December 2018

Clark Capital Management Group

Benchmark Review
& Monthly Recap

A Challenging End to the Year

HIGHLIGHTS:

- It was the worst month for the S&P 500 Index since February 2009. After recovering somewhat in November, equities fell sharply to close out the year in negative territory.
- As stocks struggled, U.S. Treasuries rallied and almost all areas of fixed income (outside of high-yield bonds) saw gains in December.
- Despite capital market volatility, the U.S. economy continued to show growth in the fourth quarter as economic data was largely positive.
- Headline risks were a constant headwind to markets to close out the year as trade tensions continued with China, the Fed raised rates again and a partial government shutdown was in effect.

EQUITY MARKETS

December proved to be one of the most challenging months for stocks in years. The Santa Claus rally never materialized in December as stocks suffered one of their worst months in years. Despite gains over the final few trading days of 2018, stocks dropped and posted large declines in December, which pushed equities into negative territory for the year. The S&P 500 hit its lowest point of 2018 in a shortened trading day on Christmas Eve as the VIX Index spiked to its highest level since February.

Fed Chairman Powell did little to comfort the market after a mid-December FOMC meeting where policy rates were raised for the fourth time of 2018 and little flexibility seemed to be shown regarding the ongoing wind down of the Fed's balance sheet.

The numbers for December were as follows: The S&P 500 declined -9.03%, the Dow Jones Industrial Average fell -8.59%, the NASDAQ Composite lost -9.40%, and the Russell 2000 Index slumped -11.88%.

For all of 2018, the numbers were as follows: The S&P 500 declined -4.38%, the Dow Jones Industrial Average dropped -3.48%, the NASDAQ Composite slipped by -2.84% and the Russell 2000 Index fell by -11.01%.

Growth stocks, as measured by the Russell 1000 Growth Index, and value stocks, as measured by the Russell 1000 Value Index, both struggled in December dropping -8.60% and -9.60%, respectively. Growth stocks enjoyed a clear advantage to value stocks overall in 2018, but declines in December drove both of these indices into negative territory for 2018 with results of -1.51% and -8.27%, respectively.

International equities declined as well in December, but not to the extent of U.S. equities. However, they had already struggled through most of 2018, so the declines in December further exacerbated what was already a tough year. Trade issues with China continued to loom in December as the initial positive news of a trade war truce between the U.S. and China from the G20 meeting faded throughout the month.

Furthermore, the European Central Bank ended its bond-buying program in December, as this important economic region begins to change course with its own monetary policy as well. With this backdrop, emerging market equities, as measured by the MSCI Emerging Markets Index, declined -2.66% in December, which pushed 2018 losses to -14.58%. The MSCI ACWI ex USA Index, a broad measure of international equities, fell -4.53% in December, which put the losses for the year at -14.20%.

FIXED INCOME

The yield on the 10-year U.S. Treasury declined during the month from 3.01% to just 2.69% by the close of 2018, which created a more constructive backdrop for most fixed income sectors with the exception high-yield bonds. High-yield bonds had been one of the few pockets of strength in fixed income for much of the year, but this sector had a bad fourth quarter, punctuated by weakness in December, which pushed returns into negative territory for the year.

The declining rate environment helped the U.S. Treasury market show gains across the board during the month. Overall, the Bloomberg Barclays U.S. Aggregate Bond Index gained 1.84% in December, allowing it to sneak into positive territory for 2018 with a gain of 0.01%.

The Bloomberg Barclays U.S. Credit Index gained 1.50% in December, but it was still down for the year. TIPS and muni bonds also gained during the month. The Bloomberg Barclays U.S. Aggregate Corporate High Yield Index showed the most weakness as it declined -2.14% in December and ended the year down -2.08%.

ECONOMIC DATA AND OUTLOOK

Economic data released in December largely continued to reflect ongoing growth in the U.S. economy. However, broader macro concerns continued to exist and dominated market action including the pace of rate hikes by the Fed, ongoing trade issues with China, and a government shutdown.

The November Institute for Supply Management (ISM) manufacturing index exceeded expectations coming in at 59.3, marking its 27th consecutive month of growth in manufacturing. Meanwhile, the ISM non-manufacturing index, which represents the much larger service industries in the U.S. economy, also exceeded expectations, coming in at 60.7 for November compared to estimates of 59.0. This marked the third month in a row this index was above 60—recall that ISM readings above 50 indicate expansion. Non-farm payroll additions at 155,000 in November were below expectations of 198,000, but continued to reflect a solid labor market.

The unemployment rate stayed at 3.7% as expected. Average hourly earnings rose by 3.1% on a year-over-year basis, matching expectations and the prior month's mark. The Conference Board's leading economic indicators index (the Leading Index) increased by 0.2% in November, when it was expected to be flat, but the prior month's previously reported 0.1% gain was revised to show a -0.3% drop.

Both headline retail sales and retail sales excluding auto and gas stations sales were stronger than expected and prior month data was revised higher as well. The final reading of Q3 2018 GDP growth was lowered to 3.4% compared to the prior release and expectations of 3.5%.

The Federal Reserve (Fed) continues to be a central focus of the market and the scrutiny by the President and some market commentators has intensified. Although the rate hike in December was expected and the fourth in 2018, comments from Chairman Powell following the meeting were not as dovish as some expected and stocks continued to struggle.

The Federal Open Market Committee (FOMC) will be under heightened scrutiny in 2019 as this rate hike cycle enters into the latter innings. Any comments regarding the Fed's thinking on the pace for rate hikes in 2019 will be monitored closely.

Event	Period	Estimate	Actual	Prior	Revised
PPI Final Demand YoY	Nov	57.5	59.3	57.7	—
PPI Ex Food and Energy MoM	Nov	59.0	60.7	60.3	—
PPI Ex Food and Energy YoY	Nov	198k	155k	250k	237k
CPI MoM	Nov	3.7%	3.7%	3.7%	—
CPI YoY	Nov	3.1%	3.1%	3.1%	—
CPI Ex Food and Energy MoM	Oct	7100k	7079k	7009k	6960k
CPI Ex Food and Energy YoY	Nov	0.0%	0.1%	0.6%	—
Retail Sales Ex Auto and Gas	Nov	2.5%	2.5%	2.9%	—
Industrial Production MoM	Nov	0.1%	0.3%	0.5%	—
Building Permits	Nov	2.5%	2.7%	2.6%	—
Housing Starts	Nov	0.0%	0.0%	0.3%	—
New Home Sales	Nov	2.2%	2.2%	2.5%	—
Existing Home Sales	Nov	0.2%	0.2%	0.2%	—
Leading Index	Nov	2.2%	2.2%	2.1%	—
Durable Goods Orders	Nov	0.4%	0.5%	0.3%	0.7%
GDP Annualized QoQ	Nov	0.3%	0.6%	0.1%	-0.2%
U. of Mich. Sentiment	Nov	1260k	1328k	1263k	1265k
Personal Income	Nov	1226k	1256k	1228k	1217k
Personal Spending	Oct	575k	544k	553k	597k
S&P CoreLogic CS 20-City YoY NSA	Nov	5.20m	5.32m	5.22m	—
Leading Index	Nov	0.0%	0.2%	0.1%	-0.3%
Durable Goods Orders	Nov P	1.6%	0.8%	-4.3%	—
GDP Annualized QOQ	3Q T	3.5%	3.4%	3.5%	—
U. of Mich. Sentiment	Dec F	97.4	98.3	97.5	—
Personal Income	Nov	0.3%	0.2%	0.5%	—
Personal Spending	Nov	0.3%	0.4%	0.6%	0.8%

Event	Period	Estimate	Actual	Prior	Revised
S&P CoreLogic CS 20-City YoY NSA	Oct	4.86%	5.03%	5.15%	5.21%

P = Preliminary; S = Second; F = Final