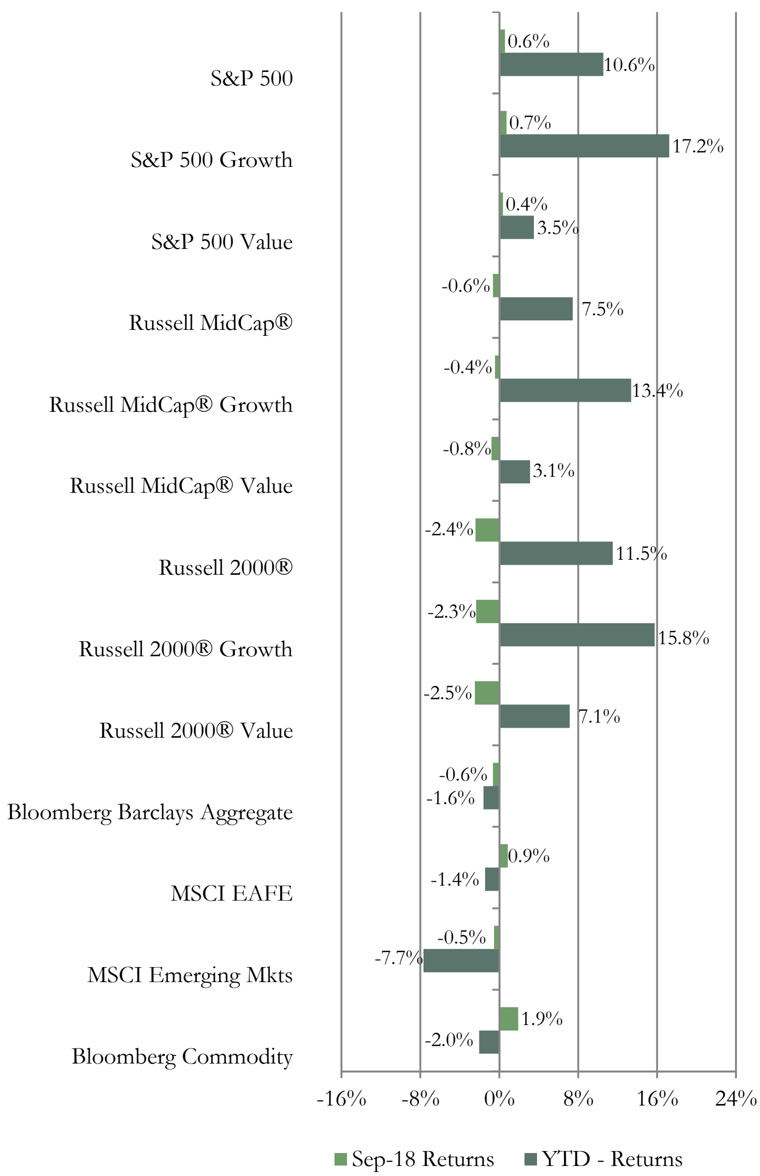
Monthly Market Summary – September 2018

Global financial market returns were mixed in September in reaction to variations in economic growth by region, country specific political events, and evolving trade issues. For example, strong economic growth data in the U.S., such as the July Institute of Supply Management Manufacturing Index hitting a 14-year high and year-over year wage growth coming in at the highest rate since November 2008, provided a boost to U.S. large-capitalization (cap) stocks driving the S&P 500 and the Dow Jones Industrial Average to new record highs. In contrast, signs of slowing economic activity in China and the implementation by the U.S. of 10% tariffs on an additional $200 billion worth of Chinese goods pushed the Shanghai Composite index to a four-year low.

Market Indices – September 2018



U.S. equity market movement in September varied by market cap. The S&P 500 index trended higher during much of the month and set a new record closing high on September 20. The Russell Midcap index traded in a tight range but ended the month slightly lower. After reaching record highs in August, the Russell 2000 index of small-cap stocks trended lower throughout September. Sector returns varied widely with no common trends across the market cap segments except that the growth stock indices outperformed the value stock indices by a small margin. As a reminder, on September 24, index providers S&P and MSCI made a change to the telecommunications services sector. The sector is now called communications services and combines telecommunications, media, and internet industry stocks. In the S&P 500 index, stocks such as Facebook, Alphabet, Disney, and Netfix were recategorized into the communications services sector. After the September changes, the communications services sector will have more growth stock characteristics than the former telecommunications services sector.

Non-U.S. equity markets were mixed in September. The MSCI EAFE index of developed international stocks had a return for the period of 0.9% but the MSCI Emerging Markets (EM) index had a return of -0.5% on a U.S. dollar basis. The currency impact was limited in September but provided a small positive boost for the EM index since the U.S.

dollar dipped against certain currencies. The local currency return was 1.4% for the EAFE index and -1.2% for the EM index. Value stocks outperformed growth in both the EAFE and EM indices. On a geographic basis, among the developed international economies, Japan was the best performing region boosted by a weaker yen, which is a benefit in an export heavy economy, and by the report of a rebound back into positive territory for second quarter gross domestic product (GDP) growth after a negative GDP report in the first quarter. Strong retail sales gave additional evidence that Japan's economy is strengthening. Germany was one of the weakest performing developed international equity markets in reaction to reports of declines in industrial output and exports. Among emerging markets, Russia was one of the top performers boosted by higher oil prices. Higher oil prices had a negative impact on equities in India since India is dependent on oil imports resulting in India being the worst performing EM equity market.

U.S. bond market returns were mostly negative in September leading the Bloomberg Barclays U.S. Aggregate Bond index to post a return of -0.6%. Treasury bond yields rose, and prices declined, in reaction to strong economic news such as positive job and wage growth data. Yields also rose in response to the 0.25% increase in the federal funds rate by the Federal Reserve. The 2-year Treasury note yield rose to 2.81%, which is the highest level in a decade. The 10-year Treasury bond yield rose to 3.05% up from 2.85% at the end of August. Only the shortest maturity bonds had small positive returns while longer maturity bonds posted negative returns. High yield bonds outperformed other sectors. High yield bond prices were driven higher primarily by a supply demand imbalance. New bond issuance in the sector has been low and has not been at adequate levels to accommodate investor demand for reinvestment of proceeds from bond maturities.

The Bloomberg Commodity index had a return of 1.9% for September. Performance of the sub-indices was mixed. The livestock sub-index, which was up almost 8%, had the largest gain among sectors we track. The energy sector had a solid gain of over 5% as both oil and natural gas prices rose during the month. West Texas Intermediate (WTI) crude oil rose almost 5% to over $73 per barrel on tight supply levels due to lower production related to pipeline capacity constraints as well as in reaction to reports that Saudi Arabia will not increase production to offset supply disruptions from other countries. The industrial metals sub-index also had a gain for the month. In contrast, precious metals prices declined in September. Grain prices fell as inventory levels continue to rise.

Vogel Consulting, LLC (Vogel) Tactical Recommendations

We continue to be cautiously optimistic. Solid economic and earnings reports and forecasts along with still accommodative central bank policies and fiscal stimulus in the U.S. and other major economies appear to outweigh the current risks to earnings from rising interest rates, tight labor markets, higher oil prices, and continuing trade tensions between the U.S. and China. However, it is likely financial markets will continue to be volatile as investors react to news on trade talks and tariff actions, management comments in earnings reports, and economic data releases.

We continue to recommend an equal weight to U.S. large-cap, mid-cap, and small-cap stocks and to developed international equities. We recommend an overweight to emerging markets equities. We are maintaining the overweight due to the growth potential and improved fundamentals in various emerging market countries along with more attractive relative valuations. Stability in the U.S. dollar would also be a positive for many emerging markets. We continue to favor equities over bonds and retain our underweight recommendation for fixed income investments. Our underweight recommendation is because the return expectation for bonds is low since yields are likely to move higher (and prices lower) as the Federal Reserve continues to hike its policy rate. Within fixed income we continue to recommend a focus on short to intermediate term bonds. We also continue to favor non-Treasury bonds for the yield advantage they provide. We continue to favor hedge fund strategies over fixed income for the lower expected volatility portion of portfolios but also recommend an underweight allocation to hedge funds. Since our expectation is for a moderate rate of inflation, we recommend an equal weight to real assets. We continue to recommend an overweight to cash reserves that includes adequate cash to support spending needs over the coming 12-24 months.