 500	-1.6%	18.3%	2.9%	12.7%	10.1%	13.4%	9.0%
U.S. Large Value	-2.7%	13.1%	1.0%	8.8%	7.4%	11.6%	7.8%
U.S. Small	-4.9%	11.8%	-12.9%	7.9%	6.4%	11.6%	8.4%
U.S. Small Value	-5.3%	8.7%	-13.0%	5.1%	4.8%	10.9%	7.9%
Int'l Large	-2.6%	9.7%	-3.3%	5.9%	1.9%	5.0%	5.3%
Int'l Large Value	-4.1%	2.7%	-7.4%	3.8%	-0.8%	3.1%	4.1%
Int'l Small	-2.8%	8.4%	-10.2%	5.6%	4.1%	7.7%	7.8%
Int'l Small Value	-2.5%	6.1%	-10.7%	4.2%	3.1%	7.2%	7.8%
Emerging Mkts	-4.9%	3.9%	-4.4%	5.8%	0.4%	4.1%	8.1%
World Stock (AC)	-2.5%	13.5%	-1.4%	8.9%	5.4%	8.7%	7.3%
BONDS							
TIPS	2.4%	9.1%	7.5%	2.9%	2.2%	3.8%	4.0%
Short-Term Bonds	0.4%	2.3%	3.1%	1.4%	0.9%	0.6%	1.6%
Interm-Term Bonds	1.8%	6.8%	8.1%	2.6%	2.6%	3.2%	3.6%
International Bonds	2.6%	10.5%	13.0%	4.5%	5.2%	4.8%	4.9%
ALTERNATIVES							
Global REITs	2.5%	19.9%	10.8%	5.3%	6.6%	11.3%	7.8%
Commodities	-2.3%	1.9%	-5.9%	-0.9%	-8.6%	-4.3%	-2.8%
Managed Futures	3.7%	4.2%	7.4%	-0.7%	4.2%	2.2%	5.9%
Reinsurance	0.2%	1.6%	0.2%	2.3%	3.6%	6.3%	6.9%

Source: Morningstar Direct. Indices used in above graphs: S&P 500 Index, U.S. Large Value-MSCI U.S. Prime Market Value Index, U.S. Small-Russell 2000 Index, U.S. Small Value-MSCI U.S. Small Value Index, Int'l Large-MSCI EAFE Index, Int'l Large Value-MSCI EAFE Value Index, Int'l Small-S&P EPAC Small Index, Int'l Small Value-S&P EPAC Small Value Index, Emerging Mkts-MSCI Emerging Markets Index, World Stock Index-MSCI All Country World IMI Index, TIPS-Barclays Gbl Infl Linked US TIPS Index, Short-Term Bonds-Ibbotson 1 Yr Treasury Const Mtg Index, Interm-Term Bonds-Barclays Interm-Term Govt/Credit Index, International Bonds-JPM GBI Global Ex US Hdg, Global REITs-S&P Global REIT Index, Commodities-Bloomberg Commodity Index, Managed Futures-Credit Suisse Mgd Futures Liquid Index, Reinsurance-SwissRe Global Cat Bond Index.

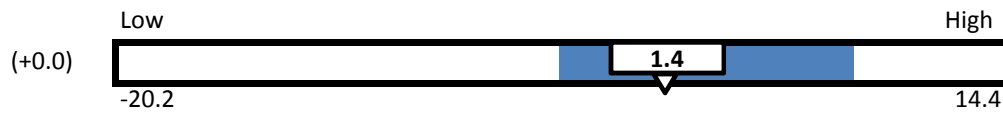
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Economic Indicators

Leading Economic Index Year over Year Change (%)



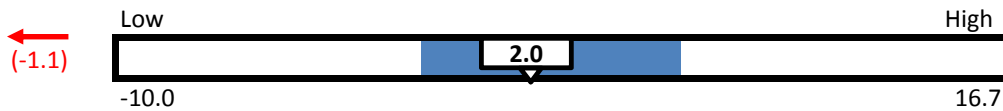
Unemployment (%)



Inflation CPI (YOY %)



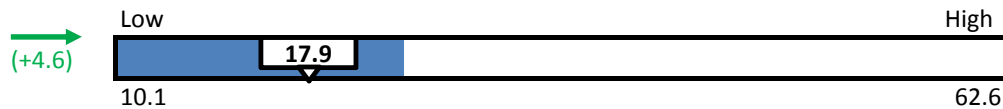
Real GDP Growth (%)



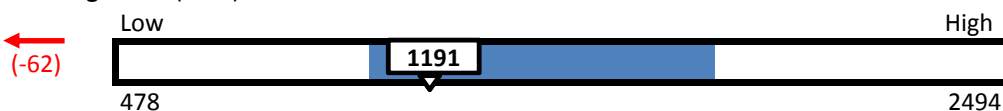
Consumer Confidence



VIX - Market Volatility




Housing Starts (000s)




10-year Treasury Yield (%)



 Typical range (within 1 standard deviation of the median)

 Current Value

 Historical Range

 Change in value since last month

 **See appendix for sources and data ranges*

Appendix

Leading Economic Index Year over Year Change (%)

The Leading Economic Index is composed of 10 indicators used to forecast the direction of the economy. A fall in the index over three consecutive months is seen as a sign of a recession. The value shown represents the 12-month change in the index level. *(Data Source: The Conference Board. Monthly data since 1/1/1959)*

Unemployment

The unemployment rate measures the percentage of workers that are out of work in the U.S. labor force. *(Data Source: U.S. Bureau of Labor Statistics. Monthly data since 1/1/1948)*

Inflation CPI (YOY)

The Consumer Price Index (CPI) measures the change in the price level for a broad basket of goods in the U.S. economy. The value shown represents the percent change in the index from a year ago. *(Data Source: U.S. Bureau of Labor Statistics. Monthly data since 1/1/1948)*

Real GDP Growth

Real GDP Growth represents the change in the market value of all output in the U.S. economy. It is an annualized quarterly measure. *(Data Source: U.S. Bureau of Economic Analysis. Quarterly data since 4/1/1947)*

Consumer Confidence

The Consumer Confidence Index measures the level of optimism among U.S. consumers on the economy and their overall financial situation. *(Data Source: The Conference Board. Monthly data since 1/31/1991)*

VIX

The CBOE Volatility Index (VIX) measures the volatility of the S&P 500 index. An increase in the index level represents a spike in market volatility. Conversely, a decrease in the index represents a move towards stability. *(Data Source: Chicago Board Options Exchange. Daily data since 1/2/1990)*

Housing Starts

The number of housing starts (new construction) in the U.S. each year. *(Data Source: U.S. Bureau of the Census. Monthly data since 1/1/1959)*

10-year Treasury

The annualized return that would be realized for holding a 10-year Treasury bond to maturity. The 10-year Treasury yield is the primary benchmark for measuring interest rate movements. *(Data Source: U.S. Board of Governors of the Federal Reserve System. Daily data since 1/2/1962)*

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