

Capital Markets Flash Report

Overview

Global economic data this month was decidedly mixed. US GDP growth was 2.5% in the 1st quarter – better than the prior quarter but below expectations. Consumer spending increased in the 1st quarter largely to the detriment of saving. Business activity contracted in April while consumer confidence rose. Home prices added an impressive 9.3% in February. US inflation, however, is still quite low (PCE at 1.1%). In Europe, inflation is also low (1.2%) and unemployment rates are rising. Amid these mixed signals, what are central bankers to do? Well, there are two very clear signals globally: low inflation and high unemployment. Therefore, the market seems convinced (and logically so) that the Fed and the ECB will be staying all-in and are possibly set to increase easing measures.

US Equity

The S&P 500 gained 1.9% this month and is now up 12.7% this year. Small caps underperformed large caps by 230 basis points with relative weakness across all sectors, except financial services. In last month's report, we pointed out defensive sector leadership in the S&P 500. April saw many of the same sectors leading the S&P 500 higher while technology, materials, and energy continued to lag.

International Equity

Europe's equity markets added 4.5% in April while the Euro gained 2.7%. The rebound in equity pricing is a bit surprising in light of record Eurozone unemployment and persistently high levels of sovereign indebtedness. Expectations are sufficiently low, however, that even modest improvements in the outlook for Europe have shifted sentiment. Optimism is also rooted in the likelihood of an ECB rate cut later this week – now it just seems a question of how much of a cut (25 or 50 basis points)? Japan's equity market surged by nearly 9% this month as the Yen continued its stimulus-driven decline (down 3.5% versus the US dollar). For the year, Japan's equity market is up by over 20%!

These huge year-to-date equity gains in the developed markets convey a much different picture of global economic health than the losses in emerging market equities. At some point this divergence should revert but in April, the performance gap only expanded.

Hedge Funds

Given the recent disparate performance of global equities, it should come as no surprise that the early estimates for hedge strategies this month are highly correlated to geography. For instance, international (particularly Japan) long-short equity strategies have been some of the biggest winners while emerging market strategies have generally trailed other equity hedge strategies. More aggressive positioning (i.e., higher net exposure to equities and credit) has generally been rewarded. Global macro strategies and commodity traders have struggled year-to-date.

Fixed Income

The recent performance and near-term outlook for both fixed income and real assets appear to be highly linked. In April, global investors shunned their respective inflationary bets/US dollar hedges in the form of commodities, particularly gold, and bought into equity and bond markets. As a result, the current yield on the 10-year Treasury of 1.7% stands in stark contrast to the S&P 500 hovering near all-time highs. The last time the 10-year yield was this low was late 2012 and the S&P 500 was trading just above 1,400 (today we are near 1,600). Clearly, more investors are buying into the low growth/low inflation scenario and less concerned with rampant inflation stemming from excessive monetary stimulus.

Real Assets

The big story in commodities this month was obviously gold's catastrophic fall (down 7.5% for the month, adding to year-to-date losses). The overall commodity picture wasn't much better as base metals got hammered (pardon the pun) and crude oil prices were off 4-6%. Natural gas prices soared 6.8% and agricultural commodities were pretty steady as the outlook for this year's US crop production is good. REITs had another impressive run in April, adding 6.3%. For the year, REIT performance is now leading that of the broader US equity benchmarks.

US Equity Markets	Apr-13	YTD
Large Stocks:		
S&P 500	1.93%	12.74%
Russell 3000	1.64%	12.89%
Russell 1000	1.81%	12.97%
Russell 1000 Growth	2.12%	11.87%
Russell 1000 Value	1.52%	14.02%
Small Stocks:		
Russell 2500	0.31%	13.20%
Russell 2000	-0.37%	11.98%
Russell 2000 Growth	-0.66%	12.47%
Russell 2000 Value	-0.10%	11.52%
International Equity Markets**		
MSCI EAFE	5.33%	10.84%
MSCI EAFE Growth	4.34%	11.45%
MSCI EAFE Value	6.37%	10.23%
MSCI Europe	4.52%	7.48%
MSCI Japan	8.77%	21.50%
MSCI Emerging Markets	0.79%	-0.79%
Hedge Fund Markets***		
HFEX Indexes:		
Convertible Arbitrage	2.33%	6.10%
Distressed	0.49%	1.90%
Equity Hedge	0.27%	5.42%
Equity Market Neutral	0.24%	0.80%
Event Driven	0.61%	5.97%
Macro	0.46%	0.50%
Relative Value Arbitrage	0.48%	2.17%
US Fixed Income Markets		
U.S. Treasury Bonds ⁽¹⁾	1.07%	1.37%
Treasury Inflation-Protected Securities ⁽²⁾	0.78%	0.53%
Tax-Exempt Bonds ⁽³⁾	0.94%	1.31%
Corporate Bonds ⁽⁴⁾	1.23%	1.60%
High-Yield Bonds ⁽⁵⁾	1.60%	3.41%
Real Asset Markets		
DJ UBS Commodity Index Total Return	-2.79%	-3.89%
FTSE NAREIT Equity Index	6.33%	14.94%

(1) Fidelity Spartan Intermediate Treasury Bond Index is used as a proxy for intermediate US Treasury bond funds. (2) Vanguard Inflation-Protected Securities Fund is used as a proxy for US Treasury Inflation Protected Securities funds. (3) Vanguard Intermediate-Term Tax-Exempt Fund is used as a proxy for tax-exempt bond funds. (4) Vanguard Intermediate-Term Investment Grade Bond Fund (Admiral shares) is used as a proxy for intermediate corporate bond funds. (5) Vanguard High-Yield Corporate Fund is used as a proxy for high-yield corporate bond funds.

*Data Source: Bloomberg ** The MSCI returns are gross returns calculated in US Dollars. *** Hedge Fund Index returns are reported using Simple Price Appreciation and are only available on a one day lag. For complete Index Descriptions, please go to <http://www.greycourt.com/indices.html>