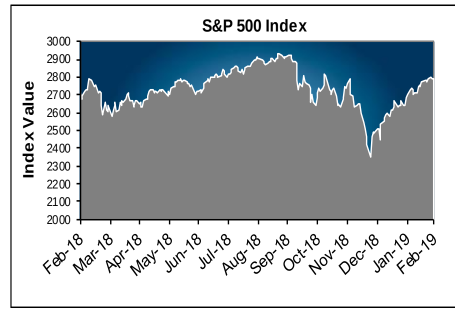
This Month in the Markets

February 2019

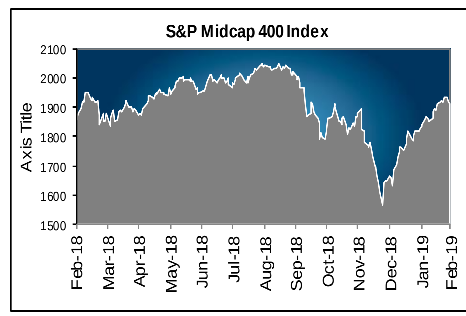
EQUITY COMMENTARY

Focus on the Positives

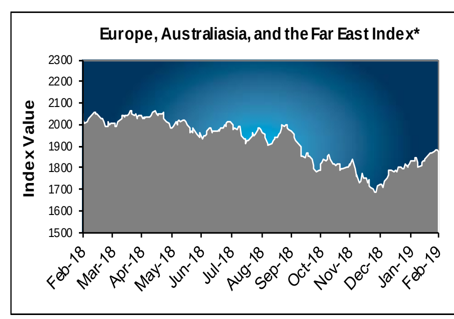
Equity markets continued their rally in February with positive Chinese trade developments, a much more dovish Federal reserve and Chinese stimulus. The MSCI World Total Net Return market index rallied 3%. The S&P 500 was up 3.2% while the MSCI Emerging Markets Net Total Return index posted a very small gain of 0.2% after outperforming over the last few months. Technology was the top performing sector in February while the REIT sector posted the smallest gains. The Bloomberg Commodities Index was up slightly by 0.8% - distillates posted slight gains while wheat slid.



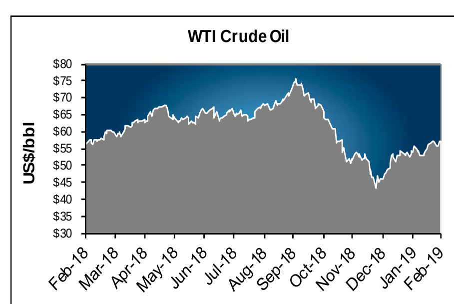
Economic and sentiment data through the U.S and Europe appears to be weakening. This has not been able to dampen spirits, however, as market participants seem to have swung from extreme pessimism to extreme optimism. We continue to be cautious given continued downward revisions in earnings, mixed to weak corporate guidance and tougher comparisons going into the next two quarters. We favor more defensive positions that have individual secular stories and remain warry of certain stocks that may be optically cheap but potentially expensive in a slowing economic environment.



Roper Technologies was the biggest gainer in the month with a surge of 14.3%. The company posted solid earnings and continues to be a cash-flow machine – its portfolio of companies continues to focus on asset-light, high free cash flow businesses with significant recurring revenue. We look forward to its next acquisition under new CEO Neil Hunn which we believe will continue to drive high returns on capital and expand its software as a service portfolio. The biggest detractor in the month was CVS Health which stumbled on losses in its long-term care business and growing concerns of political intervention within the health insurance market.



There was only one equity portfolio change overall - we bought Skyworks Solutions ("SWKS"). We remain constructive on 5G, - fifth generation cellular wireless. Clients will note that we already own another company that benefits from the roll-out of 5G – Cisco Systems. We also feel SWKS will benefit from the major technological upgrade as radio frequency content will be exponentially higher in 5G products. SWKS is a market leader in the radio frequency semiconductor chips market, which is expected to grow at a high single-digit to low-double-digit cumulative annual growth rate (CAGR) through the remainder of the decade. Additionally, the growing complexity of wireless technologies will boost radio frequency (RF) dollar content per device, contributing to sales and margin expansion. Growing wireless adoption in devices and the Internet of Things (IoT) should also bolster its Broad Markets segment. Despite the levelling off in smartphone demand, the company is still on track to drive further gross margin and operating margin expansion in the next few years.



*MSCI EAFE Index

FIXED INCOME COMMENTARY

Steady as She Goes

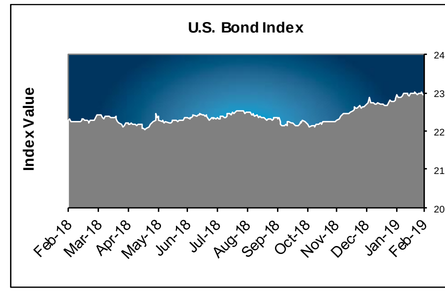
Credit spreads tightened across the board in February led by the high yield market, most notably the lower-rated cohort. Markets have been buoyed by a Fed that has stressed "patience" with regard to rate hikes and will likely cease the balance sheet run-off this year (the method with which the Fed controls the fed funds rate necessitates an elevated level of bank reserves). The USD was stronger month-on-month as U.S. economic data largely held-up despite the government shut-down, while euro area growth continues to wane. On the political front, headlines and comments from the administration signal that progress is being made on a U.S.-China trade deal. Indeed, in late February President Trump delayed the March 1st deadline when the U.S. was due to increase tariffs on $200 billion of Chinese exports to the U.S. As such the risk-on, low volatility environment that characterized January carried on into February.

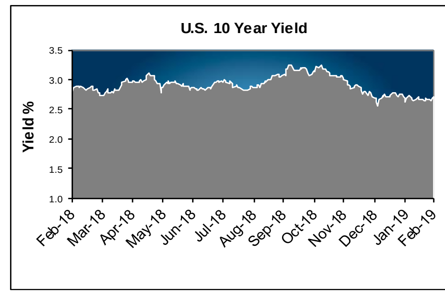
Interest rates were largely unchanged in February. The 10 year Treasury has traded in a narrow range since January and ended February at 2.71%. Investor positioning has shifted from short-bias to a neutral positioning indicating subdued expectations for upward rates movements in the near term. Indeed, the market is currently pricing zero Fed funds cuts/hikes in 2019 and one 0.25% rate cut by year-end 2020. These moves were driven by the shift in the Fed's outlook/rhetoric and slowing U.S. economic data, and the government shutdown. In addition to these factors that together have kept rates relatively low and subdued, the Fed is evaluating their framework for targeting inflation. If they move to a price targeting or average inflation target approach, it would suggest that the Fed will continue to hold off on rate hikes since inflation has undershot their 2% target for so long.

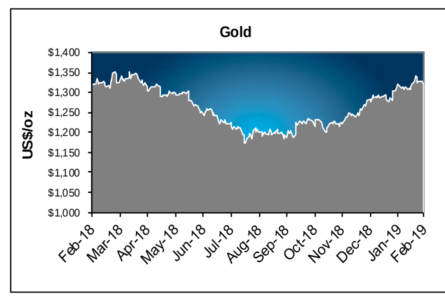
If either of the above approaches are adopted the Fed would essentially leave rates unchanged until inflation prints above the 2% target for a period of time (depending on the approach). The risks to leaving rates 'lower for longer' include the potential build-up of asset bubbles and possible rampant inflation. The labor market remains tight and wages have risen, however inflation has remained largely subdued.

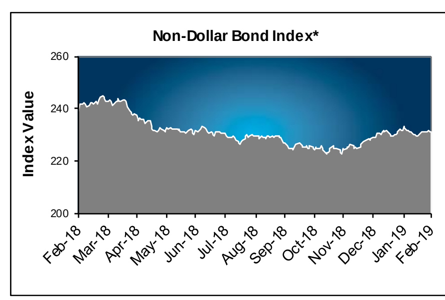
Inflation is a lagging indicator. Should inflation pick-up the Fed may eventually have to raise rates higher and quicker than it currently projects. It should be noted that run-away inflation is seen as very unlikely as evidenced by market pricing (break-even rates) and economic surveys. As such, this looks to be a trade-off the Fed is willing to accept. The Fed would rather have too much inflation versus no inflation or deflation. After all, the Bank of Japan and European Central Bank are mired in negative interest rates (according to Bloomberg there was USD$8.8 trillion of negative yielding debt globally at February-end) because of subdued inflation and slow (falling) economic growth.

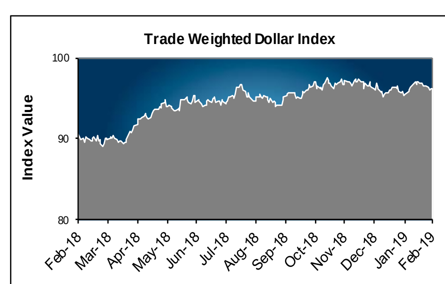
On the currency front, the dollar recovered from January weakness and is little changed on the year. Sterling has remained well bid this year despite Brexit fears and has rallied 3.2%. Weak economic data has hurt euro sentiment. Anchor remains selective in our non-dollar positioning as we believe interest rate differentials will continue to benefit the greenback.











*Merrill Lynch Global Broad Market, Ex US Dollar Index

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