GREYCOURT

Capital Market Flash Report

January 2019 The big news was that the tension between tightening financial conditions and slowing growth was addressed, for the time being, by Chairman Powell's announcement that the Fed would pause its rate hikes and "adjust" its pace of quantitative tightening. The Fed reasonably caved to the needs of global growth, implicitly acknowledging by its reduced estimate of the natural rate of interest that it had already tightened too much. Risk assets surged and will continue to increase until markets come to grips with why the Fed capitulated.

US EQUITY

The S&P 500 had its best January since 1987 as the Fed shifted to a dovish stance. US Stocks were boosted by the December jobs report, stronger-than-expected earnings, rebounding oil prices, and optimism regarding US-China trade talks. Volatility fell on stellar returns across size, style, and sectors. Intra-index return dispersions, however, increased to well-above average levels, suggesting a higher risk regime than last year. Short-covering resuscitated tech stocks and higher oil prices propelled energy stocks.

	Month (%)	YTD (%)
S&P 500	8.0	8.0
Russell 1000	8.4	8.4
Russell 1000 Value	7.8	7.8
Russell 1000 Growth	9.0	9.0
Russell 2000	11.2	11.2
Russell 2000 Value	10.9	10.9
Russell 2000 Growth	11.5	11.5

NON-US EQUITY

Developed stocks rebounded materially from last month's dismal returns, notwithstanding mounting fears of a eurozone growth slowdown. The German ifo Index reached its lowest level since 2016, and the Euro-area composite PMI declined. A selloff in Italian bank shares also highlighted the ECB's limited capacity to manage non-performing loans. China had its slowest growth in nearly thirty years. Nonetheless, Fed pausing, a weaker US dollar, and future BOC stimulus led to outstanding EM performance.

	Month (%)	YTD (%)
MSCI All-Country World ex-US	7.6	7.6
MSCI EAFE	6.6	6.6
MSCI Europe	6.6	6.6
MSCI Japan	6.1	6.1
MSCI Emerging Markets	8.8	8.8
MSCI BRIC Index	9.9	9.9

FIXED INCOME

With the Fed acting as the world's central banker and pausing to revive global growth, US Treasuries rose. Strong US economic and employment data, Chinese stimulus, and trade optimism combined to lure investors back to investment-grade credits and very high-returning, high-yield bonds. Markets expected a modest rise in inflation, although Fed tightening will lower growth and housing data were weaker than expected. Light issuance and limited supply remain supportive of tax-exempt bonds.

	Month (%)	YTD (%)
U.S. Intermediate Treasuries	0.4	0.4
U.S. Long Treasuries	0.7	0.7
U.S. TIPS	1.3	1.3
Corporate IG Bonds	2.1	2.1
High-Yield Bonds	4.5	4.5
Tax-Exempt Bonds	0.8	0.8

CURRENCIES

The dovish Fed and higher relative inflation expectations pushed the US dollar down, despite strong domestic economic data and indications of slowing growth abroad. The Euro hit its lowest level in two months given evidence of eurozone weakness, Italy entering a technical recession, and the ECB's "temporary slowdown" rhetoric getting long in the tooth. During the month, growth concerns aided the yen and pressured EM currencies, until Chairman Powell's month-end statement pushed EM currencies much higher.

	Month (%)	YTD (%)
US Dollar	-0.6	-0.6
Euro	-0.2	-0.2
Yen	0.7	0.7
Emerging Markets[1]	2.6	2.6

REAL ASSETS

Commodities staged a broad comeback led by energy prices. Restricted oil supplies trumped demand concerns given OPEC cuts, Venezuelan turmoil, and lower US inventories. MLPs jumped in response. Natural gas prices surged on cold weather demand. Gold continued to rise as central banks gold buying hit the highest levels in almost 50 years. Russia, Turkey and Kazakhstan increased purchases to shift reserves away from the US dollar. REITs responded favorably to rate pauses that should extend the US recovery.

	Month (%)	YTD (%)
Commodities[2]	5.4	5.4
Energy	9.2	9.2
Industrial Metals	8.0	8.0
Gold	3.1	3.1
Master Limited Partnerships[3]	12.6	12.6
Real Estate Investment Trusts[4]	11.7	11.7

HEDGE STRATEGIES

Equity hedge, event driven, and distressed strategies performed well given increased exposures to riskier assets in the US and EM, long positions in the industrials and consumer discretionary sectors, and dynamic management of trade issues between the US and China. Equity market neutral strategies failed to add value given increasing dispersion and lacking broader market exposure in a bullish month. Macro strategies overall short positions were mis-timed and disproportionately unsuccessful.

	Month (%)	YTD (%)
Equity Hedge	3.7	3.7
Equity Market Neutral	0.1	0.1
Event Driven	2.4	2.4
Distressed	2.1	2.1
Macro	-2.7	-2.7

Data Source: Bloomberg. MSCI returns are gross USD. Currency returns are Simple Price Appreciation (SPA) USD basis. Fixed Income reported on Bloomberg Barclays Indices. [1]MSCI Emerging Markets Currency Index. [2]Bloomberg Commodity Indices. [3]Alerian MLP Index. [4]FTSE NAREIT Equity REIT Index. Hedge Strategies reported on HFRX Indices SPA with one-day lag. For complete Index Descriptions, see http://www.greycourt.com/indices.html