"Whether you think you can, or you think you can't, you are right."

Henry Ford

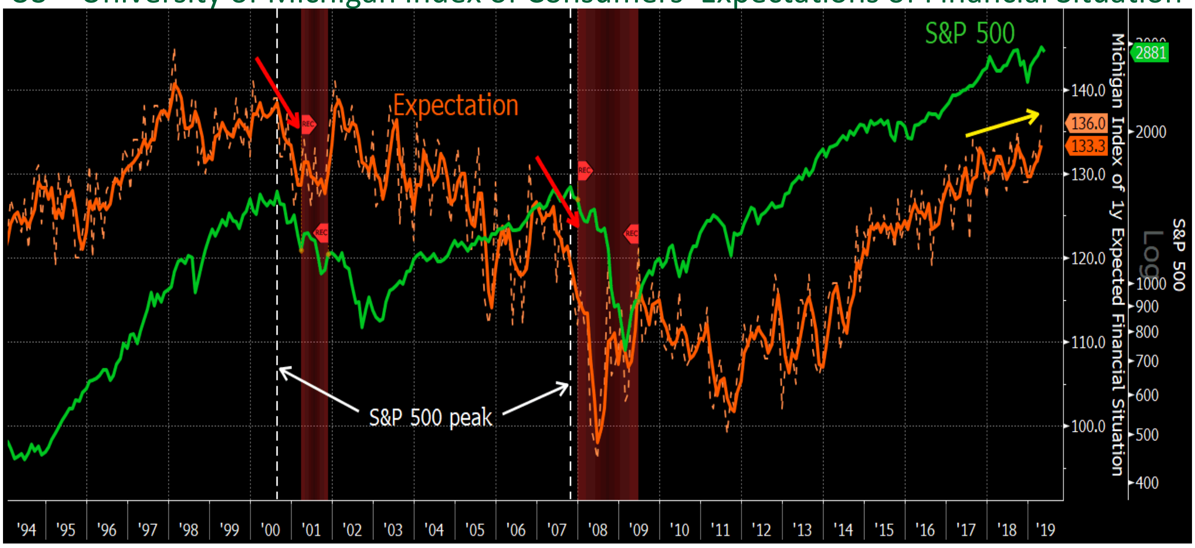
1. US CONSUMER

With the strong US economy consumption still makes up 69.4% of their GDP. Along with the comfort of continuing relatively constructive leading economic indicators, we also focus on the stability of consumer confidence.

US – Conference Board and University of Michigan Consumer Confidence Indices

Both the above consumer confidence indices have softened moderately recently but remain at elevated levels. With the Conference Board's index more volatile, the spread between the two series also provides valuable information (the green bars). This spread historically shrinks well before the upcoming recessions. It currently remains on a constructive course.

US – University of Michigan Index of Consumers' Expectations of Financial Situation



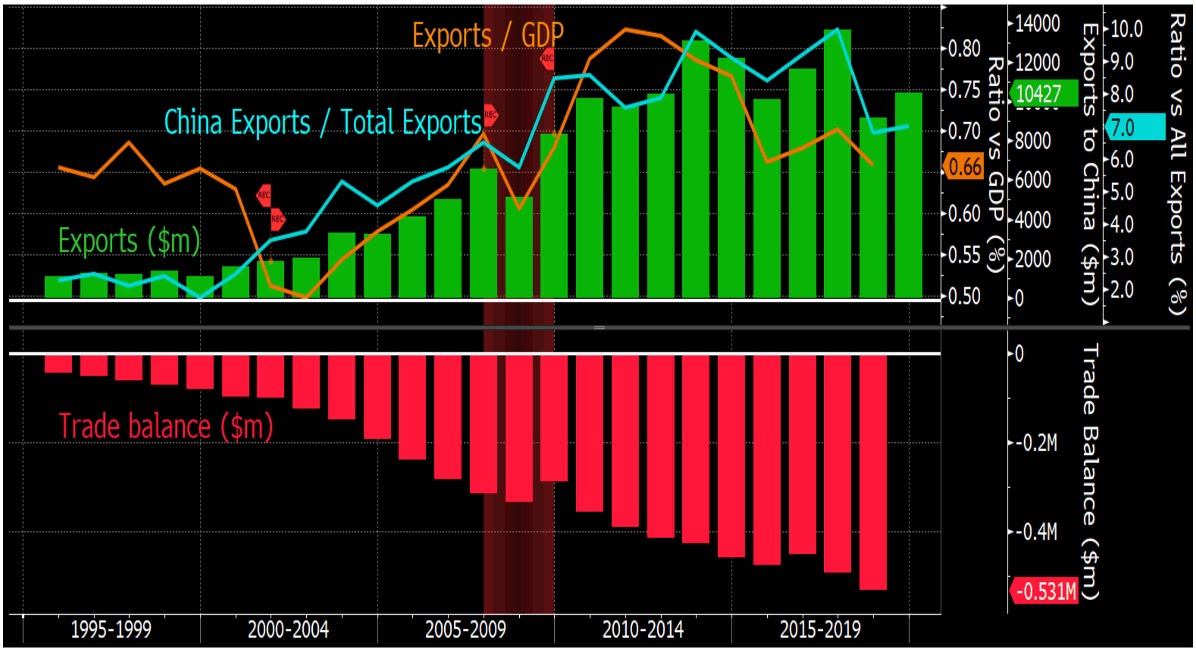
The University of Michigan also publishes an index of the public's expectations of their financial position a year forward. This index historically provided good early warnings against upcoming recessions (see the red arrows). It currently remains on a constructive course.

Source: Bloomberg & Stonehage Fleming Investment Management Limited. May 2019. Past performance should not be used as a guide to future performance.

2. US TRADE TARIFFS

The market is currently quite volatile because of renewed fears of inconclusive US-Sino trade tariff negotiations. The following chart reflects the US trade issues with China:

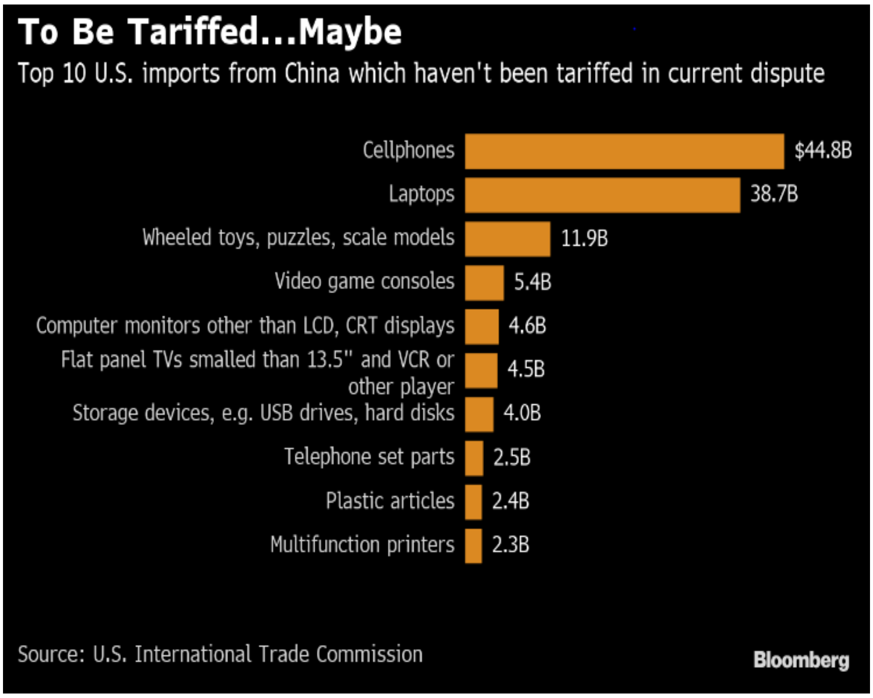
US – Data on Trade with China



The trade deficit with China is currently at a record level (the red bars). Exports to China in nominal terms (the green bars) are currently lower than they were in 2014. It make up only 0.66% of US GDP (the orange line) and only 7.0% of all the US exports (the blue line), whilst China is the world's second largest economy. Both these series are in receding trends.

Considering this data and trends between the world's two largest economies it becomes clear that we probably cannot expect President Trump to soften his stance in these negotiations (which now also seems to be the view of the Democratic Party). It may be that we should prepare for more volatility in this context.

This table shows the type of imported products that may be most affected in the US. New tariffs may affect predominantly consumer and business electronic products. The question obviously also becomes to what extent China will tax which US imports. The current indication is more towards agricultural imports, but we can expect a wider net to develop should negotiations fail to make good progress.



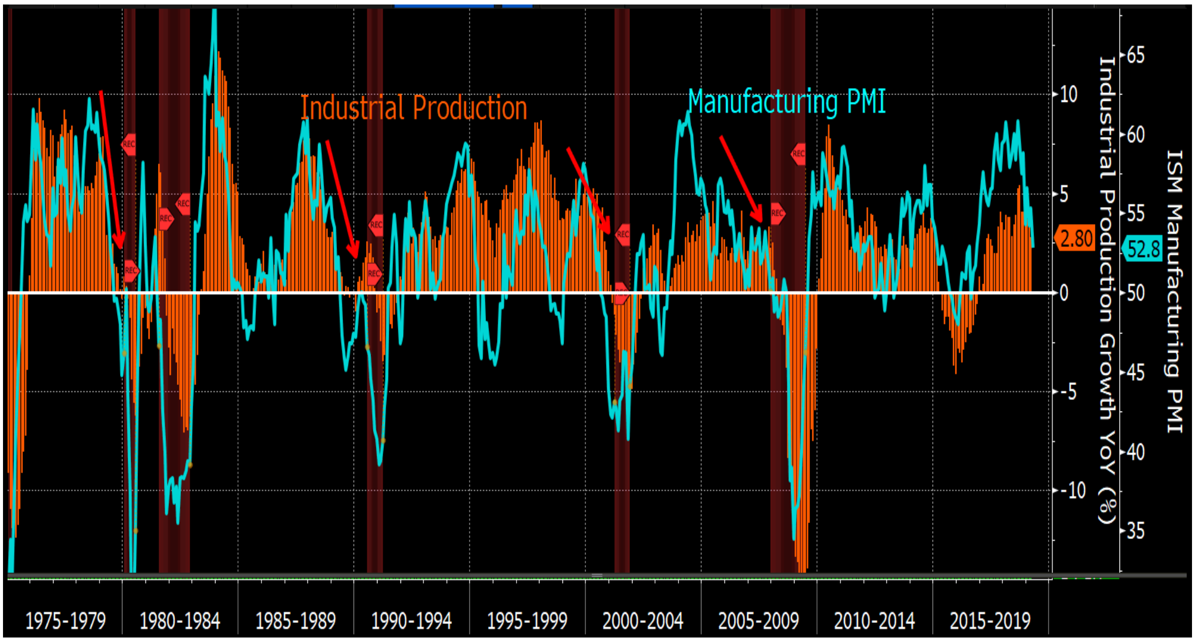
Whilst it is in the interest of both parties to reach agreement and we remain hopeful that one will be reached, we should continue to consider risks in the US manufacturing sector.

Source: Bloomberg & Stonehage Fleming Investment Management Limited. May 2019. Past performance should not be used as a guide to future performance.

3. US INDUSTRIAL PRODUCTION

Industrial production (manufacturing) makes up about 15% of the US economy. Despite this relatively small contribution, it can have a disproportional affect on the economy because of the higher volatility in this sector.

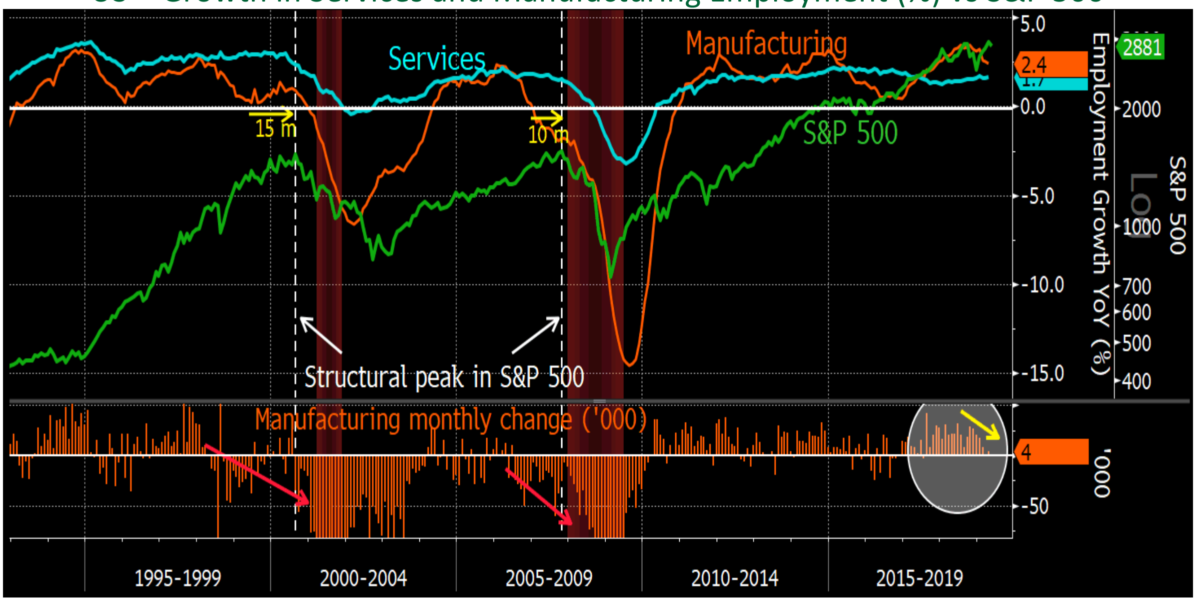
US – Growth in Industrial Production (%) vs ISM Manufacturing PMI



Industrial production is currently growing at a solid +2.8%, moderating somewhat from recent levels. Whilst the Manufacturing PMI index has dropped from the elevated levels in mid-2018, it remains well in constructive territory. We have a similarly constructive picture considering industrial production against the Conference Board's leading economic index.

Employment in the manufacturing sector is also a good barometer of the outlook for the US economy:

US – Growth in Services and Manufacturing Employment (%) vs S&P 500



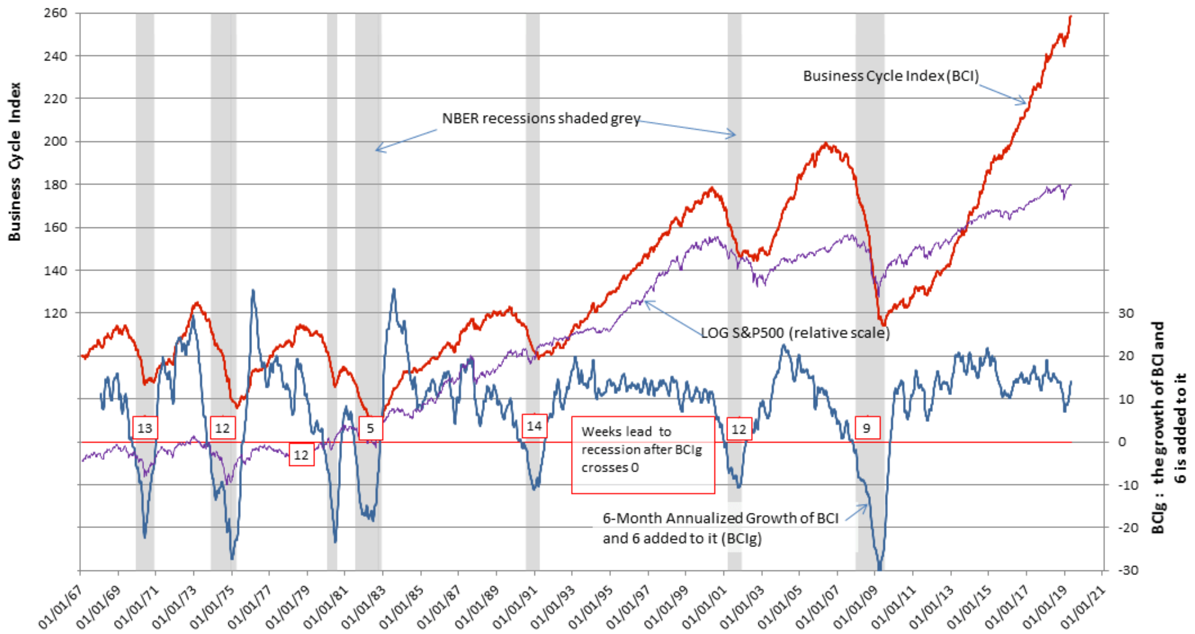
Total employment is currently growing at a healthy +1.8%. Services employment is growing at +1.7% and Manufacturing employment at +2.4%. The latter historically provided early warnings of structural stock market peaks and subsequent recessions when employment growth stagnated (the yellow arrows). We do not currently have such indications.

Source: Bloomberg & Stonehage Fleming Investment Management Limited. May 2019. Past performance should not be used as a guide to future performance.

4. US RECESSION WATCH

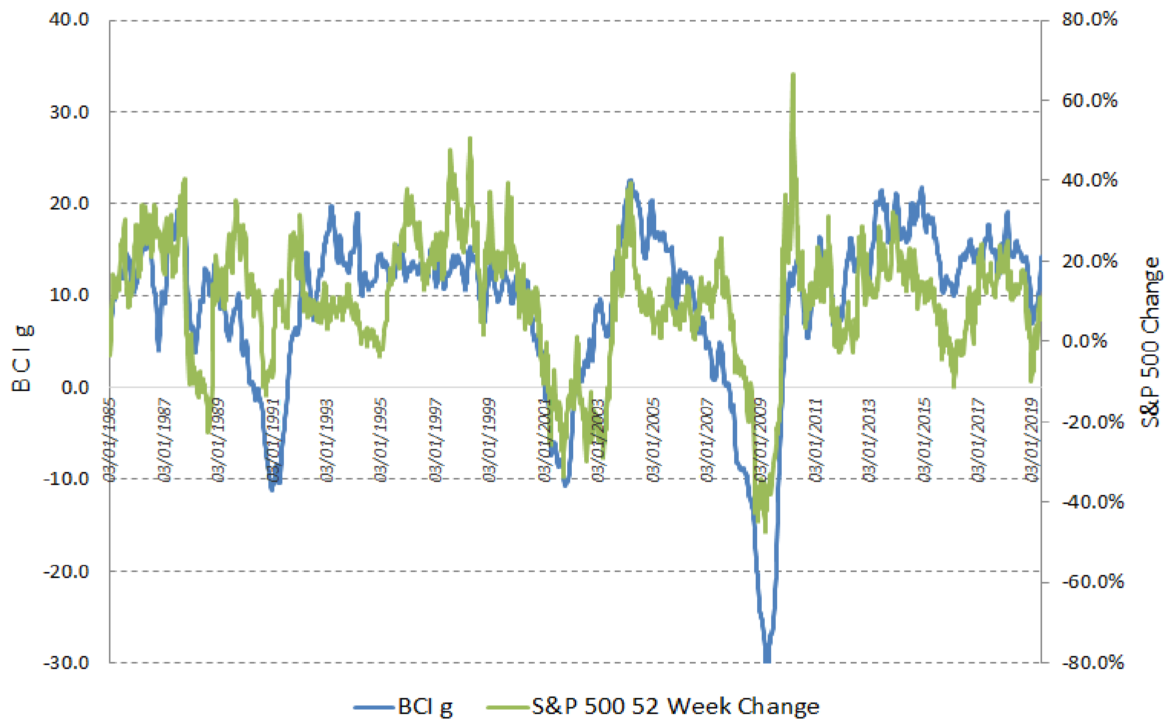
We follow several data series and service providers to understand the risks for an imminent recession and a structural peak in the stock market. The following chart provides valuable information in this context:

US – iM Business Cycle Index (BCI) and Growth (BCIg)



The above Business Cycle Index has a good record of foreseeing upcoming recessions well ahead of time (when its growth level matures, the blue line in the above chart drops to zero). The growth level has been in constructive territory for long and after some moderation earlier this year is currently accelerating to attractive levels.

BCI vs S&P 500



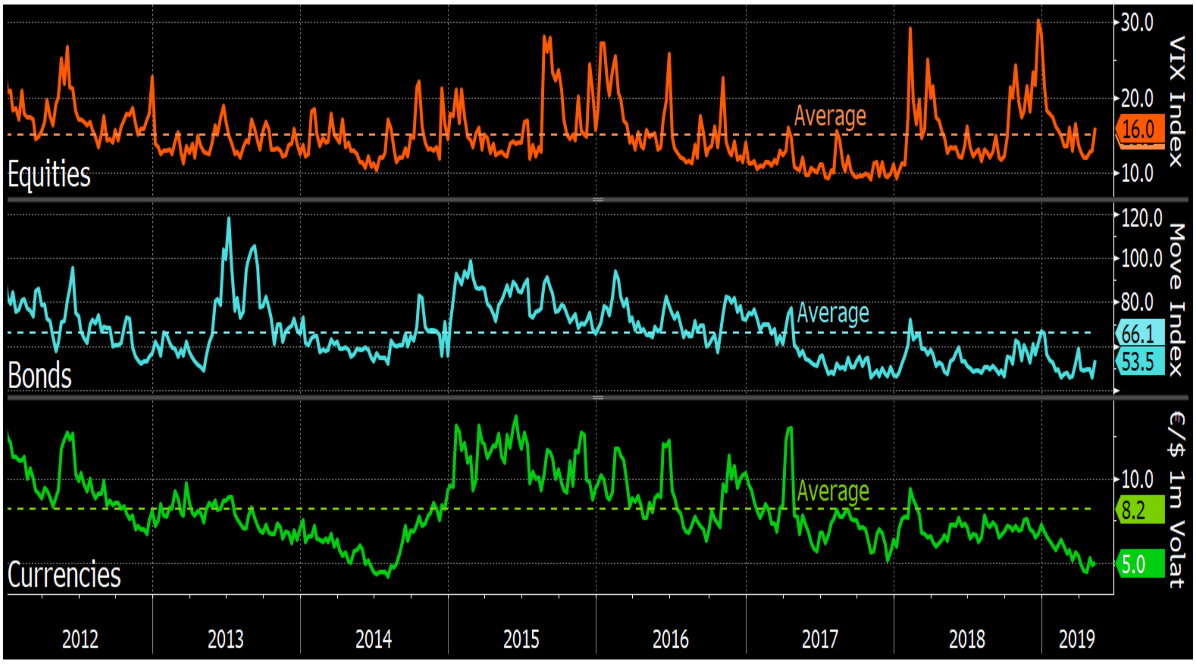
We have drawn the same BCIg chart (blue line in the above chart) along with the growth in the S&P 500 index (the green line). There is clearly a high correlation between these two series. We conclude from this analysis that the US market remains on a positive course.

Source: iM & Stonehage Fleming Investment Management Limited. May 2019. Past performance should not be used as a guide to future performance.

5. STABLE ENVIRONMENT

Apart from issues around the tariff negotiations the US capital market is currently relatively stable as reflected in the following chart:

US – Equity, Bond & Currency Market Volatility



The VIX Equity volatility index picked up to average levels last week but the Move Bond volatility index and the €/$ one-month volatility index are both close to their respective historic low levels. This reflects the stable US economic environment. Along with this, President Trump's approval rating (45.1%) is close to its peak level shortly after his inauguration.

We can realistically expect volatility to pick up from here, but in the interim this backdrop can put investors' mind to rest and provide the US Administration with some confidence in dealing with economic and political challenges.

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