Market Comments

July, 2018

Top-10 Market & Economic Insights

Here is a list of current perspectives and actions on the mind of the Investment Management Team in this complex environment.

1. Economy – The U.S. economy is currently in its second longest post-WWII economic expansion at nine years. This is only eclipsed by the 10-year economic expansion from 1991 to 2001. While many may view this economic expansion as extended, keep in mind that Australia has not had a recession since 1991.

    - *Takeaway – Never underestimate the resiliency of capitalism.*

2. Diversification – Since 1950, a portfolio consisting of 50% stocks (S&P 500) / 40% bonds (intermediate treasuries) / 10% cash (91-day T-bills) has produced an average annual return of 9.0%, with the best annual return year being +40.4% and the worst return year being -19.5%. On average, a diversified portfolio of this type has been positive in 87% of the 67-year period.

    - *Takeaway – It pays to be diversified, patient and invested through all economic and market periods.*

3. Active vs. Passive Investing – According to Morningstar, the average Active Large Blend Mutual Fund outperformed the S&P 500 Index prior to, during and just after the last two recessions in 2001 and 2008/09. NOTE: This was also true during and just after the 1990/91 recession.

    - *Takeaway – It is important for investors to balance active and passive investing through an economic cycle.*

4. Stocks – Over the past 10 years, the S&P 500 has outperformed the MSCI EAFE Index by +10.84% to +3.11% annualized as of July 16. Over the past year, that outperformance has accelerated to +16.69% versus +6.13%. Currently we favor U.S. stocks, but at some point we realize this strong U.S. outperformance will end.

    - *Takeaway – That is why we stay dynamic and diversified.*

5. Stocks – The longest post-WWII economic expansion was from March 1991 to March 2001 and featured the S&P 500 having a total return of 283.96% (calculated monthly). The current economic expansion began in June 2009 with the S&P 500 having a total return of only 256.72% as of 6/30/2018.

    - *Takeaway – Don't give up on this economy or the stock market yet.*

6. Bonds – The 10-year treasury yield has been below the year-over-year rate of headline inflation for extended periods three times in the last 10 years (…and is so currently in July 2018). Prior to that, the only time a 10-year treasury yield was below the rate of inflation was in the high inflation periods of the mid-1970s and early-1980s.

   - *Takeaway – Bond yields have not been a good hedge against inflation in an era of central bank intervention. It will be of interest how bond yields and inflation interact as global central banks try to normalize interest rates in the coming years.*

7. Bonds – An inverted yield curve (2-year yields being higher than 10-year yields) has preceded each of the last three recessions by 6 to18 months.

   - *Takeaway – The shape of the yield curve in the bond market is dominated by Federal Reserve actual actions and anticipated actions. It will be important to monitor the shape of the yield curve over the coming years as the Federal Reserve strives to normalize interest rates and shrink its balance sheet.*

8. Commodities – There are 19 components in the Thomson Reuters/Core Commodity CRB Commodity Index. Since 1900, it has taken an average of 16.3 years for that index to go from peak to trough in three major cycles. The current cycle peaked in July 2008 at a reading of 473.52 on the CRB Index. However, the index has now been below a reading of 200 since late 2015.

   - *Takeaway – While commodities are considered one of the four asset classes (equities, fixed income, commodities and currencies), they are very difficult to utilize and achieve consistent total returns. However, many find them an attractive short-term investment vehicle for the inherent volatility and supply/demand cycles of the 19 components.*

9. Gold – Gold rose 6.5-fold from 1976 to 1981, but then lost two-thirds of its value steadily falling into 2001. From 2001 to 2012, gold rose 6.4-fold. Since then, gold has been steadily falling and lost 31% of its value from its 2012 high of $1,788/ounce.

   - *Takeaway – Gold tends to rise quickly but fall for long periods of time since the U.S. ended the gold standard in 1971.*

10. REITs – The REIT Sector of the S&P 500 was established in Fall 2016. This puts REIT holdings back in individual stocks for S&P 500 based investors and out of their own asset group for portfolio purposes.

    - *Takeaway – We are utilizing global REITs in portfolios to enhance diversification, risk management and return potential. Over the past year, the FTSE Global REIT index has a total return of 6.85% vs. 4.14% for the S&P 500 REIT index (as of July 16).*

We hope you found this information useful. Our strategists and analysts are paying these topics much attention this year and in years to come for our Private Bank clients.

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