Entrust Financial LLC® Market Commentary – Fourth Quarter, 2018

A Very Bumpy Sleigh Ride

It is no secret that the fourth quarter capital markets did not leave investors feeling as festive as they might have preferred during the December holiday season. However, the final three months were not representative of 2018 in its entirety, and therefore portfolio results were buffered from more significant declines by solid returns earlier in the year.

Emotions run high in times of market uncertainty, and there is often a strong correlation between consumer confidence and stock market performance. What may help ease some investor anxiety is to cut through the noise of our omnipresent news media and focus instead on what matters. At Entrust, we will be paying special attention to what action (or not) the Federal Reserve takes with respect to interest rate hikes and the resulting impact on inflation.

The good news is that despite the bumpy ride caused by the recent equity market decline, there are still economic indicators of strength. For instance, the U.S. economy continues to grow, the labor market remains strong, and finally, in the spirit of our holiday theme, the recent holiday shopping season was one of the most robust in the last decade.

Here are some highlights from the fourth quarter:

- A temporary pact between the U.S. and China to suspend additional tariffs did little to calm investors.
- U.S. equities tumbled, with the major indexes experiencing their worst single quarter since 2011.
- Shares of Apple, Amazon and Netflix each declined by at least 25%.
- The Federal Reserve raised rates by a further 25 basis points following their December meeting, as expected.
- The U.S. labor market added 312,000 jobs, far exceeding industry expectations.
- The US dollar strengthened against most currencies, including the euro.
- After posting positive returns through September, global equity markets declined in the fourth quarter.

Negative year-end results notwithstanding, in 2018 U.S. equities prevailed yet again and continued their streak of leading the other developed markets. It may help reassure long-term investors to keep in mind that based upon historical trends, the asset class winner during one extended period of time frequently hands off that leadership to a different asset class for the period following. As we begin the new year, it will be interesting to see which asset class will lead the market in 2019 and beyond.

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

Asset Class Review

	Q4 2018	2018 Year to Date	1 Year Trailing	3 Year Trailing	5 Year Trailing	10 Year Trailing
US Large Cap Equity	-13.82%	-4.78%	-4.78%	9.09%	8.21%	13.28%
US Small Cap Equity	-20.20%	-11.01%	-11.01%	7.36%	4.41%	11.97%
International Equity	-12.54%	-13.79%	-13.79%	2.87%	0.53%	6.32%
Emerging Market Equity	-7.47%	-14.58%	-14.58%	9.25%	1.65%	8.02%
Global Real Estate	-5.79%	-5.90%	-5.90%	2.25%	5.28%	10.05%
US Corporate Bond	-0.11%	-2.30%	-2.30%	3.23%	3.26%	5.69%
US Government Bond	2.60%	0.86%	0.86%	1.41%	2.03%	2.12%
International Bond	0.91%	-2.15%	-2.15%	3.15%	-0.01%	1.74%

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 12/31/2018.

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

Results in North America

- A deepening trade conflict with China as well as a partial inversion of the yield curve renewed concerns about the sustainability of the current economic expansion and bull market.
- Political disputes rankled markets as disagreements over security funding contributed to a partial U.S. government shutdown during the final week of the year.
- Many previously high-flying growth companies have lowered guidance for future quarters amid concerns over global trade and rising interest rates.
- The tech-heavy Nasdaq Composite entered bear territory, becoming the first of the three major U.S. indexes to do so since the bull market started in 2009.
- Defensive stocks held up best, including utilities companies and real estate investment trusts. Procter & Gamble was one of the better returning stocks, posting an 11% gain.

International Results

- Europe European stocks declined sharply amid slowing economic growth and continuing uncertainty over the U.K.’s impending departure from the European Union.
- A worsening global trade dispute between the U.S. and China also weighed heavily on Europe’s trade-dependent economy.
- Shares of German software giant SAP tumbled in concert with a broad-based decline among U.S. technology stocks.
- Japanese equities were caught in the global sell-off. Japanese stocks fell in the fourth quarter, finishing near their 2018 lows.
- Other markets across the Asia-Pacific region also retreated as investors worried about slowing economic growth, trade conflicts and rising U.S. interest rates.
- Stock markets in Hong Kong, Singapore and New Zealand saw mid-single-digit declines.

Fixed Income

- In December, the Federal Reserve hiked the federal funds target rate by 25 basis points for the fourth time in 2018, to a range of 2.25%–2.50%.
- Despite weaker-than-expected growth, the European Central Bank ended its bond-buying stimulus program in December, as planned, leaving market participants to speculate on when the ECB might begin raising interest rates.
- The Bank of Japan maintained loose policy, keeping its aggressive stimulus in place at its final meeting of 2018. Continued low inflation suggests no end in sight for the central bank’s negative short-term interest rates and asset purchases.
- Bond yields fell dramatically, while credit tumbled.
- U.S. bond markets returned 1.6% overall as falling yields outweighed wider credit spreads.
- The benchmark 10-year Treasury yield fell 36 basis points to 2.69%.
- High-yield corporate bonds saw the brunt of the credit selling, falling 4.5%, while investment-grade bonds lost 0.2%.
- Investment-grade spreads ended the quarter meaningfully wider, hitting levels not seen since 2016. Wider spreads indicate the market is pricing corporate bonds lower, all else held equal.
- In fixed income markets, European government bonds rallied on safe-haven buying and investor speculation that the ECB may forego raising interest rates until late 2019 or beyond.