May 4, 2018

What Happened in the Markets?

- US stocks reversed early losses to end the week on a strong note with the S&P 500 rising 1.3% to close at 2,663. All three of the major indices notched +1% gains; The Dow Jones gained 332 points (up 1.4%) and the tech-heavy NASDAQ composite rallied 1.7%.
- All eleven S&P sectors finished the day in the green, with mixed sector performance; the three best sectors were Tech (+2.0%), Staples (+1.4%) and Discretionary (+1.4%). Energy and Utilities were the biggest laggards, though they returned 0.5% and 0.4%, respectively.
- The notable piece of news on the day was the mixed jobs report released this morning. Though unemployment dropped to 3.9% to mark an 18-year low, non-farm payrolls came in at 164k, below expectations of 193k. Wage gains were also a bit softer than anticipated, with average hourly earnings rising 2.6% versus forecasts for 2.7%. The report failed to produce any meaningful movements in rates with the US 10-Year Treasury finishing the day flat at 2.95%.

Catalysts for Market Move

A strong end to the week for the S&P 500 with Friday’s 1.3% rally recovering much of the early week losses to see the index finish only slightly down for the week. After initially opening up lower this morning, the S&P 500 rallied throughout the day, bouncing off its 200-day moving average, which has been a key level of support for the index over the last couple of years. There were few directional drivers for today’s broad-based gains, in which all 11 sectors finished the day in the green; however attention this morning was on the jobs report release where numbers generally disappointed relative to expectations. Nonfarm payrolls rose 164k (vs 193k expected with prior months’ data revised up by a net of 30k), the unemployment rate hit an 18-year low at 3.9%, and wage growth disappointed, continuing its slow ascent at 2.6% year over year (vs. 2.7% expected). In trade news, the results from U.S. officials’ trip to China failed to produce any notable takeaways as of yet with the situation remaining fluid.

Meanwhile, earnings season is in the later stages with 408 companies of the S&P 500 having reported. Results have been stronger than anticipated with 73% of companies having reported better-than-expected revenues and 77% better-than-expected earnings. This has translated to aggregate year-over-year revenue growth of 8.7% and earnings growth of nearly 24% led by Energy, Financials, and Tech (with each sector posting EPS growth of greater than 26% thus far).

The Global Investment Committee’s Current Outlook

The GIC continues to recommend equities over fixed income given their constructive view on accelerating global economic and earnings growth, supportive financial conditions, the potential for global fiscal stimulus and cheap relative valuations. Investor sentiment and positioning for global equities became much more optimistic and full in January. The GIC believes we may have even entered the Euphoria stage they predicted—February was a reset and may set the stage for potential new highs by summer. The GIC prefers a barbell of positioning within equity portfolios—consider deep cyclical stocks, Financials and reasonably priced growth stocks. They expect ultra-defensive/low-volatility stocks to have a comeback this year as market participants consider the inevitable deceleration in growth in 2019. They favor dividend growth over dividend yield. The GIC thinks Japan still offers an attractive opportunity for both stock picking and beta plays levered to global recovery. They forecast a strengthening/flat yen and continue to recommend no currency hedging for Japanese equity positions. Many of the structural imbalances in emerging markets (EM) have improved. Concerns about EM from anti-trade “rhetoric” are increasing. Europe is tied to EM via its exports and banking system, and has strong long-term valuation support as fears of political risk and banking crisis remain too high. Organic earnings growth in Europe should outpace the US over the next several years and they do not recommend hedging currency risk for European equity investments. Within fixed income, the GIC recommends US-only positioning with no exposure to high yield and some TIPS as inflation expectations recover further with a stable/weaker dollar, rising oil prices and tighter labor. They remain underweight longer maturities and other interest rate-sensitive assets like REITs where there are also some signs of credit risk. The GIC still believes oil prices may surprise on the upside in 2H18 and maintains exposure via energy stocks and MLPs. Lastly, interest rates are likely to rise as inflation and growth expectations rise but then fall again in the second half, leaving high-quality fixed income investments with low, but positive returns for 2018. There may be a better time to add to duration later in 1H2018, in their view.

Market data provided by Bloomberg.

Dow Jones Industrial Average (DJIA): A price-weighted average of 30 blue-chip stocks that are generally the leaders in their industry.

NASDAQ Composite Index: A broad-based capitalization-weighted index of stocks in all three NASDAQ tiers: Global Select, Global Market and Capital Market.

S&P 500 Index: The Standard & Poor's (S&P) 500 Index tracks the performance of 500 widely held, large-capitalization US stocks.

US Trade-Weighted Dollar Index: A weighted average of the foreign exchange value of the US dollar against a subset of the broad index currencies that circulate widely outside the US.

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Master Limited Partnerships (MLPs) are limited partnerships or limited liability companies that are taxed as partnerships and whose interests (limited partnership units or limited liability company units) are traded on securities exchanges like shares of common stock. Currently, most MLPs operate in the energy, natural resources or real estate sectors. Investments in MLP interests are subject to the risks generally applicable to companies in the energy and natural resources sectors, including commodity pricing risk, supply and demand risk, depletion risk, exploration risk and interest rate risk.

Bonds are subject to interest rate risk. When interest rates rise, bond prices fall; generally the longer a bond's maturity, the more sensitive it is to this risk. Bonds may also be subject to call risk, which is the risk that the issuer will redeem the debt at its option, fully or partially, before the scheduled maturity date. The market value of debt instruments may fluctuate, and proceeds from sales prior to maturity may be more or less than the amount originally invested or the maturity value due to changes in market conditions or changes in the credit quality of the issuer. Bonds are subject to the credit risk of the issuer. This is the risk that the issuer might be unable to make interest and/or principal payments on a timely basis. Bonds are also subject to reinvestment risk, which is the risk that principal and/or interest payments from a given investment may be reinvested at a lower interest rate. **Bonds rated below investment grade** may have speculative characteristics and present significant risks beyond those of other securities, including greater credit risk and price volatility in the secondary market. Investors should be careful to consider these risks alongside their individual circumstances, objectives and risk tolerance before investing in high-yield bonds. High yield bonds should comprise only a limited portion of a balanced portfolio. **Treasury Inflation Protection Securities' (TIPS)** coupon payments and underlying principal are automatically increased to compensate for inflation by tracking the consumer price index (CPI). While the real rate of return is guaranteed, TIPS tend to offer a low return. Because the return of TIPS is linked to inflation, TIPS may significantly underperform versus conventional U.S. Treasuries in times of low inflation.

Duration, the most commonly used measure of bond risk, quantifies the effect of changes in interest rates on the price of a bond or bond portfolio. The longer the duration, the more sensitive the bond or portfolio would be to changes in interest rates. Generally, if interest rates rise, bond prices fall and vice versa. Longer-term bonds carry a longer or higher duration than shorter-term bonds; as such, they would be affected by changing interest rates for a greater period of time if interest rates were to increase. Consequently, the price of a long-term bond would drop significantly as compared to the price of a short-term bond.

Investing in commodities entails significant risks. Commodity prices may be affected by a variety of factors at any time, including but not limited to, (i) changes in supply and demand relationships, (ii) governmental programs and policies, (iii) national and international political and economic events, war and terrorist events, (iv) changes in interest and exchange rates, (v) trading activities in commodities and related contracts, (vi) pestilence, technological change and weather, and (vii) the price volatility of a commodity. In addition, the commodities markets are subject to temporary distortions or other disruptions due to various factors, including lack of liquidity, participation of speculators and government intervention.

Physical precious metals are non-regulated products. Precious metals are speculative investments, which may experience short-term and long term price volatility. The value of precious metals investments may fluctuate and may appreciate or decline, depending on market conditions. If sold in a declining market, the price you receive may be less than your original investment. Unlike bonds and stocks, precious metals do not make interest or dividend payments. Therefore, precious metals may not be suitable for investors who require current income. Precious metals are commodities that should be safely stored, which may impose additional costs on the investor. The Securities Investor Protection Corporation ("SIPC") provides certain protection for customers' cash and securities in the event of a brokerage firm's bankruptcy, other financial difficulties, or if customers' assets are missing. SIPC insurance does not apply to precious metals or other commodities.

Equity securities may fluctuate in response to news on companies, industries, market conditions and general economic environment.

Companies paying **dividends** can reduce or cut payouts at any time.

REITs investing risks are similar to those associated with direct investments in real estate: property value fluctuations, lack of liquidity, limited diversification and sensitivity to economic factors such as interest rate changes and market recessions.

Value investing does not guarantee a profit or eliminate risk. Not all companies whose stocks are considered to be value stocks are able to turn their business around or successfully employ corrective strategies which would result in stock prices that do not rise as initially expected.

Growth investing does not guarantee a profit or eliminate risk. The stocks of these companies can have relatively high valuations. Because of these high valuations, an investment in a growth stock can be more risky than an investment in a company with more modest growth expectations.

Yields are subject to change with economic conditions. Yield is only one factor that should be considered when making an investment decision.

Because of their narrow focus, **sector investments** tend to be more volatile than investments that diversify across many sectors and companies. **Technology stocks** may be especially volatile.

Asset allocation and diversification do not assure a profit or protect against loss in declining financial markets.

The **indices** are unmanaged. An investor cannot invest directly in an index. They are shown for illustrative purposes only and do not represent the performance of any specific investment.

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