ARX
MANAGEMENT, LLC

JULY 2018 MARKET COMMENTARY — *"Runnin' With The Devil"*

"I live my life like there's no tomorrow…….." -David Lee Roth

That's the mantra for this 10-year bull market, which seems to be focused on strong earnings and economic data while ignoring some major risk factors. Here's a quick recap of July market events:

Theme	***Event***	***Mkt Effect***
Trade Tensions Escalate	US implements and threatens more tariffs on all trade partners	-
Trump's NATO / Putin Trip	Trump threatens alliance with Euro allies; befriends Russia	-
FAANG's Begin to Bifurcate	FB, NFLX hit; AAPL, AMZN, GOOG strong	+/-
2Q Earnings	85% of companies beat estimates	+
2Q GDP	+4.1% y/y	+
Easy Money Era Ending	Central banks raising interest rates & Quantitative Tightening	-
Fed Independence Threatened	Trump tries to influence Fed to stop raising rates via Twitter	-
Housing Market Pulling Back	Home sales dropping; affordability rapidly declining	-

Equities had a strong month, with the S&P 500 returning 3.6% in July despite a plethora of disruptive headlines. Even more surprising, stock market volatility (VIX) *declined 20%* in the face of a President determined to launch a trade war and cracks emerging in the tech and housing sectors. Growth, corporate earnings, and GDP have been strong, but these tend to be backward looking and were boosted by such one-time events as the repatriation of foreign assets after the tax cut, and a surge in imports and exports as businesses rushed to get ahead of higher tariffs.

US Treasury rates continued to grind higher in anticipation that the Fed will stay the course and raise rates 25 basis points each quarter for the next year. In fact, on August 1st (I'm cheating a bit here), the Fed left rates unchanged at 1 ¾-2% but guided markets to two more increases this year. The yield curve continues to flatten, a theme we have discussed the past few months, with the spread between the 2 and 10-year Treasury narrowing to 29 basis points. A massive trade war will increase inflation in the near term but be a drag on long term growth, exacerbating this curve flattening trade. Breaking custom in yet another arena, President Trump ended a 20+ year period of White House silence on Fed Policy with a Tweet.[1] The Fed's independence, now under threat, is critically important to its ability to effectively steer monetary policy.

Outlook:

We expect the Fed to raise rates a quarter point each quarter on its way to a "neutral" rate near 3% next summer. This predictable rate path will continue to foster an attractive environment for short-term bond investors, as return opportunities will increasingly become more attractive with virtually no interest rate risk - an ideal environment for actively managed Qualified Settlement Funds.

Stocks and risk assets can only run with the devil for so long before the weight of higher rates, trade, housing, narrow market leadership, and policy error are too much to bear. Buckle up!

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1 https://twitter.com/arxceo/status/1021460883623501826

Market Snapshot:

	6/29/18	7/31/18	Change
Fed Funds Target Rate	1.75-2.00%	1.75-2.00%	UNCH
3-month US Treasury	1.92%	2.03	+9
2-year US Treasury	2.53%	2.67	+14
10-year US Treasury	2.86%	2.96	+10
30-year US Treasury	2.99%	3.08	+9
S&P 500	2,718	2816	+3.6%
Stock Mkt Volatility (VIX)	16.09	12.83	-20.3%
US Dollar (DXY)	94.58	$94.49	-0.1%
Oil	$74.39	$68.76	-7.6%
Gold	$1,255	$1,233	-1.8%
Bitcoin	$5,892	$7,724	+31.1%

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About ARX Management:

Established by professionals with direct experience in complex litigation and institutional investment management, ARX offers an unmatched mix of expertise relevant to managing 1.468B Qualified Settlement Funds. Prior to establishing ARX in 2011, our partners actively managed $8 billion in fixed income assets for a large institutional investment manager. Our expertise investing conservative capital preservation products is directly applicable to the management of institutional QSFs. To learn more about ARX: Click Here