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indifference regarding Steve Wynn's inappropriate and sexual misconduct allegations, with a minimal fine of $20 million. A few weeks later, the Massachusetts' Gaming Commission fined the company $35 million for not disclosing sexual misconduct allegations against its founder and then granted the new Encore Boston Harbor it's gaming license. Settlement of these two issues removed a dark cloud over potential future revenue streams. Strong bookings in Las Vegas served as the cherry on top of a really good start to the 2nd quarter.

Just as the company seemed to be riding a wave of momentum, the combination of President Trump's tweets about additional tariffs on Chinese goods and evidence of slowing economic data in China (which negatively affects bookings and high stakes gambling at the Wynn property in Macau) caused the stock to fall over 30% in just 20 trading days. We typically have a trigger where if a stock falls 20% or more, we automatically sell. In this case, our sell discipline was followed and positions were sold.

This was one of those situations where all of the fundamentals supported a timely purchase. WYNN had broken out of its previous price range to the upside, all of its value metrices met our criteria and the new management team was implementing its growth strategy. Sometimes, no matter how fundamentally sound a decision might be, you have to take your lumps and move on. This was one of those times.

Moving On Up

The Markets

Marketer-In-Chief

In early May, I sat proudly in the audience watching my daughter graduate with a degree in Public Relations from the College of Journalism and Communications at the University of Florida. As I listened to the commencement speaker, an alumnus and famed National and International correspondent, reference the obligation the media had to provide accurate and unbiased reporting, I could not help but chuckle. While her words might be well intended for the "naive" graduates sitting in the audience, the irony was rich, as her employer had recently been accused of promoting "fake news" with political bias. Nonetheless, she was right about one thing, it is the job of a good reporter to let the consumer of news form their own opinion of the report's validity.

The reporting of news has changed dramatically over the last several decades from trusted reporters with an art of delivery to social media void of context, thought, sensitivity and many times truth. Often, the consumer has little time to ponder and digest what they have read on Twitter, Facebook or other social forums before a war of words breaks out.

Our President uses Twitter as his personal forum to by-pass the National Press Corp and other media outlets to speak directly to the American people. His emotional tweets often miss the mark and are nothing more than spontaneous eruptions misconstrued as news. Other times the President seeks to create news by tweeting a self-serving PSA (public service announcement) or promoting a new policy or program. The difference between the two is nuanced. We all know Trump is vested in seeing stock prices move higher, as the markets are his proxy for the economy. Therefore, his tweets are tilted to pacify Wall Street. His tweets on trade negotiations were designed to be a short-term catalyst at a time when the markets were volatile. Yet, there was no real progress. Is that considered fake news? The markets didn't think so. Stocks thrived, setting new records with each tweet.

We don't hold much hope for any grand deal between the U.S. and China any time soon and worry that investors could be way out over their skis in expectations for a deal.

Social media and tweeting might be all the rage as the new efficient mass marketing media but it should not be confused as a catalyst to move stock prices higher over the long-term, especially knowing that the president uses it to promote an agenda and provides no context, substance or proof of accuracy. As an investment professional, I have to stick with my process and not get sucked into the emotional urge to make spontaneous and potentially ill-advised investment decisions based on an off-the-cuff tweet or social media post.

More Juice, Please

Trump's exploitation of social media helped upward market trajectory in 2Q'19, but it was not the primary catalyst. The major push in market growth resulted from the expectation of lower rates. Economists, Wall Street gurus, investors and even the president want the Fed to take back last December's rate increase. The general consensus is that lowering rates will stimulate greater economic growth. By the looks of it, everyone is getting their wish. Federal Reserve Chairman Jerome Powell all but promised Congress that the Fed will lower rates at the next Open Market Committee meeting on July 30th and 31st. His comments came during two days of testimony to Congress in which Powell rationalized that "The economy performed reasonably well over the first half of 2019 and the current expansion is now in its 11th year. However, inflation has been running below the Federal Open Market Committee's (FOMC) symmetric 2 percent objective, and crosscurrents, such as trade tensions and concerns about global growth, have been weighing on economic activity and the outlook."

Powell's comments jive with what I have been saying since last fall, but a slowing economy is not a recession! The Fed needs to lower interest rates because: (1) inflation targets are low, (2) capital investment is sluggish or (3) Trump's tough tariff talks are a bit of a stretch (at this point). I think the real motive in lowering rates is to follow the lead of other central bankers around the world. The concern is if China (which just reported its slowest growth since 1992) and the ECB (European Central Bank) both lower rates in unison without the U.S., then the dollar will rip higher, resulting in a real headwind for U.S. companies selling products and services abroad. It's unusual for a sitting president to be campaigning for a weaker dollar, which insinuates or portends a slowing economy.

Should the Fed choose to lower rates by 25 or 50 basis points over the next couple of months, there is no guarantee that it will create the desired growth. Afterall, global rates have been zero or negative for years. There is a record $13 trillion of global debt with negative rates. This means investors are willing to pay issuers for the luxury of owning their bonds. They figure it is safer than putting money into their local stock market. That is not very encouraging!

I'm not sure why the United States is taking their monetary policy cues from the rest of the world. We seem to be the anomaly since we are growing (albeit slowing)! Household wealth is rising, unemployment is at record lows, wages even at the low end are rising and the consumer is spending. We have seen this low-rate policy play out over the last decade in the form of TINA, the acronym made popular over the last decade, referencing There Is No Alternative to stocks. Income sensitive investors must seek riskier assets to satisfy income needs since bond yields are so low. As we saw during the Obama Administration, higher stock prices did not translate to greater economic growth. It only served to create a greater disparity in household wealth among the top and bottom economic classes. The bottom line is that savers should not be penalized with lower rates just because inflation is nonexistent or that Trump decides to assault global trade.

Lower rates do not necessarily translate into greater sustainable growth. The best way to support the economy and stimulate the stock market is to provide an environment conducive for growing profits through capital investment, efficiencies, hiring and wage growth. As we get closer to the election, volatility should increase as uncertainty over future economic policies reduce the incentive for companies to reinvest in their business, hire and raise wages.

Quarterly Review

A dovish Fed, expectations for lower rates, optimism for an end to tariffs and the trade war helped the financial markets build on the torrid pace of gains set in the first quarter of the year. While market performance was not nearly as strong as the previous quarter, combined, the pace of first half returns was memorable. The S&P 500 had its best first half of the year since 1997!

In April, the S&P 500 overtook the highs set back in October of 2018. On the back of stronger than expected earnings and hope for détente in trade, the index set three additional all-time closing highs in the month. The Nasdaq hit its all-time high set back in August of 2018 and closed the month at record levels. The Dow Jones Industrial Average rose more modest 2% for the period and closed less than 1% from its all-time high.

Optimism faded in May amid deteriorating trade talks between the U.S. and China. When talks broke down, Trump threatened to escalate tariffs on Chinese imports. As a result, investors began to worry about a global recession. The Dow and S&P 500 both lost almost 7% in the month, while the Nasdaq lost 8%. In early June, the Fed dominated the headlines as Powell addressed trade fears and indicated that it would work with fellow central bankers to support the economy as needed to combat the potential negative effects of tariffs and a slowing global economy. The expectation of easy money policies kick-started a rally that enabled the three major indices to gain back more than what was lost in May. The month was so strong that the Dow and the S&P 500 recorded their largest gains for June since 1938 and 1955, respectively.

Gains were broad based in the quarter as more than 60% of companies in the S&P 500 recoded gains and 10 of the 11 sectors were positive. Surprisingly, with all the talk of the Fed lowering rates, the Financial sector led the way with gains of over 7%. Typically, when the Fed lowers rates, banks don't respond well as lower borrowing costs reduce their interest income and profits. But Large-cap diversified banks helped lead the group on cost cutting, favorable results on the Fed's semi-annual stress test, stock buybacks and higher dividend payouts.

Both Information Technology and Material stocks swung wildly in the quarter, as their profit prospects hung in balance with trade negotiations. Nonetheless, both sectors returned almost 6%, indicating how optimistic investors were of a trade resolution. The Technology sector had its best first half of the year since 1996.

The only sector to find itself in the red was Energy. The sector fell 3.7% in the quarter as concerns of weakening demand spreading throughout the globe. A report released by the Energy Information Administration (EIA) and OPEC signaled growing supply at a time when the summer driving season should be drawing down inventories, causing a downgrade of projected demand for the back-half of 2019.

Due to better economic fundamentals and growth outlook, all three major U.S. indices outpaced the returns of other popular markets around the world. On a year-to-date basis, the S&P 500 bested the UK's FTSE 100 by over 7%, the European STOXX 600 by over 3%, the Japanese Nikkei by over 10%, emerging markets by 7% and the all developed markets represented by the EAFA by 3%.

Once again, growth companies continued to do better than value. The Russell 1000 growth index was up 21% this year while the equivalent index tracking value jumped 15%. The trend held for all cap sizes except for the very smallest of companies. The Russell Micro-cap value index was higher by 1.4% compared to the corresponding growth index of 0.4%.

Treasury bond prices increased (yields fell) for a third straight quarter, as risk averse investors flocked to safe haven assets in the face of growing concern over the slowing economy and trade negotiations. The Treasury yield curve continues to be inverted. This means investors can get higher yields for lending money over shorter periods rather than longer terms. At the end of June, the 6-month Treasury Bill was yielding 2.1% compared to a 10-year Treasury yield of 2%. Would you rather tie up your money for 6 months and get a higher yield than if you invested for 10 years? Of course, it's a no brainer! Typically, an inverted yield curve is not a healthy economic indicator as it usually portends a recession within 18 months.

The Portfolio

Staying Prudent

Although we put a good deal of money to work this year, portfolios still have between 10% -12% cash. This is high for us as we like to have no more than around 5%. We attribute this to a couple of factors. First, cash is and has been a viable asset class for the last several quarters as rates plateaued around 2.5%. Since we don't buy stocks or ETF's at or near record highs, we choose to carry a bit more cash enabling us to be opportunistic when the markets fall back. Case in point, most of our new positions this year have been added during brief pullbacks off record highs. The second reason for carrying cash is that the markets have not really provided much of a chance. The general market trend has been higher, and we see fewer value candidates.

The third reason we hold more cash than usual is that we question the sustainability of the upward market momentum going into the second quarter earnings period. While the S&P 500 has reached historic highs this year, earnings have been declining. In the first quarter, earnings grew less than 1% over the same period in 2018. So far this quarter, with 25 companies having reported so far, earnings are coming in down 10.9%. Overall, Wall Street consensus is projecting year-over-year declines in earnings for the second and third quarters, extending a streak that began in the first quarter. If these estimates hold, it will mark the longest streak of declines since 2015-2016. Rhetorically speaking, how can the markets consistently reach new highs as earnings are falling? There must be a limit to how much value investors are placing on the Fed and Trump's trade policies and tweets. At some point the markets and investors must come to grips with the reality of declining earnings and valuations. This explains why the S&P 500 market multiple has expanded this year from 19.5X at the end of December to over 22X at quarter-end.

Our pledge to investors is that we will remain vigilant in our pursuit for appropriate investments. We will not chase the markets higher and will continue to pick our spots as asset prices churn with every Fed speech, Presidential tweet and economic report.

Where to Invest

As we enter the third quarter, all major U.S. indices have enjoyed significant double-digit gains for the year. Yet, there is no conclusion on trade. The president continues to use tariffs as a tool to encourage China to come back to the negotiating table. The global economy continues to stumble about and central bankers around the world are promising more stimulus to fend off a potential recession. While the U.S. economy seems to be on better footing than other developed countries, its growth is uneven at best and corporate earnings will likely decline for the third straight quarter. Therefore, what's clearly moving the markets to record highs and what seems to be most important to investors is the Fed! When Fed Chairman Powell went dovish and promised no more rate increases back in January, the markets took off. When he indicated that the Fed would do whatever it takes to support the economy in March, the markets took off. Finally, in June when Powell all but insinuated that the Fed would lower rates at its July meeting, guess what, the markets took off.

My point is, fundamentals be damned, investors need their fix of lower rates. I don't agree with the reliance of monetary policy as a market catalyst nor do I believe lower rates are necessary. In addition, markets are expensive and inflated in lieu of a true catalyst.

Nonetheless, we are making investment decisions based on the notion that trade and the global economy will continue to be an issue and the Fed will remain on the sideline after its July meeting as economic fundamentals stabilize and improve. The combination of global headwinds and future Fed indifference could create a volatile third quarter. As such, we will continue with a defensive posture to protect asset values until there is a retracement to value or a true sustainable catalyst emerges. I might sound like a broken record but we will continue to focus on Staples, Healthcare, REIT's and Communications sectors as viable options for finding value. We are also moderately interested in material and technology stocks that don't have big exposures to China.

Additions & Subtractions

We were busy adding stocks to equity portfolios in the second quarter. We went back and revisited old favorites like **United Health Care (UNH)** and **Home Depot (HD)**. Both stocks have unique characteristics that combine both growth and value elements, while operating in challenging business environments. UNH looks and feels like a growth company. It has growing revenues (over 8%) and earnings (over 14%), pays a small dividend and has valuation metrics that range at the higher end of its peer group.

However, the overall healthcare industry has come under significant pressure over the last several months from fears of healthcare reforms ahead of the 2020 presidential election. Some of the frontrunners are floating proposals that would increase Medicare Part D rebates while other candidates are looking to generally expand Medicare. There is a high likelihood that, should the democrats win the White House, "Medicare for All" would expand lowering premiums which would cut UNH's revenue and pressure margins.

These concerns helped push United Healthcare's stock down over 20% from all-time highs set this past December. Valuations have become much more attractive relative to its growth opportunities. Earnings per share (EPS) are projected to grow 13% in 2020 while its PE multiple is 14X, equal to the S&P 500. Typically, investor have to pay a significant premium for companies with revenue and earnings that are growing faster than the market.

We like UNH because it is one of the few stocks that has growth elements at a very reasonable prices. Furthermore, we are not worried about the potential political fallout that could affect the industry with higher payout requirements or lower premiums because UNH has flexibility to respond to whatever changes are imposed. They have a solid balance sheet, minimal debt and strong cash flow to position the company for long-term profitability. We are happy to have this name back into the portfolio, especially when its P/E, dividend rate and other valuation metrics are much more attractive than when we sold it back in 2016.

Home Depot has similar characteristics as UNH. HD has been operating in an industry that has come under pressure due to weak supply and demand fundamentals even as mortgage rates have fallen. While housing dynamics are broken down into regional components and markets, national economic trends do impact the overall industry. The biggest thorn in the side of housing has been oversupply, especially for entry-level homes. As more houses are listed on the market, prices fall especially with fewer consumers looking to buy. Although mortgage rates have been falling, making the overall cost of buying a home cheaper, first-time consumer buyers have had no appetite for plunging into home ownership. The softening home market has had a negative effect on Home Depot's stock price as it fell over 25% throughout the fall of 2018. After a sharp bounce in January, the stock once again fell over 6% throughout the late-winter and early Spring selling season due to weak fundamentals and weather.

We bought HD late in the spring once we noticed that sales (across most regions) had perked up, bringing the housing market closer to supply/demand equilibrium. According to realtor.com, an inventory correction should help support pricing throughout the summer and fall. Housing inventory is already declining as the number of for-sale listings declined in June as buyer interest bumped higher. This helps HD as 40% of revenues are generated from professional contractors who typically buy in bulk for better pricing. The other 60% is generated from the everyday customers who can be divided into "do-it-for-me" (those that initiate projects on their own and are willing to pay extra for installation services) and "do-it-yourself" (who prefer to buy raw materials and complete projects on their own).

Not only should improving industry fundamentals help the stock price, but HD expects to reap the benefits of implementing operational changes designed to create efficiencies in supply chain management and merchandising technologies. This will allow stores to expand omnichannel strategies in order to offer a variety of convenient pick-up and return options for customers, whether in-stores or online. These new policies will help HD compete with online and brick and mortar competitors while maintaining operating margins.

When we added HD to the portfolio, it had attractive growth opportunities and value characteristics. Its P/E ratio was below its 10-year median. The company's dividend yield was significantly higher than its 10-year average and had a price-to-free cash flow that was almost 30% cheaper than its peer group. Although Home Depot has a good bit of debt, it generates enough cash to more than cover its interest payments and dividends.

We feel Home Depot stands to benefit from improvements in the housing sector as well as internal efficiencies to drive profitability. The company has a strong management team which helps reduce execution risk while paying an above market dividend. We consider this a long-term anchor (core) holding and believe we will realize our target rate of returns.

We established an initial position in **Southwest Airlines (LUV)** after the stock fell over 15% from its fall 2018 highs. The stock dropped in the fall with the rest of the market on fears of a slowing global economy and the Fed embracing a tighter monetary policy. In the spring, investors priced in problems with the 737 Max and tighter equipment supply.

LUV's "point-to-point" low-cost, short-haul routes currently capture the largest percentage of U.S. domestic market travel of any of the major carriers. With fewer opportunities to add new routes that fit its strategy, the company is investing in new ways to stimulate top-line growth, such as international and longer-haul domestic routes. Even though these routes might temporarily pressure profit margins due to higher costs, we believe the management team will be able to integrate new strategies in a profitable manner.

We believe there is long-term value in LUV as they navigate through the ongoing supply issues associated with the 737 Max. The management team has maintained a conservative balance sheet with little debt and strong cash flow needed to support its interest payments, capital investment and dividends.

We expect the problems with the 737 Max will subside as the plane gets clearance to get back into the skies in the fall, which should alleviate much of the headwinds. Until then, short-term volatility might persist throughout the summer. Nonetheless, we see this as an opportunity to establish a position in a high-quality company.

They say timing is everything and nothing could be truer than our purchase of **Wynn Resorts (WYNN).** We bought shares in this high-end hotel and casino operator in mid-April after the company received two positive legal rulings that initially propelled the shares higher by 23%. Within the first two weeks in April, the Nevada Gaming Commission concluded their investigation into management

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