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First quarter Market Update

If the last few years of relatively steady appreciation have lulled investors into complacency, 2018 has likely been a stark reminder of what markets can, and will, do from time to time! The year started the way 2017 ended, then volatility seemingly rose from the dead in the back half of the quarter. In the end, the S&P 500 finished the quarter down slightly at .76% and international developed markets, measured by the MSCI EAFE, also ended down at 1.41%. Rounding out the major asset classes, broader fixed income markets, measured by the Barclay's US Aggregate Bond Index, also ticked down 1.46% as the Federal Reserve continued to raise rates. In times like this it is important for investors to revisit their plan and investment allocations to make sure they remain appropriate for their goals. If nothing their goals and time horizons have remained intact, we would encourage rebalancing back to the original target allocation, but do not see any capital market developments as cause for wholesale changes.

A Bumpy First Quarter

As mentioned Domestic markets, ended the period down .76%. While broader markets slid toward the end of the period we would again point out that the S&P 500 is a broad measure and that there continues to be certain aspects of the market that have done better than others. The biggest difference we see is the performance of growth stocks vs value stocks. Growth stocks are companies that tend to reinvest their earnings in expansion, new products, factories or efforts to enter new markets. Shareholders are primarily rewarded through share price appreciation of growth companies. On the other side of the coin are value stocks, which tend to lack the significant expansion opportunities and instead pass more of their earnings back to investors in the form of dividends. These distinctions become important as investments in these different areas do not move in lock step in different stages of market cycles. Due to these different rates of return it can provide investors significant rebalancing opportunities.

Looking back to the start of 2017, the S&P 500 growth index has appreciated 29.9% while the S&P500 value index has only appreciated 11.24%. At some point we would expect the gap between these two to close. While we do not profess to know if it will be growth companies retreating or value companies improving, but we do see the dispersion as an opportunity to rebalance portfolios locking in gains in the investments that have performed well and theoretically entering investments that have lagged at more attractive prices. Identifying these types of movements can help investors make sense of what can be difficult to reconcile, such as the fact that analysts are currently expecting the first quarter earnings from the S&P 500 to be the best quarterly growth since 2011 with headlines of potential trade wars.

Similar to their domestic counterparts, international markets, measured by the MSCI EAFE, declined 1.41% in the period. One bright spot internationally was from emerging markets, which ended the period up 1.47%. As we mentioned in our last note, international markets remain relatively inexpensive measured by their PE ratio when compared to their domestic counterparts. Currently international markets are trading at 92% of the 20-year average for the ACWI ex-US index compared to the S&P 500 which is currently trading at 1.03% of its 20-year average. Like the growth vs value discussion above international markets have lagged domestic markets since the 2008/2009 recession and could offer investors an attractive rebalancing opportunity.

In a rising interest rate environment, fixed income markets had a difficult period, ending down 1.46%. This difficult backdrop is likely to persist as it is now largely expected that the Federal Reserve will increase interest rates two more times in 2018, likely in quarter point increments. This is not to say that fixed income investments do not play an important role in a well-diversified portfolio. We would remind investors that in severe market contractions a la 2008, Barclays US Aggregate bond index gained 5.2% providing disciplined investors a nice area of respite versus the S&P 500's 38.5% decline.

The above 2008 reference was in no way our attempt to be alarmists with today's volatility. It is instead a reminder to investors that all the major asset classes play an important role in a well-diversified portfolio. In some market cycles different components of the portfolio should do better than others and it is important to revisit the weightings of these asset classes to make sure that they are in line with your goals, time horizons and risk tolerances.

We are always ready to assist you and answer any questions regarding this newsletter or any other financial matter that may come up. If any changes to your situation have occurred, please contact us at your convenience.

Index	Closing Price: 3/30/2018	Closing Price: 12/29/2017	Q1 2018 Return	2018 YTD Return
S&P 500	2,642.31	2,673.61	-0.76%	-0.76%
S&P 500 Value	1,080.05	1,126.98	-3.57%	-3.57%
S&P 500 Growth	1,557.68	1,533.38	1.93%	1.93%
Russell 2000	3,801.01	3,816.13	-0.08%	-0.08%
Russell 2000 Value	6,639.44	6,851.08	-2.64%	-2.64%
Russell 2000 Growth	5,869.99	5,748.35	2.30%	2.30%
MSCI EAFE	2,005.67	2,050.79	-1.41%	-1.41%
MSCI EM	1,170.87	1,158.45	1.47%	1.47%
BBgBarc US Agg Bond	2,016.48	2,046.37	-1.46%	-1.46%

Written by Finity Group

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