

"Cup of Joe"

Summer is upon us, which usually means that not much should be happening in the markets. European traders go on vacation and don't get back until September, leaving many to wonder if they should have "sold in May and gone away". Well, it just so happens that this summer is full of excitement. We have the possibility of trade wars, rising oil prices, drama in Europe, a political kerfuffle and the list goes on and on. So, is all this much ado about nothing? We will try and shed some light on this with your "Cup of Joe"!

First and foremost, the BIG white elephant in the room is TRADE WARS. Over the past year, the President has been attempting to roll back many of our nation's global trade agreements, in hopes of negotiating new "bilateral" deals that would favor the U.S. and help curtail our country's ever-growing trade deficit. The playbook is very similar to what can be found in the President's literary endeavors where he initially comes out swinging with fiery rhetoric and threats, then uses this to his advantage as a bargaining chip to get a better deal in the end. You may be thinking…how do markets handle these trade "squabbles"? The market favors things that are certain. What it doesn't like is the uncertainty - wondering if the President's hardline rhetoric is for real (that may cause us to enter a real trade war) or if it's just political posturing as he digs in for negotiations. While our intention here is not to wade into this war of words, it is our job to try and foresee how this will affect the markets and your portfolios overall.

What would a trade war do in a nutshell? It makes everything we buy more expensive - a giant tax on goods people buy at the store. By taxing products that consumers buy, it takes money out of the hands of the regular people and reduces their ability to buy goods and services. This, in turn, damages the economies of all countries who participate. Essentially the same idea as when the price of gasoline goes up. If everyone in the world uses gas, and the price rises, the entire economy gets a haircut. While it may help selective industries (think steel) in the short-term, it hurts the average consumer who then must pay more for their everyday goods they buy at Walmart (think China makes everything at Walmart). How will this potential trade war with China end up? Here is the one fact we know for sure. The stock market does not like it…AT ALL.

If you've noticed how volatile markets have been of late, it's essentially a big tug-of-war. The US economy is doing great and the unemployment rate is historically low. Companies are beating earnings estimates and the stocks are rising. Then enter trade war rhetoric in the news and the talk of tariffs… right back down we go! The market, to date, is only up about 5% for the year with the backdrop of robust

earnings. So, how will this end?

As I optimistically opine…I do not, for one minute, think we will go ahead with these moves. Not with the midterm elections in a few months and the possibility of throwing the world into recession. That doesn't bode well for anyone.

The other point of optimism is that while all these trade war shenanigans take place, earnings are still going up, beating their estimates while the market remains relatively flat. This only helps the previously labeled "overvalued market" come back down to reality as it takes a breather and lets the great earnings releases catch up to their companies' lofty valuations. Do we think the trade war will happen? NO! Do we think it could happen? YES, but you really need to set aside common sense and reality. Only time will tell. But if rhetoric turns to vitriolic action and things get out of control, that recession word will start popping up.

One other area of concern we are watching closely are the rising oil prices. They're an economy killer and if they keep going up, we will begin to rethink portfolio allocations in the future. When you combine trade wars along with rising gas prices eating into the consumer's pockets, that doesn't bode well for growth.

Let's look at Europe: Italy remains a wildcard with many fearing that it, too, could decide to leave the EU. While this is just conjecture, it remains a possibility that could lead to further contagion talk within the Euro region. Up until now, the market has put this on the back burner, but we will be monitoring the region closely for further signals.

And finally, the political firestorm that will eventually come to a head in our nation's capital could create an increase in volatility. Remember, markets do not like uncertainty! Why? Because companies and industries do not react quickly. They plan for the future by making investments in factories, technology and employees. When they cannot count on laws, regulations, and especially taxes on products due to trade-wars, they just stop and wait. This creates a pause in growth due to the lack of spending by the companies and the consumer. If drastic shifts in the political landscape happen, market volatility would be following close behind. So, we continue to monitor and make decisions based on all the possible outcomes.

All in all, we are very happy with the economy. The FED is slowly raising rates, exactly as they have predicted **(NO UNCERTAINTY),** which allows the markets to react with confidence. Unemployment remains very low and consumer confidence is strong. Gas prices have started to drop due to an increase in US production and the subsequent OPEC reaction (good news). Markets have put the trade wars in perspective for the short-term. A deal with the European Union came to fruition. China and the U.S. have been rumored to have re-started talks and Apple just went over a trillion dollars in market cap. While we do not think this year will be much like 2017, we remain cautiously optimistic that we will end the year higher than where we are today.

We hope everyone is having a great summer as we look forward to a more prosperous second half of the year!

Please note: If you have received this e-mail from a friend and wish to discuss an investment relationship with our firm, please feel free to contact us. Also, feel free to check out the interesting articles below!

*Disclosure: Chapel Hill Investment Analysts Inc. is long AAPL, DIS, BRK.B.

-Joe, Ryan, and the Chapel Hill Investment Team

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