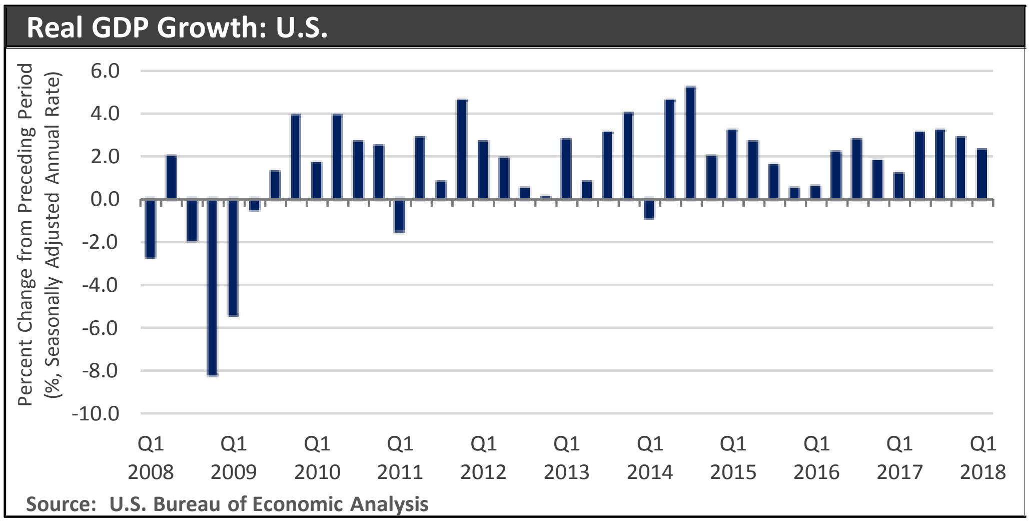
# MONTHLY UPDATE AND COMMENTARY
## MAY 2018

**Recap:** Over the past few years, first-quarter growth has slowed notably from the fourth quarter, often attributing to residual seasonality. This year has been no exception as first-quarter growth came in at 2.3% (annualized) – slower than the 2.9% recorded in the fourth quarter. Economic activity has been supported by improved business investment and an unexpectedly small positive contribution from net trade.

Following a 4% annualized expansion in the fourth quarter that was partly boosted by post-hurricane recovery spending, consumer spending slowed markedly, contributing just a measly 0.7 percentage points to growth. Consumer spending should regain a firmer footing ahead, buoyed by upbeat consumer confidence, a healthy labor market and tax cuts.




There should still be time for the U.S. and China to settle their trade differences without much collateral damage – something that would appear more likely now with trade talks scheduled with China. However, there is still a possibility that talks could fail and tariffs could be implemented, with this scenario expected to weigh on economic growth.

**Inflation:** The headline consumer price index (CPI) was down 0.1% (month-over-month) in March, as a decline in gasoline prices weighed on the headline number. Core inflation rose 0.2% in the month, matching February's pace. Also, as expected, the year-over-year pace of core inflation jumped back up above 2.0% in March to 2.1%. Inflation, after being dormant much of last year, has again risen steadily toward the Federal Reserve's goal of 2%.

Businesses have increasingly faced rising input costs for both labor and raw materials, and with declining unemployment, strong economic growth, and the risk of further tariffs, this trend looks set to continue. It is likely only a matter of time before companies pass these higher costs on to consumers, ultimately pushing inflation higher.

Core inflation should continue to rise as a strong economy, wage pressure, consumer spending and new tariffs increasingly filter through the economy putting pressure on prices

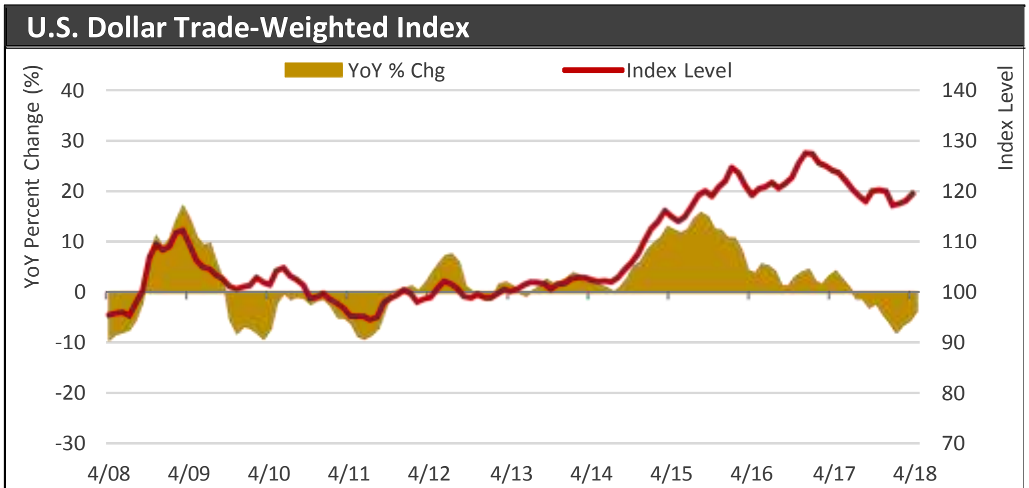
**Housing:** Housing starts also posted a decent rebound in March, rising by 1.9%. The details were slightly softer than suggested by the headline. The gain was concentrated in the volatile multi-family segment, while single-family starts declined. For the first quarter homebuilding outperformed expectations; however, it remained low relative to underlying demand and history. Even though economic fundamentals remained strong, a shortage of workers and available building lots, as well as risings costs of labor and materials, continued to weigh on homebuilding activity. These headwinds contributed to tight inventory of houses on the market.

Housing starts are expected to continue gaining ground through 2018, supported by positive fundamentals expected to offset likely higher mortgage rates.

**Retail Sales:** After three lackluster months, retail sales jumped 0.6% in March and the core measure rose by 0.4%. March was the first full month where taxpayers would have felt the impact of tax cuts in their paychecks, raising the bar for retail sales. Consumers responded to higher after-tax income by ramping up spending on most categories of products, particularly on discretionary and big-ticket items, as well as at online retailers.

**Dollar:** The U.S. currency posted its fifth straight quarterly loss in the first three months of the year, puzzling investors who bet the dollar would benefit from corporations repatriating cash in the wake of tax cuts signed into law late last year.

Uncertainty over U.S. policy, the risks of a global trade war and an acceleration in growth abroad would mean more declines are likely in store for the dollar. If the dollar falls too rapidly, however, that could shake faith in the U.S. economy and complicate the Fed's plans to tighten monetary policy. An extended fall also could raise inflation and spark concerns that consumer prices would rise too quickly.



Source: Board of Governors of the Federal Reserve System

The threat of a trade war has certainly not had a constructive impact on the dollar. Also weighing on the dollar has been a global economic upswing that has encouraged central bankers in Europe and Asia to take the first steps toward normalizing monetary policy after years of expansive support.

**Euro Zone:** The European Central Bank has fretted about the risk of trade wars and a stronger euro just as data suggested the eurozone's long-awaited economic recovery was losing some speed. Industrial production in the currency union unexpectedly fell in February, marking a third straight month of declines. Other recent indicators pointing to a slowdown included surveys of purchasing managers at manufacturers and service providers, retail sales data, and barometers of confidence among households and businesses.

Some of the weakness has reflected temporary factors that shouldn't hurt growth in the months to come, including a spell of unusually cold weather across Europe and strikes among German metal and electrical workers. That said, there have been other threats to the region's export-focused economy, including possible trade conflicts triggered by the U.S. administration, volatile financial markets and the U.K.'s withdrawal from the European Union.

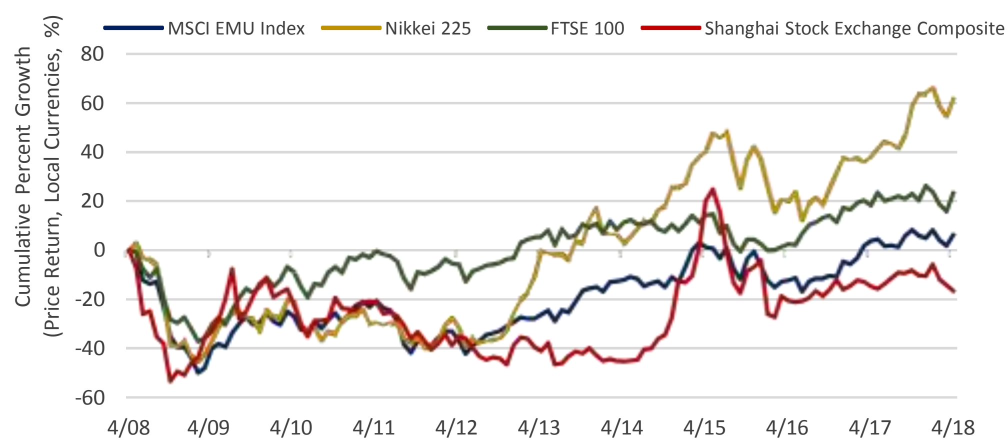
The ECB is likely to phase out Quantitative Easing, currently running at €30 billion a month, by the end of 2018, and start raising interest rates in the second half of 2019. The ECB will move cautiously to phase out its giant bond-buying program and follow the Federal Reserve in raising interest rates.

**Global Investing:** Stock-market investors, already grappling with the tech rout and the threat of a trade war, have started to reassess a fundamental premise of the powerful rally—that world-wide economic growth is on the verge of blasting out of a long period of weakness. The world's major economies started to pick up steam together last year, in a break from years of sluggish post-crisis growth in which the U.S. often seemed like the lone bright spot. But recently, the global economic comeback has been in a bit of a rut. Investor confidence has been flagging alongside the Trump administration's increasingly protectionist bent and China's vow to retaliate, raising concerns that a trade spat will undermine growth.

Global financial markets have also started to reflect a more pessimistic view of the economy. The differential between short- and long-term U.S. Treasury yields, which tended to grow and shrink alongside the economy's prospects, has been at its narrowest in more than a decade. Manufacturing activity was down in March from the previous month in 21 of 30 countries, led by declines in Asia and Europe. Though there's little fear of an imminent global recession, the less-than-stellar numbers have forced investors to reconsider global growth.

For U.S. investors, much of the economic outlook has hinged on trade. A trade war could have massive repercussions, such as posing new challenges for the production of American goods or sparking declines in foreign demand. Even a prolonged threat could cause some companies to hold off on investment until they have more clarity.

**Stock Market Percent Growth (10 Years)**




Source: MSCI, Nikkei, FTSE, China Securities Index Co.

However, even if economic growth moderated, that would not necessarily be a bad sign for stocks. Major U.S. indexes have managed to reach scores of record highs during the current bull market, based partly on the premise that the economy is neither too hot to risk overheating nor too cold to fall into a recession.

But questions about global growth have come at a time when investors are already on edge about central banks' withdrawal of monetary stimulus. Additionally, the U.S. government has been ramping up borrowing to fund a widening budget deficit and a $1.5 trillion tax overhaul. As the Federal government borrows and the Fed trims, less money will be available for stocks and other risky assets.

**Outlook:** The fundamentals of the U.S. economy certainly support continued momentum. The unemployment rate has held at a 17-year low since October. The tight labor market is finally starting to drive faster wage growth indicating an improvement in consumer power with wage gains outstripping inflation. These dynamics speak to underlying strength of consumer fundamentals, even before income tax cuts feed through.

Consumer spending is expected to run roughly 2.9% in real terms after the Q1 soft patch, boosted by tax cuts. With workers becoming scarce, businesses have resorted to ramping up investment. This is an encouraging sign that stronger productivity growth may be just around the corner.

There are concrete signs that inflation has firmed, on the merits of an economy with little spare capacity. In fact, the Fed's preferred inflation gauge, the core PCE deflator, has run at a 2.1% annualized pace over the past three months. As the temporary factors weighing on inflation in 2017 fade, price growth will accelerate. Now, new tariffs and fiscal stimulus will tilt the balance of risks for inflation to the upside.

With respect to America's major trading partners, underlying inflation dynamics have improved in a majority of advanced economies over the last year, but in most cases are still lagging behind the U.S. rate. Layering on the fact that tax reform improves U.S. competitiveness relative to its peers and tariffs incentivize production inside America's borders, discretion from other central banks seems prudent. The Fed has a tricky balancing act in weighing how quickly to raise interest rates given the uncertainty about how the economy will respond to tax cuts and spending increases.

**Sources:** Department of Commerce, Department of Labor, Institute for Supply Management.

## Index Performance as of 4/30/18

| | 1 Week | 1 Month | QTD | 3 Month | YTD | 1 Year | 3 Year | 5 Year |
|---|---|---|---|---|---|---|---|---|
| **Russell** | | | | | | | | |
| **3000 Value** | -0.93 | 0.43 | 0.43 | -5.85 | -2.40 | 7.42 | 7.77 | 10.50 |
| **3000** | -0.88 | 0.38 | 0.38 | -5.26 | -0.27 | 13.05 | 10.20 | 12.75 |
| **3000 Growth** | -0.83 | 0.33 | 0.33 | -4.70 | 1.82 | 18.78 | 12.60 | 14.97 |
| **1000 Value** | -0.94 | 0.33 | 0.33 | -6.14 | -2.51 | 7.50 | 7.66 | 10.52 |
| **1000** | -0.84 | 0.34 | 0.34 | -5.54 | -0.35 | 13.17 | 10.25 | 12.84 |
| **1000 Growth** | -0.76 | 0.35 | 0.35 | -4.96 | 1.77 | 18.96 | 12.84 | 15.13 |
| **Mid Cap Value** | -0.70 | 0.50 | 0.50 | -4.22 | -2.02 | 6.83 | 7.81 | 10.97 |
| **Mid Cap** | -0.92 | -0.15 | -0.15 | -4.22 | -0.61 | 11.17 | 8.28 | 11.77 |
| **Mid Cap Growth** | -1.19 | -0.94 | -0.94 | -4.21 | 1.21 | 16.87 | 9.08 | 12.76 |
| **2000 Value** | -0.85 | 1.73 | 1.73 | -2.16 | -0.95 | 6.53 | 9.27 | 10.36 |
| **2000** | -1.28 | 0.86 | 0.86 | -1.79 | 0.78 | 11.54 | 9.64 | 11.74 |
| **2000 Growth** | -1.67 | 0.10 | 0.10 | -1.44 | 2.40 | 16.60 | 9.89 | 13.07 |
| **Standard & Poors** | | | | | | | | |
| **S&P 500** | -0.82 | 0.38 | 0.38 | -5.77 | -0.38 | 13.27 | 10.57 | 12.96 |
| **Consumer Disc** | 0.50 | 2.36 | 2.36 | -3.49 | 5.53 | 16.82 | 13.09 | 15.53 |
| **Consumer Staples** | 0.05 | -4.32 | -4.32 | -12.52 | -11.13 | -6.14 | 4.17 | 7.01 |
| **Energy** | 0.01 | 9.36 | 9.36 | -0.86 | 2.92 | 12.43 | -0.40 | 1.57 |
| **Financials** | -1.49 | -0.37 | -0.37 | -7.32 | -1.32 | 18.60 | 14.11 | 14.75 |
| **Health Care** | -0.24 | 1.22 | 1.22 | -6.25 | -0.02 | 10.91 | 6.50 | 13.57 |
| **Industrials** | -4.38 | -2.79 | -2.79 | -9.13 | -4.31 | 8.85 | 10.62 | 13.55 |
| **Information Technology** | -0.71 | 0.09 | 0.09 | -3.72 | 3.62 | 24.65 | 19.01 | 20.46 |
| **Materials** | -3.11 | 0.15 | 0.15 | -9.14 | -5.37 | 9.18 | 6.37 | 9.79 |
| **Real Estate** | 2.01 | -0.62 | -0.62 | -3.79 | -5.61 | 0.95 | 4.70 | 5.73 |
| **Telecom Services** | -2.26 | -0.98 | -0.98 | -8.89 | -8.39 | -2.58 | 2.42 | 2.52 |
| **Utilities** | 2.45 | 2.10 | 2.10 | 1.85 | -1.27 | 3.22 | 9.06 | 8.35 |
| **Other U.S. Equity** | | | | | | | | |
| **Dow Jones Industrial Avg.** | -1.17 | 0.34 | 0.34 | -7.09 | -1.63 | 18.09 | 13.44 | 12.97 |
| **Wilshire 5000 (Full Cap)** | -0.88 | 0.53 | 0.53 | -5.25 | -0.17 | 13.02 | 10.02 | 12.58 |
| **International Equity - Broad Market** | | | | | | | | |
| **MSCI EAFE** | 0.09 | 2.28 | 2.28 | -4.09 | 0.72 | 14.51 | 4.94 | 5.90 |
| **MSCI EM** | 0.56 | -0.44 | -0.44 | -6.80 | 0.97 | 21.71 | 6.00 | 4.74 |
| **MSCI Frontier Markets** | -0.71 | -3.15 | -3.15 | -3.73 | 1.79 | 21.84 | 5.45 | 7.18 |
| **MSCI ACWI** | -0.33 | 0.95 | 0.95 | -5.36 | -0.02 | 14.16 | 7.43 | 8.80 |
| **MSCI ACWI Ex USA** | 0.24 | 1.60 | 1.60 | -4.90 | 0.40 | 15.91 | 5.01 | 5.46 |
| **MSCI AC Asia Ex Japan** | 1.19 | 0.71 | 0.71 | -5.75 | 1.38 | 24.01 | 6.95 | 7.98 |
| **International Equity - Country Region** | | | | | | | | |
| **MSCI Brazil** | -0.69 | -3.99 | -3.99 | -7.66 | 7.88 | 21.38 | 9.39 | -1.38 |
| **MSCI BRIC** | 1.30 | -0.49 | -0.49 | -8.74 | 1.73 | 26.88 | 6.27 | 5.93 |
| **MSCI China** | 1.93 | -0.02 | -0.02 | -9.51 | 1.79 | 35.27 | 4.96 | 11.07 |
| **MSCI Europe** | -0.30 | 2.77 | 2.77 | -4.44 | 0.73 | 13.65 | 4.26 | 6.05 |
| **MSCI India** | 1.01 | 4.12 | 4.12 | -6.35 | -3.12 | 12.60 | 8.08 | 7.86 |
| **MSCI Japan** | 0.60 | 0.67 | 0.67 | -2.94 | 1.51 | 19.19 | 7.35 | 7.25 |
| **MSCI EM Latin America** | -0.64 | -1.27 | -1.27 | -5.74 | 6.65 | 17.78 | 6.14 | -2.06 |
| **MSCI Russia** | 0.76 | -7.43 | -7.43 | -10.07 | 1.24 | 11.89 | 7.28 | -0.36 |

## Index Performance as of 4/30/18

| | 1 Week | 1 Month | QTD | 3 Month | YTD | 1 Year | 3 Year | 5 Year |
|---|---|---|---|---|---|---|---|---|
| **F xed Income** | | | | | | | | |
| **Barclays U.S. Aggregate** | 0.20 | -0.74 | -0.74 | -1.05 | -2.19 | -0.32 | 1.07 | 1.47 |
| **ICE BofAML US 3M Trsy Bill** | 0.03 | 0.13 | 0.13 | 0.37 | 0.49 | 1.17 | 0.57 | 0.36 |
| **Barclays U.S. Gov't** | 0.26 | -0.80 | -0.80 | -0.62 | -1.94 | -1.04 | 0.37 | 0.74 |
| **Barclays U.S. Credit** | 0.08 | -0.91 | -0.91 | -2.11 | -3.02 | 0.65 | 2.05 | 2.27 |
| **Barclays High Yield Corp.** | -0.22 | 0.65 | 0.65 | -0.81 | -0.21 | 3.26 | 4.98 | 4.75 |
| **Barclays Municipal** | -0.19 | -0.36 | -0.36 | -0.29 | -1.46 | 1.56 | 2.31 | 2.44 |
| **Barclays TIPS** | 0.36 | -0.06 | -0.06 | 0.01 | -0.85 | 0.27 | 1.04 | -0.12 |
| **Barclays Gbl Agg Ex USD** | -0.73 | -2.27 | -2.27 | -1.71 | 1.27 | 7.68 | 3.09 | 0.44 |
| **Barclays Global Aggregate** | -0.33 | -1.60 | -1.60 | -1.44 | -0.26 | 4.09 | 2.23 | 0.89 |
| **JPM EMBI Global Div** | -0.52 | -1.45 | -1.45 | -3.13 | -3.17 | 1.27 | 4.70 | 3.78 |
| **A ternative Investments** | | | | | | | | |
| **Alerian MLP** | -0.96 | 8.09 | 8.09 | -9.16 | -3.92 | -12.48 | -10.71 | -4.54 |
| **Bloomberg Commodity** | 0.48 | 2.58 | 2.58 | 0.18 | 2.17 | 8.02 | -4.17 | -7.33 |
| **FTSE NAREIT Equity REIT** | 3.45 | 1.43 | 1.43 | -2.82 | -6.88 | -3.26 | 3.49 | 4.86 |
| **S&P Global Natural Res.** | -1.10 | 5.00 | 5.00 | -1.88 | 3.26 | 23.72 | 6.92 | 3.74 |
| **S&P N. Amer Natural Res.** | -0.55 | 7.83 | 7.83 | -1.01 | 1.32 | 10.48 | -1.39 | 0.61 |

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