INVESTMENT COMMITTEE MARKET COMMENTARY

FEBRUARY 27, 2017 www.clearbrookglobal.com

U.S. EQUITIES

U.S. equity markets closed in positive territory after a late Friday session rally, as the S&P 500 and the Nasdaq rose for a fifth straight week, while the Dow brought its weekly winning streak to three. The markets are being pushed by inflows into passive vehicles, which are blindly driving equity indexes higher.

a) **Dow Jones +0.99% MTD +5.14% YTD +5.81%** b) **S&P 500 +0.73% MTD +4.12% YTD +6.09%**
c) **Russell 2000 -0.36% MTD +2.49% YTD +2.89%**

Drivers: I) **The S&P 500 has rallied** an estimated 11.0% since President Donald Trump's election victory. The gains have been prompted by two ideas: the new administration's policies on taxes and regulation will accelerate economic growth, and that that will lead to higher corporate profits. Hope for better earnings has allowed the market to ignore bad news, including rising geopolitical tensions, but investors may be getting ahead of themselves as the **current S&P 500 P/E is 24.8X.**

II) The **mean estimate** of analysts surveyed by FactSet see **S&P 500 earnings** of $121.85 per share for 2017. At the end of January, analysts were looking for earnings of $123.13 a share, representing a drop of 1% in forecasts month to date. At the end of October, the last period before Trump's unexpected victory, the S&P 500 earnings estimate was for $121.91 a share. While consensus forecasts are essentially unchanged from then, down by 5 cents a share, the S&P 500 has risen more than 11% over the same period.

III*)* **In January**, **sales of previously-owned homes** soared to the **highest in a decade**, a sign of persistent demand despite higher mortgage rates and shrinking supply. Existing-home sales came in at a seasonally adjusted annual pace of 5.69 million, the National Association of Realtors reported. That was 3.3% above an upwardly-revised 5.51 million in December and 3.8% higher than a year ago.

IV) The level of optimism about the economy among U.S. consumers fell slightly in February, but still pointed to steady growth. The survey of the **University of Michigan Consumer Sentiment Index** fell to 96.3 this month, slightly better than the preliminary estimate of 95.7. A month earlier the index had touched a 13-year high of 98.5, essentially reflecting an increase in confidence following the election of President Donald Trump.

V) **Equity prices in February are higher with Large-Cap, Growth, Healthcare and Information Technology leading equity price performance. The laggards for the month are Small-Cap, Value Stocks and Energy.**

Capitalization: **Large Caps +4.03%** (YTD +6.12%), Mid-Caps +3.04% (YTD +5.53%) and **Small Caps** +2.49% (YTD +2.89%). Style: **Value** +**2.34%** (YTD +2.97%) and **Growth +3.28%** (YTD +4.75%). Industry Groups (Leaders): Consumer Discretionary +6.21% (YTD +11.24), **Information Technology +5.55%** (YTD +10.10%), Technology +5.13% (YTD +9.03%), **Healthcare +6.20%** (YTD +8.64), Consumer Staples +3.67% (YTD +6.67%), Utilities +4.83% (YTD +6.19%), Materials +0.97% (YTD +5.61%) and Financial Services +4.87% (YTD +5.12%). (Laggards): Telecommunication +1.16% (YTD -1.25%) and **Energy -2.55%** (YTD -5.70%).

EUROPEAN EQUITIES

The MSCI Europe index dropped by the most in three weeks, falling from 14-month highs as investors questioned the prospects for U.S. tax policy changes under U.S. President Donald Trump.

Drivers: I) **National Front party leader Le Pen** has been gaining support in her bid to become France's new president. Le Pen is seen by some as a risk to the euro-zone's foundations as she has called for France to leave the euro and withdraw from the EU. An OpinonWay ***poll showed Le Pen pulling ahead*** of Emmanuel Macron the former economics minister, and François Fillon, the conservative former prime minister.

II) IHS Markit reported its composite **Purchasing Managers Index** for the **euro-zone's manufacturers and service providers**, which is based on a survey of 5,000 companies, rose to 56.0 in February from 54.3 in January, reaching its **highest level since April 2011**. New orders flowed in at the fastest pace in six years, while businesses hired additional workers at a rate not seen since before the financial crisis, in August 2007.

III) **Performance of European Indexes for the week, month-to-date and year-to-date. The MSCI Europe Index was lower by -0.55% for the week (MTD +0.62% YTD +2.71%).**

ASIAN EQUITIES

Asian markets were mixed last week as dovish signals from the U.S. Federal Reserve weakened the dollar, with possible consequences for the competitiveness of Asian exports. The Dow Jones Asia Pacific Index was higher by +0.80% for the week, (MTD +3.46%), (YTD +8.27%).

Drivers: I) **Bank of Japan Governor Haruhiko Kuroda** stated last Wednesday that **pushing rates further into negative territory** was not being considered, reflecting both his positive inflation outlook and his concerns over the contentious policy measure. "There is not much likelihood that we will further lower the negative rate" from the current minus 0.1%, Kuroda said in parliament, citing Japan's accelerating growth.

II) Chevron Corp. has signed a preliminary deal with China's Zhenhua Oil, a state-run oil and gas explorer, to sell its major natural gas fields in Bangladesh for about $2 billion, Reuters reported, citing Beijing-based oil executives. Bangladesh, with rights of first refusal on those gas fields, could side track the deal, as its national oil company Petrobangla is trying to raise the financing to purchase them, the report said.

III) **Performance of Asian Indexes for the week, month-to-date and year-to-date. The Nikkei was higher by +0.25% (MTD +1.33% YTD +0.89%), the Hang Seng Index fell by -0.28% (MTD +2.56% YTD +8.93%) and the Shanghai Composite advanced by +1.60% (MTD +2.98% YTD +4.83%).**

FIXED INCOME

Treasury yields fell to their lowest levels in more than five weeks on Friday, posting their largest weekly decline since December, as President Donald Trump offered no new details about his plans for implementing his sweeping economic policy changes.

Performance: I) **The 10-year Treasury yield was lower last week ending at 2.314% down from 2.418%. The 30-year yield fell last week, declining from 3.006% to 2.953%.**

II) **Performance for the week, month-to-date and year-to-date. Barclays US Aggregate Bond was up +0.37% last week, MTD +0.65% and YTD +0.68%. The Barclays US MBS TR was higher by +0.30% last week, MTD +0.58% and YTD +0.36%. The Barclay's US Corporate HY Index rose by +0.57%, MTD +1.12% and YTD +2.68%.**

COMMODITIES

The DJ Commodity Index was lower last week by -0.63% and is down month to date -0.13% (YTD +0.53%) as agriculture and industrial metals declined on concerns as to when tax and regulatory reforms will take place in the U.S.

Performance: I) **The price of oil** was up last week to $54.02 and is up month to date +1.41% (YTD +0.24%). Oil prices got a boost from U.S. Energy Information Administration data that showed crude **stockpiles grew less than expected** last week.

II) **The ICE USD Index**, a gauge of the U.S dollar's movement against six other major currencies, was positive, rising +0.22% from 100.90 to 101.12 for the week (MTD +1.61% YTD -1.23%). The U.S. dollar index **eked out a small gain** as the odds of a March interest-rate increase are declining, and a lack of new details surrounding President Donald Trump's fiscal-policy plans caused the dollar to drift over the past week.

III) **Gold rose last week** as growing concerns about geopolitics and the Federal Reserve's lack of commitment to lift benchmark interest rates also helped to support higher prices in the precious metals. For the week gold was higher by +1.78% climbing from $1236.0 to $1258.0 (MTD +3.81% YTD +9.20%).

HEDGE FUNDS

Hedge fund returns in February are higher with the core strategies Equity Hedge, Event Driven, Distressed, Macro and Relative Value all in positive territory.

Performance:

I) **The HFRX Global Hedge Fund Index** is higher at +1.24% MTD and +1.75% YTD.
II) **Equity Hedge** has risen +1.31% MTD and is up +2.17% YTD.
III) **Event Driven** is up MTD +1.61% and is higher YTD +2.67%.
IV) **Distressed Debt** is higher at +1.52% MTD and is positive YTD +1.87%
V) **Macro/CTA** has risen by +1.73% MTD and is up +0.76% YTD.
VI) **Relative Value Arbitrage** is higher at +0.48% and is up +1.12% YTD.

ECONOMIC DATA WATCH AND MARKET OUTLOOK

Looking ahead to next week, over the past week the **Dow Jones Industrial Average** did something that it has not done in 10 years, it **moved less than 1.0% in either direction** for 53 sessions in a row. While this has engendered concerns that the equity market is losing momentum, the absence of large price swings does not necessarily portend the demise of the record-setting rally of the past few months.

The S&P 500 has been similarly restrained. The large-cap index has not had a 1.0% move up or down in 53 trading days, the longest since July 2014, according to the Dow Jones Data Group. Since the market's breakout following the U.S. election, there have been several rallies and pauses, and neither has ignited a sharp selloff, suggesting that investors are unwilling to make large bets without a change of sentiment in the stock market.

With the potential for substantial policy changes in Washington, political risk in Europe and geopolitical concerns, there are many **reasons to be uncertain** at present. However, we believe the **markets and economy have become accustom to high uncertainty**. Thus, market pundits believe the markets can take policy shocks in stride until there is clear evidence of harm to the economy. President Trump is scheduled to give a joint address to the Congress on Tuesday where is he is expected to highlight his successes since taking office last month and outline his ambitious tax plan and infrastructure programs.

On the **economic data front**, **Monday durable goods orders** will be reported where trends have been gradually improving. Though volatile month to month, durable goods orders (consensus forecast +0.5%) have been gradually improving for the past year and, outside of defense aircraft, did perk up in December. And core capital goods (non-defense ex-aircraft) posted strong increases in December and November that point to new business investment and improved output.

The **second estimate for fourth-quarter GDP** will follow on Tuesday, as will January trade data on goods which will offer a key indication on GDP in the first quarter. The second estimate of fourth-quarter GDP is expected to come in at a consensus plus 2.10% annualized rate, up from 1.90% in the first estimate. Inventories are the unknown, in an outsized build that made up more than half of the first-estimate's growth. But consumer spending was solid in the first estimate, rising at a 2.50% rate.

Wednesday will see **personal income and consumer spending,** where the PCE price index will get special focus, particularly if it posts a sharp gain. Personal income has been growing in the modest 3.00 to 3.50% range the past year though the wages and salaries component has been in the 4.0% range. Similarly, consumer spending has been on a moderate rise to 4.0%. For January, forecasters see income rising a monthly 0.30% with spending also up 0.30%. Key in this report will be the PCE price index which has been on the rise and is expected to post a sizable monthly gain of 0.40% that would put it very close to the Fed's 2.0% target. The core PCE (less food and energy) is expected to rise 0.30%.

Vehicle sales (consensus 17.7 million) and the ISM also head Wednesday's data, the former offering the first hard indications on February retail sales and the latter a closely followed advance indication on the factory sector. The week then closes out with the ISM non-manufacturing report, which has been very solid, released on Friday.