HORTER INVESTMENT MANAGEMENT, LLC

Weekly Commentary http://horterinvestment.com/ April 29, 2019

Why a Muni Bond Collapse is Brewing

Investors beware, the muni bond market has gone through some dramatic moves over the last year, and the market looks like it might be headed for a downturn. Changes to the US' tax policy have caused massive inflows to muni bonds as investors try to minimize their taxes. This has caused yields to plunge and spreads to Treasuries to widen. The average ten-year muni yield is now just 1.965% versus 2.6% in 10-year Treasuries, the widest gap since at least 2009. Munis in high tax states have plunged even further, with a recent California issuance having a yield of just 1.73%. One portfolio manager warns investors that they need to be responsive, saying "The best place for investors to be is shorter duration, higher-quality credit, so when opportunities present themselves, they have the flexibility to take them … You can't really set it and forget it".

Click here to read more.

The Fed's key interest rate keeps climbing, and that could become a problem

The Federal Reserve's benchmark interest rate has inched up to its highest level in 11 years even though the central bank has sent a clear message that it is done tightening policy indefinitely.

In recent days, the effective fed funds rate, which targets the overnight level that banks charge each other for loans, has moved up to 2.44%. That's the highest since March 2008 and is just 6 basis points from the top of the target range and the closest to the top since December, when the Fed last raised rates.

For now, the move is looked on as not being especially problematic given that there is still room between the current level and the top of the 2.25% to 2.5% range in which the rate is supposed to trade. But moves toward the upper end of the band have prompted action before, and the trend likely will be a topic of discussion at next week's Federal Open Market Committee meeting.

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QUOTE OF THE WEEK

"Fortune always leaves some door open in disasters whereby to come at a remedy.

- Miguel de Cervantes

Taking a comprehensive look at the overall current stock market

Taking a comprehensive look at the overall current stock market, you can see the chart below representing eight major indices and their returns through the week ending April 26, 2019. In a truly diversified portfolio, the portfolio's total return is determined by the performance of all of the individual positions in combination – not individually.

So, understanding the combined overall performance of the indices below, simply average the 12 indices to get a better overall picture of the market. The combined average of all 12 indices is 13.09% year to date.

Index	Last Week		One Month	Year-to-Date
	Close	% Change	% Change	% Change
Dow Jones Industrial Average Index	26,543.33	-0.06%	3.55%	14.57%
S&P 500 Index	2,939.88	1.21%	4.44%	18.00%
Nasdaq Composite Index	8,146.40	1.86%	5.96%	23.15%
60/40 Portfolio (BAGPX)	12.79	0.71%	2.40%	11.31%
US Aggregate Bond Index	2,107.33	0.38%	0.07%	2.98%
20+ Year Treasury Bond (TLT)	123.81	0.74%	-0.71%	1.89%
MSCI EAFE (EFA)	66.45	-0.33%	2.67%	13.05%
MSCI Emerging Markets (EEM)	43.88	-1.53%	3.10%	12.34%
France CAC Index (EWQ)	30.54	-0.78%	4.27%	17.60%
Germany DAX Index (EWG)	28.54	-0.11%	6.10%	12.58%
Italy Borsa Index (EWI)	27.93	-1.52%	1.01%	15.37%
London FTSE (EWU)	33.52	-0.86%	1.39%	14.21%

Data Source: Investors FastTrack, Yahoo Finance, Investopedia

Term of the Week:

IPO

Initial public offering. This represents the first time a company offers shares to the public.

Dow Jones - Week Ending

WEEKLY MARKET SUMMARY

Global Equities: The S&P 500 Index and the Nasdaq Composite resumed their march higher during the week, rising 1.21% and 1.85% respectively, while marking new all-time closing highs in the process. This was due to positive earnings surprises, and a bounce back from oversold conditions of the Healthcare sector, as the SPDR Select Sector Healthcare ETF (XLV) gained 3.6% during the week. The Dow Jones Industrial Average was reined in by poor reception to earnings releases from some of its key constituents, causing the index to be slightly negative. International equities were lower on the week, led to the downside by Emerging Market equities represented by the iShares MSCI Emerging Market Index ETF (EEM) losing -1.53% as negative economic news from major exporter, Korea, combined with a stronger US dollar to drag down Asian markets.

Fixed Income: The yield on the 10-year US Treasury Note broke below 2.5% despite a positive surprise for the preliminary reading of US 1st quarter GDP. The US Treasury yield curve has again slumped lower at the intermediate maturities, signaling that the market expects upcoming rate cuts. This could change if we were to see signs of inflation accelerating from the current moderate pace in next week's Consumer Price Index (CPI) release. The interest rate spread of high yield bonds over equivalent Treasury securities contracted during the week, while Lipper reported net outflows of $521 million from high yield funds.

Commodities: Oil prices took a hit, late in the week, after it was reported that President Trump contacted OPEC to "tame fuel costs". The major crude benchmarks were down as much as 4% on Friday despite other news that the US would not extend waivers to countries trading with Iran. West Texas Intermediate closed the week down over -1% at 63.30 per barrel, while the International Brent crude benchmark was down over -.5%, at $71.60 per barrel. Natural gas prices traded at the NYMEX rose over 3%, to $2.57/MMBtu.

WEEKLY ECONOMIC SUMMARY

Gross Domestic Product (GDP): The preliminary estimate for 1st quarter US Real GDP was released at an annualized 3.2% versus expectations for 2.3% growth. US consumers contributed positively, however the main factor for the upside surprise was a lower figure for imports, which reduced the drag that negative net exports have on headline GDP. Inventories and government purchases also increased more than expected during the quarter, which combined with falling imports, has some questioning the quality of the GDP figure. The price index was much lower than expected, coming in at .9% versus 1.7%, while the core price index also came up short, at 1.3% versus 1.6%.

Durable Goods Orders: Orders for durable goods increased 2.7% during the month of March. A large and welcome increase to aircraft and automobile sales helped the headline figure come in much higher than the .7% expected. When excluding the effect of these and other transportation equipment, the index rose a respectable .4% versus a .2% expected. Core capital goods (non-defense, non-aircraft) also rose a surprising 1.3%, which is a good sign for a rebound in the manufacturing sector and the economy as a whole.

1st Quarter Earnings: It was a very busy week for earnings releases, with many large cap bellwether names reporting during the week with mixed results. Technology stocks including Facebook Inc. (FB), Microsoft Corp. (MSFT), and Amazon.com Inc. (AMZN), were higher after upside earnings surprises while other blue chips stocks including Exxon Mobil Corp. (XOM), 3M Company (MMM), and Caterpillar Inc. (CAT), were punished after reporting. Boeing Co. (BA) stock was surprisingly higher despite missing on revenues and earnings, suspending forecasts, and pausing its share buyback program, due to the issues surrounding its 737 Max aircraft.

Data Source: Hanlon Investment Management

Current Model Allocations

Tactical Fixed Income Model Allocations
4/26/2019

Exchange Traded Fund — 9.6%	Exchange Traded Fund – 16.50%	Exchange Traded Fund – 13.6%	Exchange Traded Fund — 9.60%
Exchange Traded Fund —4.0%	Exchange Traded Fund – 9.6%	Exchange Traded Fund – 8.80%	Exchange Traded Fund — 4%
Exchange Traded Fund —4%	Exchange Traded Fund — 12.5%	Cash –3%	Exchange Traded Fund -4.80

Other Managers

HIM #9—	100% fund
HIM #22—	50% fund/ 50% fund
HIM #25—	100% fund
HIM #8—	16.66% Fidelity VIP/ 33.34% Franklin VIP/ 16.67% Pro funds/16.67% Mainstay VP/ 16.67% T Rowe
HIM #10—	2% into 50 holdings

Summary

In utilizing an approach that seeks to limit volatility, it is important to keep perspective of the activity in multiple asset classes. We seek to achieve superior risk-adjusted returns over a full market cycle to a traditional 60% equities / 40% bonds asset allocation. We do this by implementing global mandates of several tactical managers within different risk buckets. For those investors who are unwilling to stomach anything more than minimal downside risk, our goal is to provide a satisfying return over a full market cycle compared to the Barclays Aggregate Bond Index. At Horter Investment Management we realize how confusing the financial markets can be. It is important to keep our clients up to date on what it all means, especially with how it relates to our private wealth managers and their models. We are now in year nine of the most recent bull market, one of the longest bull markets in U.S. history. At this late stage of the market cycle, it is extremely common for hedged managers to underperform, as they are seeking to limit risk. While none of us know when a market correction will come, even though the movement and volatility sure are starting to act like a correction, our managers have been hired based on our belief that they can accomplish a satisfying return over a full market cycle, -- while limiting risk in comparison to a traditional asset allocation approach. At Horter we continue to monitor all of the markets and how our managers are actively managing their portfolios. We remind you there are opportunities to consider with all of our managers. Hopefully this recent market commentary is helpful and thanks for your continued trust and loyalty.

Data Source: Hanlon Investment Management

CHART OF THE WEEK

The Chart of the Week shows a 2-year chart of the S&P 500 Index fully retracing from the Christmas Eve low. Although not historically cheap, trading at 19.5x expected full-year 2019 reported earnings, the large-cap index should have support at this level should it continue this break above the prior high, barring a surprise from the upcoming release of US inflation data and subsequent Federal Reserve board meeting and announcement.

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