

Entrust Financial LLC® Market Commentary – Third Quarter, 2018

Flashing Yellow Lights

The third quarter was characterized by what could be called “flashing yellow lights.” What this means to investors is that while the economic road ahead will likely be bumpy, the alarm bell of recession is not yet sounding. For instance, investors continue to be concerned about the escalating conflict with China, our largest trading partner. But following months of trade war fears, the third quarter did bring about the good news of the apparent re-affirmation of NAFTA (now called USMCA, the “United States, Mexico and Canada Agreement”).

There are several reasons for optimism regarding the U.S. economy—daily, dramatic headlines notwithstanding. For example, we are currently experiencing the second-longest expansion in market history and are on pace to extend to the longest. In addition, Federal Reserve Chair Jerome Powell recently indicated there are several more rate hikes still to come before we hit our “new neutral.” Though rising rates can cause stress on sentiment, investors may find some relief in the historical trend that recessions tend to come after a rate hike cycle is completed, not during.

Here are some highlights from the third quarter:

- Strong corporate earnings and solid growth among the developed markets allowed global equities to rally.
- U.S. stocks hit a series of new record highs, with health care stocks generating the highest returns.
- Impressive earnings reports from Apple, Microsoft and others allowed Information Technology stocks to continue to shine.
- The U.S. Dollar rallied against the Euro, the Yen and most other currencies.
- European and Asia-Pacific stocks rose during the quarter. As in the U.S., European health care companies enjoyed strong earnings growth; the re-election of Japanese Prime Minister Shinzo Abe helped investor confidence with respect to policy continuity.
- Emerging markets stocks were down due to weakened currency versus the U.S. dollar, and global trade tensions.
- The Federal Reserve raised the Fed funds rate another 25 basis points in September, marking the third rate hike this year.

As we watch these and other potential “flashing yellows” as they emerge, Entrust will continue to invest our clients’ assets in well-diversified portfolios.

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

Asset Class Review

	Q3 2018	2018 Year to Date	1 Year Trailing	3 Year Trailing	5 Year Trailing	10 Year Trailing
US Large Cap Equity	7.42%	10.49%	17.76%	17.07%	13.67%	12.09%
US Small Cap Equity	3.58%	11.51%	15.24%	17.12%	11.07%	11.11%
International Equity	1.35%	-1.43%	2.74%	9.23%	4.42%	5.38%
Emerging Market Equity	-1.9%	-7.68%	-0.81%	12.36%	3.61%	5.4%
Global Real Estate	0.22%	0.77%	4.06%	7.17%	7.49%	7.07%
US Corporate Bond	1.02%	-2.19%	-1.12%	3.14%	3.51%	6.16%
US Government Bond	-0.57%	-1.69%	-1.59%	0.25%	1.35%	2.70%
International Bond	-1.74%	-3.03%	-1.45%	2.41%	-0.33%	2.2%

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 9/30/2018..

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

Results in North America

U.S. equities had the highest return of any developed market, hitting record levels at the end of the quarter.

The U.S. added tariffs on a further \$200 billion of Chinese goods, adding to trade tensions and prompting additional retaliation by China.

Growth companies continued to outpace value stocks, as pharmaceuticals soared on better-than-expected earnings.

Social media companies like Facebook and Twitter saw sharp declines amidst slowing user growth.

The Federal Reserve hiked the federal funds target rate in September by another 25 basis points. The Fed also signaled more future increases than previously expected.

International Results

European stocks rose despite investor fears about slowing economic growth and escalating trade tensions. Overall, the MSCI Europe Index rose 1% in local currency terms, but the euro declined 1% against the U.S. dollar.

The European Central Bank announced that it will remain on schedule to phase out its bond-buying stimulus program by the end of the year.

Japanese equities rose late in the quarter amidst strong economic indicators both at home and in the U.S. The MSCI Japan Index rose 6% , while the yen fell 2% against the U.S. dollar.

Emerging markets stocks fell due to rising U.S. rates and a strong U.S. dollar. Trade tensions between the U.S. and China continued to dampen this space. Overall, the MSCI Emerging Markets Investable Market Index fell 1%, putting its year-to-date loss at 8%.

Chinese stocks were down for the second quarter in a row due to escalating trade tensions with the U.S. and China's slowing pace of economic growth.

Past performance is no guarantee of future results. International investing involves special risks, including but not limited to, the possibility of substantial volatility due to currency fluctuation and political uncertainties. Diversification does not guarantee a profit nor protect against a loss. Large Cap refers to companies with a market capitalization value of more than \$10 billion. Large cap is an abbreviation of the term "large market capitalization." Market capitalization is calculated by multiplying the number of a company's shares outstanding by its stock price per share. International investing involves special risks, including, but not limited to, the possibility of substantial volatility due to currency fluctuation and political uncertainties. Emerging markets are sought by investors for the prospect of high returns, as they often experience faster economic growth as measured by GDP. Investments in emerging markets come with much greater risk due to political instability, domestic infrastructure problems, currency volatility and limited equity opportunities (many large companies may still be "state-run" or private). Also, local stock exchanges may not offer liquid markets for outside investors. Small cap stocks may be subject to a higher degree of risk than larger, more established companies' securities, including higher risk of failure and higher volatility. The illiquidity of the small-cap market may adversely affect the value of these investments so those shares, when redeemed, may be worth more or less than their original cost. Government bonds are guaranteed by the U.S. Government and if held to maturity, offer a fixed rate of return and fixed principal amount. Guarantee only applies to the timely payment of principal and interest and does not pertain to the portfolio or mutual fund, holding such securities. Values will fluctuate, and upon redemption, share values may be worth more or less than the original investment. Investments in high yield bonds entail higher risks, including greater credit risks. Their NAVs are sensitive to interest rate movements (a rise in interest rates can result in a decline in value of the investment). Upon redemption, share values may be worth more or less than the original investment. Corporate bonds are debt securities issued by a corporation and sold to investors. The backing for the bond is usually the payment ability of the company, which is typically money to be earned from future operations. In some cases, the company's physical assets may be used as collateral for bonds. Corporate bonds are considered higher risk than government bonds. As a result, interest rates are almost always higher. Treasury Inflation Protected Securities (TIPS) are a treasury security that is indexed to inflation in order to protect investors from the negative effects of inflation. TIPS are considered an extremely low-risk investment since they are backed by the U.S. government and since their par value rises with inflation, as measured by the Consumer Price Index, while their interest rate remains fixed. The value of the shares of a REIT fund will fluctuate with the value of the underlying assets (real estate properties.) There are special risk factors associated with REITs, such as interest rate risk and the illiquidity of the real estate market. A commodity is a basic good used in commerce that is interchangeable with other commodities of the same type. Commodities are most often used as inputs in the production of other goods or services. The quality of a given commodity may differ slightly, but it is essentially uniform across producers. When they are traded on an exchange, commodities must also meet specified minimum standards, also known as a basis grade.