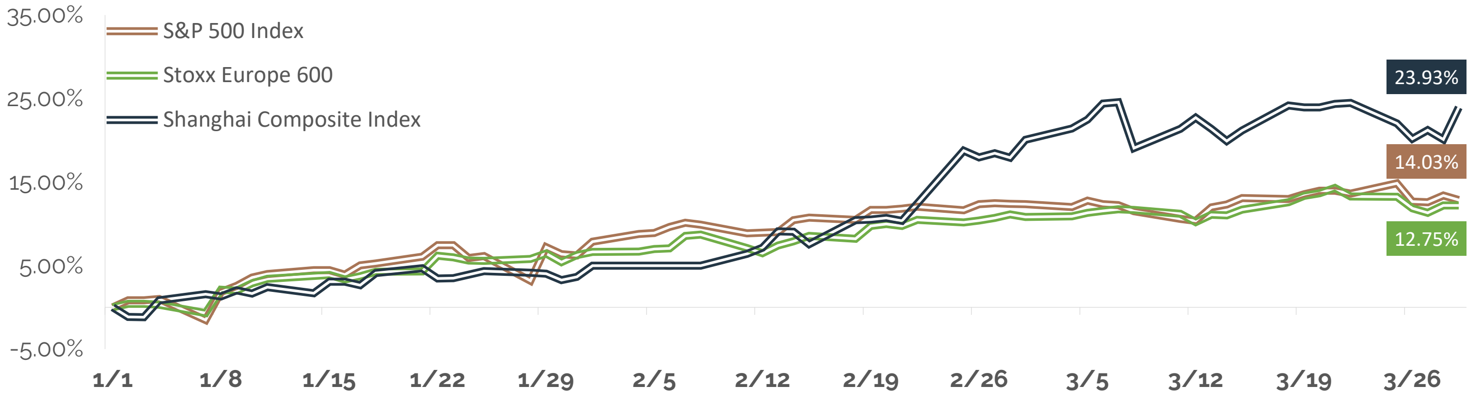


U.S. Stocks:

After a turbulent December, the U.S. stock market started off 2019 with the best January since 1989. The positive momentum continued throughout Q1, with the S&P 500 rising 14%. The U.S. stock market saw substantial inflows in March totaling $18B, due to optimism about trade talks, a halt on interest rate hikes from the Federal Reserve, and stronger reported economic data relative to global economies. The looming fears of a global slowdown favored U.S. based small-caps and high dividend companies. Information Technology continued to outperform the broad market. The Financial sector was particularly weak, with mutual funds losing $5.3B in funds and trailing the overall market by 6.1% (Figure 1). Banks sold off due to margin compression caused by the inverted yield curve (See U.S. Macro section).

Figure 1: Major Equity Fund Flows & Sector Performance Q1 – Data from Bloomberg and State Street

Equity Fund Flows Q1 2019

Region	Data Point
Emerging Markets	$13.1 B
United States	$10.7B
Global	- $2.5B
International Developed	- $0.7B

U.S. Largest Sector Fund Flows Q1 2019

Sector	Data Point
Real Estate	$2.9B
Communications	$2.5B
Health Care	$1.2B
Financial	- $5.3B
Energy	- $4.2B
Technology	- $2.7B

U.S. Best & Worst Sectors Q1 2019

Sector	Data Point
Information Technology	20.50%
Industrials	17.81%
Real Estate	16.67%
Utilities	10.10%
Financials	7.90%
Health Care	7.60%

According to Dow Jones Market Data, the S&P 500 logged its largest quarterly increase since June 2009. The ominous "fear of missing out" catch-phrase from the 1999 - 2000 tech bubble and 2008 financial crisis was recently quoted in a Wall Street Journal article describing equity markets. Despite cautious headlines the strong performance can be partially attributed to record profit margins and stock buybacks. Net margins for members of the S&P 500 hit 10.7% and stock buybacks rose to a record $223 billion, a 63% increase from a year earlier. The blowout corporate results in 2018 will certainly provide tough comparisons in 2019. Analysts had already lowered earnings-per-share estimates for 2019, dropping Q1 estimates as much as 4.1% according to FactSet.

Notable Company Specific Headlines from Q1:

- BB&T announced plans to buy SunTrust in the largest bank deal since the financial crisis ($28bn).
- AT&T defended its $85 billion merger with Time Warner against the Justice Department.
- Saudi-Arabia based oil giant Aramco finally disclosed its financial statements. The company turned a $111.1B profit in 2018, which is more than Apple, Google, and Amazon combined.
- Facebook is trying to stop the spread of fake news among its 200 million users in India ahead of general elections starting April 11th. The Israeli election is starting to face similar issues, making the spread of fake news on social media a growing global problem.

U.S. Macro News:

Key Economic Data	
Indicator	Data Point
Consensus Q1 GDP growth	1.50%
Consensus 2019 GDP growth	3.00%
Unemployment Rate	3.80%
Inflation Rate	2.20%
Federal Funds Rate	2.50%
3 Month Treasury	2.42%
1 Yr. Treasury	2.41%
2 Yr. Treasury	2.30%
10 Yr. Treasury	2.48%
WTI Crude	$60.14

The U.S. economy maintained strong footing throughout Q1. In January, Federal Reserve Chairman, Jerome Powell decided to keep the target range for the federal funds rate between 2.25% - 2.50%. In the February FOMC minutes, Mr. Powell remained upbeat about domestic growth prospects for the medium term. He continued to stress the risks from deteriorating growth in China and Europe. The market-based probability of a Fed rate cut this year is approaching 80%.

The ISM Manufacturing Index beat estimates in all three months. Despite slowing domestic industrial output growth, the U.S. continued to outperform other OECD countries by 4% - the highest difference since 1998 according to TS Lombard. This relative strength in U.S. manufacturing is due to lower reliance on demand from slowing Asian markets.

Wages grew at their fastest pace in nearly a decade in February, continuing to outpace inflation growth since 2013. Economists expect another strong wage growth reading for March. Some investors worry that the rising costs of labor can push corporate profitability down in the coming quarters. U.S. Personal Consumption remained subdued in January, registering - 0.1 actual vs 0.3 estimated. The low reading could be due to delayed tax refund processing for lower income households.

The brief inversion of the yield curve, starting March 22nd, brought discomfort to retail and institutional investors alike. Google search results for recession and yield curve inversion exploded at the end of March. The yield curve inversion refers to the 10-year treasury yield falling below the 3-month and 1-year yields. A term-spread model of recession probabilities from Refinitiv and Credit Suisse shows a 29% likelihood of a recession occurring within 1 year. At this level of probability, a recession has occurred within one year in 5 out of the last 7 such instances. In spite of all the recession fears from economists, a recent study by Andrew Bridgen on the International Monetary Fund's (IMF) success rate at predicting downturns found that IMF economists were only able to predict 4 out of 469 downturns one-year-out in the past. According to Bridgen, other major economic institutions had dismal track records as well, thus proving the challenge of economic forecasting.

Oil News:

The U.S. benchmark crude (WTI) oil price rebounded 32% in Q1, logging the biggest one quarter gain since 2009. Despite steady U.S. output, large cuts by OPEC and political uncertainty in Venezuela contributed to the oil price recovery. Saudi Arabia alone cut production by 1 million barrels per day (a 10% reduction). Venezuelan crude-oil production dropped 1.5 million barrels a day in 2018. The oil rally has increased U.S. gasoline prices at the pump to $2.71 on average, up 50 cents since January.

China

China's Shanghai Composite Index rallied 23.9% in Q1, 2019. Retail investors seem to be using leverage to boost their long positions in Chinese stocks in anticipation of a trade deal with the U.S. The rally seems highly speculative as economic indicators continue to show weaker fundamentals. China lowered its GDP growth target to 6.0% – 6.5% for the year from 6.5%. The combined January and February industrial profits were down 14% from the same time last year. Exports in the first two months of 2019 fell 4.7% year on year, reversing a rise of 3.9% in Q4 2018. Industrial growth also decelerated to 5.3% year on year in the first two months of the year from 5.7% in December 2018. According to U.S. and Chinese officials a U.S.-China trade deal might be on the horizon, which would boost economic conditions in China. According to Bloomberg, 1% of global GDP is exposed to the U.S. – China trade war.

The Chinese government took note of the slowing economy by announcing corporate tax cuts of 2 trillion yuan, or $298.31 billion. It is possible the stimulus is working, as the March Manufacturing PMI rose to 50.8 from 49.9 in the previous month. On the other hand, these tax cuts will draw funds away from infrastructure projects, which then will need to be financed with more special purpose bonds. These special purpose bonds are not reported in official government reports, yet they total $1.1 trillion or 7.4% of GDP. HSBC estimates that these off-the book bonds would increase Beijing's officially reported 2.8% budget deficit to around 8%. The People's Bank of China started to ease financial conditions to boost the economy and the stock market. It steadily decreased the Required Reserve Ratio for banks. This move has injected significant liquidity into the economy.

Europe

The European economy continued to face tepid growth with the euro-area economy expanding by a meager 0.2% in 4Q 2018. Italy remained in recession as output fell for the eighth consecutive month. German manufacturing activity slumped to an 80-month low of 44.1 (>50 equals growth). On February 20th, President Trump indicated that he could impose tariffs on autos from the EU, which would predominantly impact the German economy. The manufacturing PMI across the Eurozone hit 47.5 in March compared to 49.3 in February. The slowdown in manufacturing activity across Europe has been driven by weak external demand, mainly from China. With China's business activity stabilizing in March, we might see an uptick in business activity across Europe in Q2. While manufacturing remained weak across Europe, the Eurozone Services PMI surprised to the upside in March (53.3 v 52.7). The divergence between manufacturing and services further suggests that the Eurozone's economic weakness has been driven by external demand, not internal weakness.

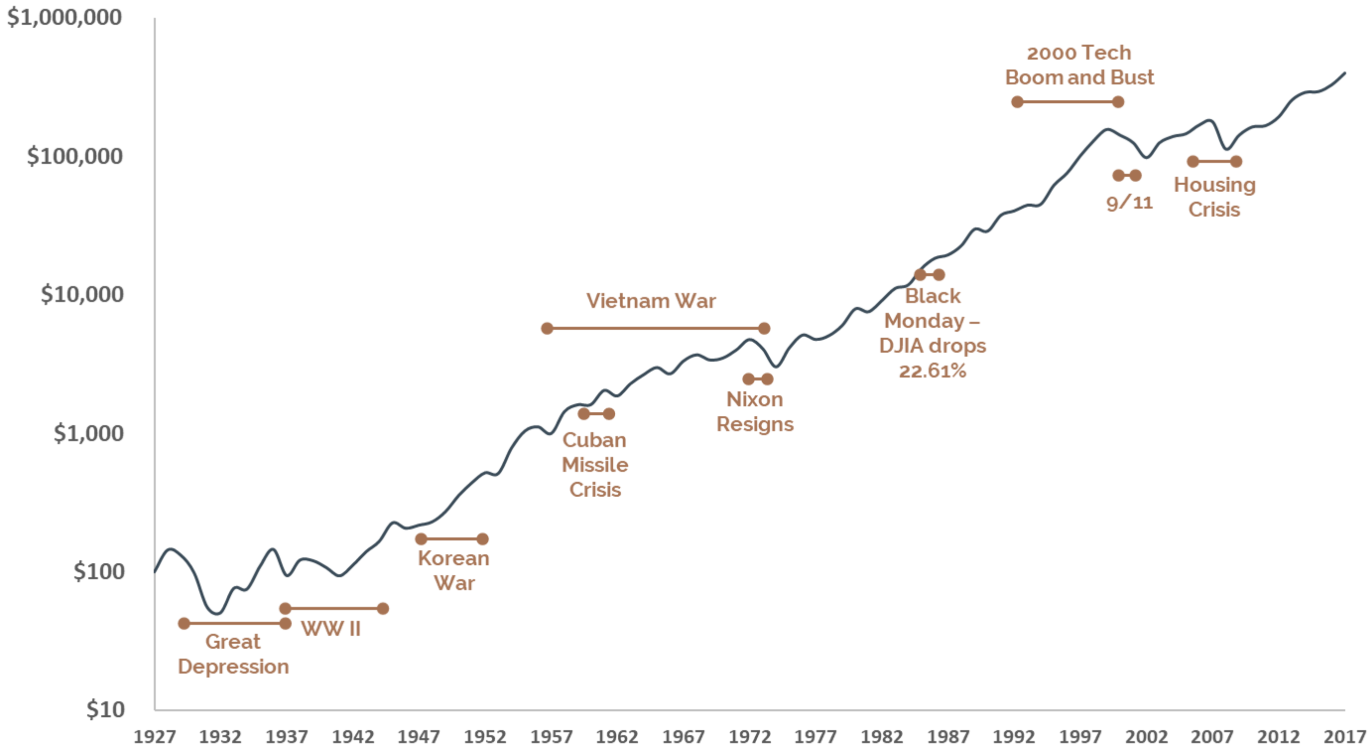
Brexit

The Brexit crisis deepened as the UK Parliament failed to find common ground once again. The following proposals were all shut down in the Parliament:

- UK-wide customs union with the EU
- Joining the European Free Trade Association
- Giving the public a vote to approve any Brexit deal
- Deal to prevent the UK exiting without any deal, including a vote to Revoke Article 50 (revoke Brexit itself)

Bloomberg estimates that about 0.9% of global GDP is exposed to Brexit trade risk. The U.K is most vulnerable with 10% of GDP embedded in exports to the E.U, and Ireland is not far behind at 9.7%. Around 2.7% of the euro area economy is exposed to trade with the U.K. In most recent developments the UK Parliament proposed another delay to Brexit negotiations. It is now up to the EU to accept the delay request. Interestingly the betting markets now assign one-in-four odds that the UK will hold another referendum and will vote to remain in the EU.

Interesting Chart: The Power of Compounding - Annual Return On a $100 Investment in Stocks from 1927 to 2017



Sources: Aswath Damodaran, NYU Stern, Annual Return on Stock

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The S&P 500 is a market capitalization weighted index of 500 leading U.S. companies and one of the most common benchmarks for the broader U.S. equity markets.

West Texas Intermediate (WTI) crude oil is the underlying commodity of the New York Mercantile Exchange's oil futures contracts.

The Consumer Price Index is used as a measure of Inflation. The Consumer Price Index (CPI) is a measure of the average change over time in the prices paid by urban consumers for a market basket of consumer goods and services. Indexes are available for the U.S. and various geographic areas. Average price data for select utility, automotive fuel, and food items are also available.

The NASDAQ Composite Index measures all NASDAQ domestic and international based common type stocks listed on The Nasdaq Stock Market. Launched in 1971, the NASDAQ Composite Index is a broad based Index. Today, the Index includes over 3,000 securities, more than most other stock market indices. The NASDAQ Composite is calculated under a market capitalization weighted methodology index. To be eligible for inclusion in the Composite the security's U.S. listing must be exclusively on the Nasdaq Stock Market (unless the security was dually listed on another U.S. market prior to January 1, 2004 and has continuously maintained such listing), and have a security type of either: American Depositary Receipts (ADRs); Common Stock; Limited Partnership Interests; Ordinary Shares; Real Estate Investment Trusts (REITs); Shares of Beneficial Interest (SBIs); Tracking Stocks. Security types not included in the Index are closed-end funds, convertible debentures, exchange traded funds, preferred stocks, rights, warrants, units and other derivative securities. If at any time a component security no longer meets the above eligibility criteria, the security is removed from the Composite Index.

The Stoxx Europe 600 is a subset of the STOXX Global 1800 Index. With a fixed number of 600 components, the STOXX Europe 600 Index represents large, mid and small capitalization companies across 17 countries of the European region: Austria, Belgium, Czech Republic, Denmark, Finland, France, Germany, Ireland, Italy, Luxembourg, the Netherlands, Norway, Portugal, Spain, Sweden, Switzerland and the United Kingdom.

The Shanghai Composite Index is a market capitalization weighted index made up of all the A-share and B-shares that trade on the Shanghai Stock Exchange. If at any time a component security no longer meets the above eligibility criteria, the security is removed from the Composite Index.

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