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Monthly Market Review

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MARKET ENVIRONMENT 1Q19

Global Economy

The U.S. economy grew at a +2.2% pace in the fourth quarter, closing the year at +2.9% for the trailing twelve months. While there is some evidence of softening, data does not suggest that a recession is around the corner as corporate fundamentals remain solid, unemployment remains low and wages are rising. Overseas, the economic picture was more worrisome due to ambiguities regarding Brexit persist, Italy falling into recession, weak manufacturing numbers in Germany and the magnitude of the slowdown in China.

U.S.

- Fourth quarter real GDP growth slowed to +2.2%, due to
  - Softer consumer spending; rose 2.8% after a 4.0% gain in Q3
  - Lower government spending; edged up 0.4% after rising 2.6% in Q3
  - Slowing manufacturing; PMI down to 53.7 from 55.6 in Q3
- Corporate fundamentals solid, Unemployment remains low
  - After-tax profits moderated in Q4; EPS up 14% (y/y)
  - Business investment rose 6.2%, up from 2.5% in Q3; fueled by software and research department
  - Unemployment rate remained low at 3.8% in February
  - Wage growth at +3.4% (y/y) in February, fastest in a decade
  - Conference Board Consumer Confidence Index remained high
- Inflation remained benign
  - Headline CPI up 1.5% in February (y/y)
  - Less volatile Core CPI also rose by 2.1% as of February (y/y)
  - Headline PCE Deflator rose 1.4% as of January
- Housing starts drop again, led by single family homes
  - Housing starts in the US fell 8.7 percent from a month earlier, the largest decline in housing starts since last June
- Fed pauses the pace of rate hikes
  - Target rates unchanged at 2.25% – 2.50%
  - Fed fund futures now pricing in a 65% probability of a fed cut in 2019

Overseas

- Euro zone
  - GDP rose just 0.2% in Q4, the slowest pace since 2Q14
  - Core inflation rate stood at +1% y-o-y as of February
  - ECB announced a new bank lending program to support growth
  - Euro zone manufacturing extended its downtrend in February; PMI at lowest level since July 2013 and German manufacturing surprisingly weak
  - ECB further lowered GDP growth forecast from +1.7% to +1.1%
- U.K. economy slowed
  - GDP growth decelerated sharply to +0.2% in Q4 from +0.7% in Q3, as Brexit uncertainty weighed on business investment
  - Delay to Brexit beyond March 2019
  - Employment growth remained robust; nominal wages continued to pick up
- Japan's economy growth revised higher
  - Economy grew at +0.5% in Q4 (+1.9% annualized), supported by rebound in household consumption and an upward revision of business spending following a series of natural disasters
- The slowdown in China's economy continued
  - GDP growth slowed to 6.6% in 2018, at 28-year low; China also lowers its growth target to 6.0% - 6.5%
  - The profits of industrial companies fell 14% in the first two months of 2019 versus one year ago, worst since 2008

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Global Equity

The U.S. equity market erased the pain of fourth quarter as the S&P 500 rose 13.7% with double-digit gains across market cap and style spectrums. Non-U.S. developed markets and emerging markets equities also rebounded strongly in Q1, as concerns over the China-US trade dispute eased and major central banks grew more accommodative.

U.S. Equity

- S&P 500 Index gained 13.7% in Q1
  - Rebounded strongly from prior quarter's decline; 4Q18: -13.5%
  - Volatility remains relatively low; only a few trading days seeing market movement greater than 2% in either directions
  - With the P/E for the S&P 500 at 16.4x, equity multiples are slightly above their longer-term, 20-year average of 15.8x
  - All sectors finished in positive territory and most up by double digits with exception to financials and health care
  - Technology was the top performer in Q1 (+19.9%) but second worst performer in Q4 (-17.3%)
- Growth outperformed Value
  - R1000 Growth: +16.1% vs. R1000 Value: +11.9%
  - R2000 Growth: +17.1% vs. R2000 Value: +11.9%
- Small caps modestly outperformed large caps
  - R2000: +14.6% vs. R1000: +14.0%
- High-flying growth stocks "FAAMG" plus Netflix
  - Contribution to return: +22% (S&P 500); +33% (R1000 Growth)

	1Q19
Facebook	+27.2
Apple	+20.9
Amazon	+18.6
Microsoft	+16.6
Google (Alphabet Class C)	+13.3
Netflix	+33.2

Non-U.S. Equity

- Non-U.S. developed markets also rebounded significantly
  - ACWI ex-US: +10.3%; trailed S&P 500 by 330 bps
  - As in the U.S., nearly all sectors posted double digit gains except financials, utilities and communication services
  - U.K. (+11.9%) equities rallied, led by tech and select consumer goods companies ; Italy (+14.6%) rebounded strongly after a challenging Q4
  - Germany (+6.9%) up the least due to slowing manufacturing activities
- Local currencies were mixed against the US dollar
  - British pound, Russian ruble and Chinese yuan were up
  - Japanese yen, Swiss franc, Swedish krona and Turkish lira were down
- Equities in the emerging markets underperformed developed markets peers for the quarter by 0.4%
  - MSCI EM rose 9.9% with mixed country returns
  - China (+17.7%) was the top performing country in Q1, helped by the U.S.'s decision to suspended tariff hikes on $200 billion of Chinese goods
  - China A-shares (+33.0%) were particularly strong as MSCI announced plans to quadruple their weight in the index between May and November
  - Russia (+12.5%), Brazil (+8.1%), and India (+7.2%) were up
  - Turkey (-3.15%) posted negative returns as the government's unorthodox policy response to the country's economic problems continued

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Global Fixed Income

In the U.S., portions of the yield curve inverted, but spread between 2- and 10-year Treasury notes remained positive. Yields fell sharply in March as the market digested unexpectedly dovish comments from the Fed. Overseas, yields across developed markets fell on weaker economic data. And local currency emerging market debt was up modestly but outpaced by USD-denominated EM debt.

U.S. Fixed Income

- U.S. rates fell and portions of the yield curve inverted
  - 2-year U.S. Treasury Note declined 21 bps to close at 2.27%
  - 10-year Treasury Note finished at 2.41% after a 30 bps decrease
  - 30-year Treasury closed at 2.81%, down by 21 bps from Q4
  - Portions of the yield curve inverted but spread between the 2-year and 10-year Treasury note remained positive at 14 bps as of March
- Blmbg Barclays Aggregate rose 2.9% with investment grade corporates up the most
  - Bloomberg Barclays Corporate: +5.1%
- Breakeven inflation expectations up modestly
  - 10-year breakeven inflation rate up to 1.88% (3/31) from 1.71% (12/31)
  - Blmbg Barclays TIPS Index: +3.2%
- High yield corporates sored
  - Blmbg Barclays High Yield: +7.3%
  - The sector's yield-to-worst ended Q1 at 6.4% after surging to nearly 8% in Q4
- Municipal bonds helped by a favorable supply/demand backdrop
  - Blmbg Barclays Municipal Bond Index: +2.9%
  - Mutual funds absorbed roughly $24 billion in inflows, the best first quarter since data collection began in 1992

Non-U.S. Fixed Income

- Non-US developed bonds posted positive returns
  - Blmbg Barclays Global Agg ex-U.S. (unhedged): +1.5%
  - Blmbg Barclays Global Agg ex-U.S. (hedged): +3.0%
  - Interest rates in the global developed markets generally fell during the quarter
- Emerging market debt benefited from the reversal in risk appetite
  - JPM EMBI Global Diversified gained 7.0%; none of the index's 60+ countries delivering a negative result
  - JPM GBI EM Global Diversified rose 2.9%
  - Argentina: -10.5%
  - Turkey : -10.2%
  - Brazil: +2.3%
  - Mexico: +6.8%

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Real Assets

Real assets of all varieties enjoyed a strong first quarter of the year. The price of WTI was up over 30% through the end of March. MLPs and other listed infrastructure assets also saw a strong start to the year, posting double digit gains. Likewise, public real estate saw positive returns both in U.S. and Non-U.S. markets.

- Brent crude oil prices closed the quarter at $60.14/barrel, up by more than 30% since Q4
    - S&P 1200 Energy: +14.6%
    - Alerian MLP Index: +16.8%; helped by the buoyant price of oil

- Commodities broadly posted a more modest positive return
    - Bloomberg Commodity TR Index: +6.3%
        - Gains in Energy and Metals were offset by negative returns for Natural Gas and the Agriculture
        - Bloomberg Commodity Agriculture sub-index: -3.2%
    - GS Commodity Index: +15.0%
    - S&P Gold Spot Price Index: +1.3%

- Listed Infrastructure and Real Estate posted double digit gains
    - DJ-Brookfield Global Infrastructure Index: +15.7%
    - FTSE NAREIT: +16.3%
    - FTSE EPRA/NAREIT Global: +15.0%
- TIPS delivered a positive return
    - Bloomberg Barclays U.S. TIPS Index: +3.2%
    - 10-year breakeven inflation rate up to 1.88% (3/31) from 1.71% (12/31)

Disclosures

DISCLOSURES

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