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Entrust Financial LLC® Market Commentary – Second Quarter, 2018

Trade Wars

We began the second quarter of 2018 with new tariffs on goods coming into the U.S. from abroad, put in place by the Trump administration. Retaliation has been swift. China, our largest trading partner, issued its own tariffs on certain U.S. exports. These tariffs affect not only steel and aluminum, but also agricultural products—immediately raising concerns about the strong negative effect on profitability that U.S. farmers are likely to suffer. Meanwhile, the European Union and Mexico are also expected to impose retaliatory tariffs on U.S. goods. To date, the Trump administration has responded with a list of other Chinese goods that could be hit with 25% tariffs and the back and forth threat of retaliatory tariffs continues.

If many of the threatened tariffs are implemented, they could cause higher prices for a variety of consumer products, as well as higher costs for commercial construction and infrastructure projects. Furthermore, uncertainty about tariffs could delay capital investment and increase the probability of accelerating inflation, particularly in light of existing inflation fears caused by reports of elevated wage growth.

It is unknown how the trade wars will play out and ultimately affect the markets, although tariff threats are generally considered to be a negative for the economy. So far, the U.S. market seems to be minimizing the risks from the Trump administration's trade agenda.

Here are some highlights from the second quarter:

- U.S. stocks rose during the second quarter of 2018. U.S. small cap stocks outperformed large caps as investors preferred companies less dependent on foreign trade. Growth stocks continue to outperform value stocks.
- Energy stocks were the best performers, leading the markets higher amid fears of worldwide oil supply shortages. The information technology sector rallied on solid earnings reports from Apple, Facebook and Microsoft.
- European, Asia-Pacific and Australian stocks rose during the quarter. Select companies experienced strong earnings growth which helped investor confidence.
- Emerging markets stocks were down due to weakened currency versus the U.S. Dollar, and global trade tensions.
- Global economic growth remained steady, although there are some signs of slowing economic growth.
- The euro, yen and Australian dollar fell against the U.S. dollar.
- The Federal Reserve raised the Fed funds rate another 25 basis points during the quarter; the interest rate for excess reserves is now 2%.
- Housing starts continued to climb as new homes are needed to meet housing shortages.

As we watch the trade wars play out, Entrust will continue to invest our clients' assets in well-diversified portfolios. Fine-tuning of current asset allocations may incorporate fund exchanges, particularly in the asset class of bonds, as we aim to protect against the potential for accelerating inflation.

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Following are results for indices of asset classes commonly used to build our Entrust globally diversified portfolios:

Asset Class Review

	Q2 2018	2018 Year to Date	1 Year Trailing	3 Year Trailing	5 Year Trailing	10 Year Trailing
US Large Cap Equity	3.6%	2.9%	14.5%	11.6%	13.4%	10.2%
US Small Cap Equity	7.8%	7.7%	17.6%	11.0%	12.5%	10.6%
International Equity	-1.2%	-2.8%	6.8%	4.9%	6.4%	2.8%
Emerging Market Equity	-8.0%	-6.7%	8.2%	5.6%	5.0%	2.3%
Global Real Estate	6.1%	-0.1%	4.0%	5.8%	6.3%	5.4%
US Corporate Bond	-1.0%	-3.2%	-0.9%	3.0%	3.5%	5.3%
US Government Bond	0.1%	-1.1%	-0.7%	1.0%	1.5%	3.0%
International Bond	-4.8%	-1.3%	2.8%	3.2%	0.9%	1.8%

The above chart is for illustrative purposes only and does not attempt to predict actual results of any particular investment. Past performance is no guarantee of future results. It is not possible to invest directly into an index.
Source: Morningstar Direct- US Large Cap is represented by the Russell 1000 Index; US Small Cap is represented by the Russell 2000 Index; International is represented by MSCI EAFE Index; Emerging Markets are represented by the MSCI Emerging Markets Index; Global Real Estate is represented by the S&P Global REIT Index; US Corporate Bonds is represented by the Morningstar US Corp Bond Index; US Government Bonds is represented by the Morningstar US Government Bond Index; International Bonds are represented by the Barclays Global Aggregate Bond ex USD Index. Returns as of 06/31/18.

For those interested in more in-depth technical analysis of the capital markets world-wide:

Results in North America

U.S. Stocks advanced in the second quarter despite market volatility due to geopolitical tensions.

Energy stocks rallied sharply, supported by higher oil prices.

Growth companies generally outpaced value stocks as consumer discretionary and information technology were two of the top-returning sectors.

The financials sector came under pressure by geopolitical headwinds and a flattening yield curve.

The Federal Reserve hiked the federal funds target rate in June by 25 basis points. The Fed also signaled two more rate increases later in 2018.

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International Results

European stocks rose and the euro declined sharply as signs of slowing economic growth and escalating trade tensions combined to dampen investor sentiment in the eurozone. Overall, the MSCI Europe Index rose 4% in local currency terms, but declined 1% in U.S. dollar terms.

The European Central Bank announced that it will begin winding down its massive bond-buying stimulus program in September. ECB officials made it clear they will not raise interest rates until mid-to-late 2019, a longer timeline than had been expected. That news sent the euro down against the dollar as investors realized the era of negative interest won't be ending soon. Eurozone government bond prices were down for the quarter.

Japanese finished positively for the quarter despite volatility resulting from news of decline in the country's GDP and announced tariffs between the U.S., China and Eurozone. The yen fell 4% against the U.S. dollar, boosting Japan's export-driven corporations.

Australian stocks were up for the quarter despite worldwide trade turmoil. The Australian dollar fell 4% against the U.S. dollar, making Australian exports more competitive overseas.

Emerging markets stocks fell due to trade tensions and concern about the strengthening U.S. dollar.

Chinese stocks were down for the quarter due to escalating trade tensions with the U.S.