# April 2018 Month-End Review

## Key Takeaways

U.S. and international equities markets finished April within 1.0% of where they began the year as improved earnings were not enough to overcome the market's perception of increased risk. S&P disclosed that 78% of the S&P 500 reporting results beat earnings estimates in the first quarter of 2018.

Oil prices surged to their highest level since 2014, ending the month at $68.57. Energy equities jumped 9.4% in April, far outpacing all other sectors.

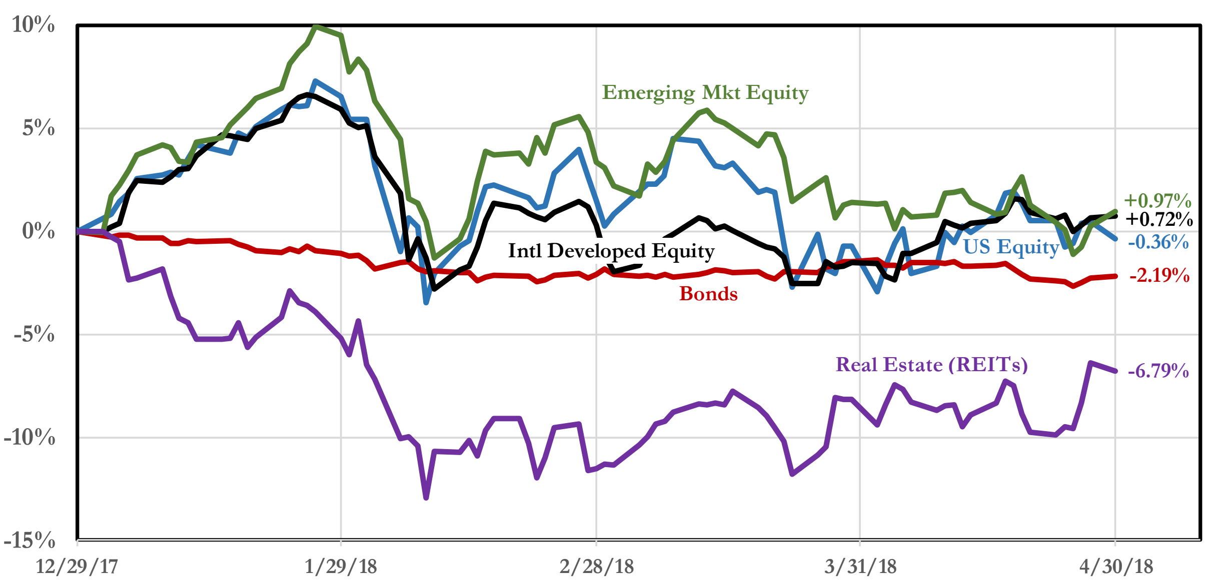
Bond prices moved lower as the 10-yr Treasury briefly touched 3.0% in late April. Real estate continued to recover after February's heavy sell-off.

The composition of returns changed in April, breaking 15-month trends. Large-cap growth stocks trended lower and the dollar strengthened. International stocks gained in local currency terms and lost in currency conversion. Emerging markets were the poorest performer of our 3 major equity markets.

### Table 1: Benchmark Index Performance as of April 30, 2018

| ***Benchmark Index*** | ***1 Mo*** | ***YTD*** | ***2017*** | ***5 Year*** |
|---|---|---|---|---|
| Domestic Equities (S&P 1500 Composite) | 0.36% | -0.36% | 21.1% | 12.9% |
| International Developed Equities (MSCI EAFE) | 2.28% | 0.72% | 25.0% | 5.9% |
| Emerging Market Equities (MSCI EM) | -0.44% | 0.97% | 37.3% | 4.7% |
| Fixed Income (Bloomberg Barclays US Aggregate) | -0.74% | -2.19% | 3.5% | 1.5% |
| US Real Estate (S&P US REIT Index) | 1.49% | -6.79% | 4.3% | 4.6% |
| Global Equities (MSCI ACWI) | 0.95% | -0.02% | 24.0% | 8.8% |

### Chart 1: Market Index Performance through April 30, 2018



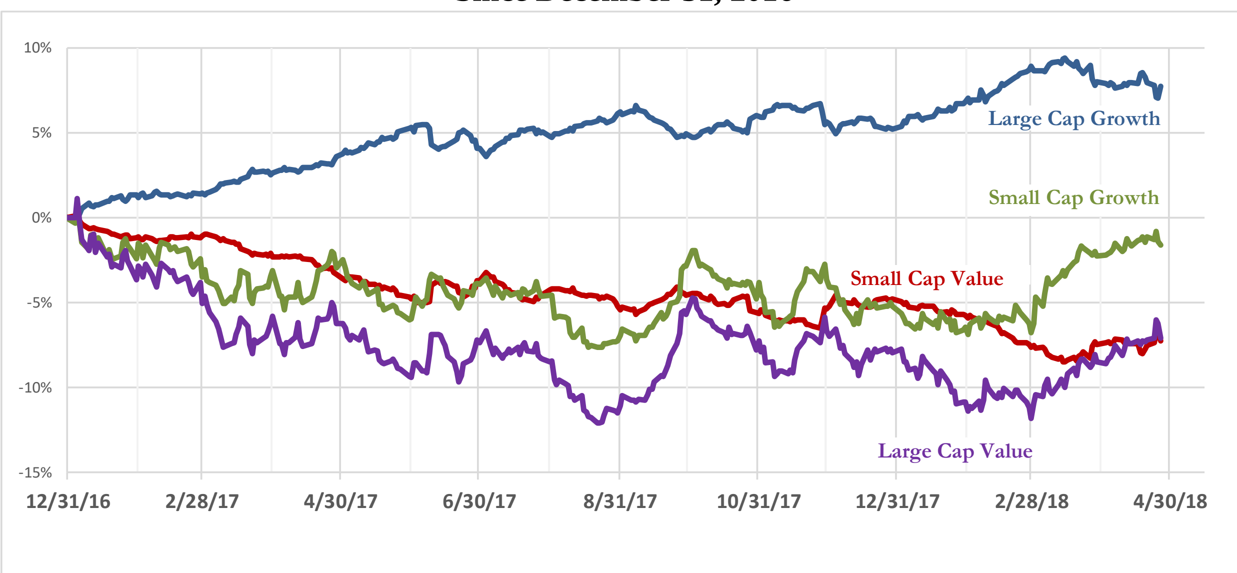
## U.S. Market Review

In U.S. equity markets, stocks were relatively unchanged in April despite strong earnings reports. S&P reported that 217 issues out of the 279 that have reported in the S&P 500 beat earnings estimates in the first quarter. If you liked stocks at the beginning of 2018, then you should love them now.

The overall source and composition of stock returns changed in April. Large-cap growth stocks, which have been leading the U.S. market forward since the beginning of 2016, took a break in April as depicted in Chart 2 below. The initial selloff started in mid-March with a drop in Facebook as data privacy concerns caused Facebook to drop 18% through mid-April. Eventually that fear aroused an overall drop in high P/E tech stocks as well. The FAANG stocks (Facebook, Amazon, Apple, Netflix, and Google) all suffered in late March and early April as investors pulled back from steep valuations. Then, in late April, Facebook, Amazon, Apple, and Netflix reported earnings that topped expectations and reinforced their high valuations. Those stocks have recovered some, but not all, of their April losses. Another set of "buy-despite-the-high-valuation" stocks, biotechs, also dropped in late March and early April but did not capture the bounceback that techs enjoyed.

While large-cap growth stocks were having difficulties, oil stocks surged forward in April as oil traded at 3-year highs and investors rediscovered their cheap valuations. S&P reported that the Energy sector in the S&P 500 was up 9.4% in April while Consumer Discretionary, the second-best sector, was up 2.4%. Small-cap stocks, especially small-cap growth stocks, continued to rally in April after outperforming in March.

**Chart 2: U.S. Equity Performance as a Percentage of Overall Market Performance Since December 31, 2016**



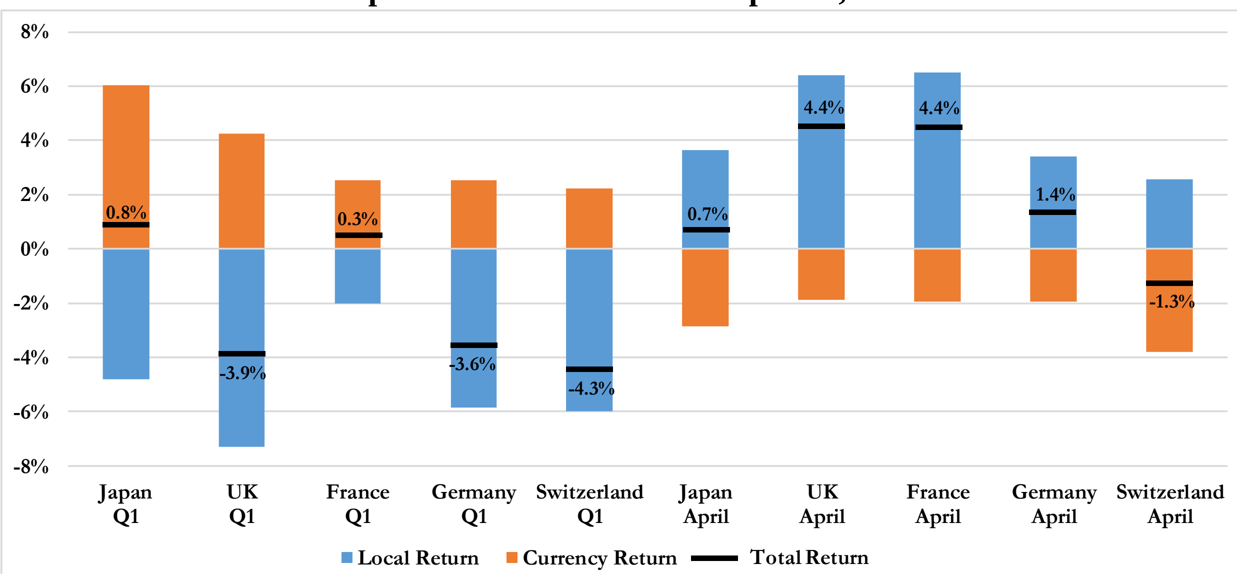

Source: Standard and Poors

## International Equity Markets

International developed equity markets as represented by the MSCI EAFE (Europe, Australasia, and Far East) Index were up 2.3% for the month, generally due to strong performance in local markets but hindered by the currency effects of a weaker dollar. Chart 3 below illustrates market performance statistics in 2018 for the top 5 EAFE countries. Orange bars indicate equity market returns in local currency terms, blue bars indicate currency returns to U.S. dollars and the black bar indicates total return. Note in Chart 3 that the left half of the chart reflects first quarter 2018 performance while the right half of the chart denotes April 2018 performance. In the first quarter of 2018 negative local market returns were offset by substantial currency gains. In April, however, strong local market returns were hurt by currency losses.

We continue to believe that EAFE equities are relatively cheap with P/E ratios in the 13.3 to 14.0X range but we are concerned that the 15-month weakening trend in the dollar is over. European economies, while strong, have seen indications of a moderation in growth rates and a small reduction in already-low inflation rates. With this as a backdrop, expectations for the European Central Bank's exit from their Quantitative Easing program are getting pushed out. We are maintaining our asset allocations and evaluating currency-hedged ETFs and funds.

**Chart 3: Comparison of the Breakdown of Equity Returns in U.S. Dollar Terms**
**Top 5 EAFE Countries as of April 30, 2018**




Source: MSCI, Federal Reserve

Emerging market equities lost 0.44% in April, barely holding on to the title of best performing asset class in 2018. One reason for the value decrease was fears about a trade war after President Trump placed higher tariff rates on steel and aluminum imports from China and threatened more tariff actions with other goods. We are skeptical that a "trade war" will have much of a lasting effect on aggregate equity prices.

Emerging markets also contended with a strengthening U.S. dollar. While most emerging economies are strong enough to handle the new environment, other economies (such as Turkey and Argentina) are struggling to adjust. We think lower prices represent a buying opportunity but we are closely watching developments in this space.

## Bond Market Review and Outlook

U.S. bonds extended their weak performance as the 10-year Treasury briefly touched 3.0%. During April two-year Treasuries increased 22bp to 2.49% and ten-year Treasuries increased 21bp to 2.95%.

Investors should always remember that short-term interest rates are determined by Federal Reserve policy actions while long-term interest rates are most influenced by inflation expectations. As expected, the Federal Reserve maintained the Fed Funds rate at 1.50% to 1.75% at the FOMC meeting on May 2nd. The FOMC also did nothing to contradict the market's expectation that the FOMC will raise rates another 25 bp in June. Interest rates will continue to encounter pressure from monetary policy actions, higher inflation expectations due to tight labor markets, and increased issuance due to deficit funding.

While higher interest rates are a negative for long bond values, they are a boon for cash holders. For the first time since the 2008 financial crisis, holders of cash can now earn a decent return. We recommend rolling short Treasury Bills to earn returns of 1.65% or more.

## Real Estate Market Review and Outlook

Real estate markets continued their recovery off their February lows. While we see value in this sector given the much cheaper valuations we also are concerned that it will trade off substantially – again – if interest rates rise. We are maintaining our real estate exposure at this time.

**Ed Yale, CFA**

**President and Chief Investment Advisor**

**May 2018**