Market Commentary – February 2018

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Over the past 15 months, investors have benefited from an environment of strong equity returns and low volatility. During this time, the S&P 500 did not experience a drawdown of more than 3%. This type of atmosphere can happen but it is unusual. Over the last few days, we got a reminder that volatility and drawdowns can happen. In these types of situations, we ask ourselves what is driving the activity and has the fundamental picture changed.

There are several factors that may have contributed to the selloff. Over the past month, we have seen interest rates move higher, pricing in expected 2018 rate hikes and an increase in expected Federal borrowing related to tax reform. Inflation expectations have been moving higher due of higher commodity prices, a weaker dollar and wage inflation. The January employment report showed wage gains of almost 3%, versus a year ago. In addition, trading in volatility linked derivatives and exchange traded products may have contributed to some of the price action on Monday. Please note, we don't use these securities in our portfolios.

The fundamental economic picture has not changed, we are still seeing an acceleration of economic activity across the globe. January economic data, such as the Purchasing Manager's Index and the Unemployment Rate, show on-trend growth. The recent tax reform bill should provide an additional boost to growth in 2018 through higher corporate earnings, increased capital expenditures and wage increases.

While this type of price fluctuation can be a concern, we believe the fundamentals are still intact. While we stand ready to make adjustments to our portfolios if warranted, we are focused on the long term and remain constructive in our outlook.

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