Clark Capital Management Group

Benchmark Review & Monthly Recap

The Risk-on Rally Continues

HIGHLIGHTS:

- Stock market momentum continued in February after a powerful rebound in January. Double-digit gains across the major U.S. equity indices over the first two months of 2019 have repaired much (but not all) of the damage done during the fourth quarter equity market sell off.
- Volatility has moved consistently lower in 2019. After ending 2018 above 25, the VIX Index, a measure of equity market volatility, closed February below 15.
- A more dovish stance by the Fed has kept rates in check thus far in 2019. Although yields remained subdued for most of the month, a late month jump pushed the yield on the 10-year U.S. Treasury higher to around 2.73%. At the end of January, the yield was around 2.63%. However, this closing level for February was only a few basis points higher than where yields ended 2018.
- Trade tensions with China ameliorated in February and the March 1 deadline to raise tariffs on some of China's goods was delayed. While no final deal is in place, better news on the China trade front was a relief to the market and helped equities continue to rally in February.
- Risks remain as the Brexit outcome looks more and more unsettled and trade negotiations with China are ongoing. Despite these risks, the pessimism that overwhelmed the market in the fourth quarter seems to have abated and economic data has remained constructive this year, which has created a positive backdrop for equity markets so far in 2019.

EQUITY MARKETS

What a difference a couple of months can make. After a tough December and a fourth quarter that was one of the worst quarters of the post credit-crisis period, equities have bounced back strongly to begin the new year. While not pleasant to go through, the weakness in the fourth quarter improved valuations on U.S. stocks to some of their best (lowest) levels in years. Furthermore, the indiscriminate selling that took place during the fourth quarter provided opportunities for active managers to enter positions at valuation levels not seen in some time. Pessimism had reached extreme levels and market metrics pointed toward oversold conditions late in 2018. Following through on strong gains in January, equities continued to rise in February as economic conditions were not as dire as some had feared and negotiations with China generally trended in a positive manner. A "risk on" environment ensued and has been the driving theme so far in 2019. This is not to say that we won't experience more bouts of volatility as we move through 2019, but this year's performance to date seems to reflect a counter to the overdone nature of the sell off that took place in the fourth quarter of 2018.

The numbers for February were as follows: The S&P 500 advanced 3.21%, the Dow Jones Industrial Average (DJIA) rose by 4.03%, the NASDAQ Composite gained 3.60%, and the Russell 2000 Index, after being one of the worst pockets of equities in 2018, rallied 5.20% for the month.

Two months into 2019, the S&P 500 has gained 11.48% and the Russell 2000 has rallied 17.03% with the DJIA and the NASDAQ falling in between those two points. While not as pronounced for the month, growth stocks, as measured by the Russell 1000 Growth Index, maintained their advantage compared to value stocks, as measured by the Russell 1000 Value Index, gaining 3.58% and 3.20%, respectively, in February.

International equities continued to advance in February as well, but their gains were not as pronounced as U.S. stocks during the month. Although relatively unchanged so far in 2019, the U.S. dollar weakened modestly in January only to strengthen somewhat in February. However, we believe the headwinds faced by international equities in 2018, driven in

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large part by U.S. dollar strength, will be less intense in 2019 as multiple rate hikes by the Fed are highly unlikely this year. With this backdrop, emerging market equities, as measured by the MSCI Emerging Markets Index, gained 0.22% in February. The MSCI ACWI ex USA Index, a broad measure of international equities, performed better as developed market equities had stronger results, advancing 1.95% in February.

FIXED INCOME

The dispersion of bond returns truly reflected the "risk on" environment in February. The yield on the 10-year U.S. Treasury rose for the month and ended February around 2.73% with much of this move higher coming over the last couple days of the month. The stronger-than-expected GDP reading on the final day of February likely pressured U.S. Treasury prices lower and a subsequent rise in yields. With this backdrop, high-yield bonds were the clear leader in fixed income in February with strong gains as U.S. Treasuries were lower across most maturities during the month. Overall, the Bloomberg Barclays U.S. Aggregate Bond Index slipped by -0.06%, the Bloomberg Barclays U.S. Credit Index gained 0.22% and the Bloomberg Barclays U.S. High Yield Index advanced by 1.66% in February. TIPS were fractionally lower, but muni bonds continued their recent momentum and posted gains for the month. Most bond sectors are in positive territory two months into the year.

ECONOMIC DATA AND OUTLOOK

Economic releases remained somewhat disjointed in February due to the after effects of the government shutdown in January. However, progress was made and some key economic data points were finally released during the month. At the top of the list, the first reading of Q4 2018 GDP was released on the last day of February (about a month behind schedule), and it came in stronger than anticipated. While below the 3.4% annualized growth rate from the third quarter, the advanced reading of 2.6% GDP growth for the fourth quarter was ahead of expectations of a 2.2% gain.

Job market data remained strikingly strong as the January non-farm payroll additions totaled 304,000, a little less than double the expected gain of 165,000. However, significant revisions were made to the prior two months, which reduced those two readings by an aggregate 70,000 fewer job gains. The unemployment rate ticked higher to 4.0% in January coinciding with the labor force participation rate increasing to 63.2% from 63.1% when a drop to 63.0% was anticipated.

The January Institute for Supply Management (ISM) manufacturing index was improved from December and above expectations at 56.6. The ISM non-manufacturing index, which represents the much larger service industries in the U.S. economy, was below expectations at 56.7 in January and below December's mark. However, the initial December readings were revised higher for both the ISM manufacturing and non-manufacturing indices. Recall that ISM readings above 50 indicate expansion and both readings remained comfortably in growth territory.

Housing starts dropped sharply in December and were below expectations, but Building Permits were better than expected and slightly improved for the month. After consumer confidence readings took a hit in January, the reopening of the government and better stock market performance led to improved confidence levels in February. The Conference Board's leading economic indicators index (the Leading Index) dropped by -0.10% in January when a gain of 0.10% was expected. However, the prior month's initially reported decline of -0.10% was revised to 0.00% to show no decline occurred in December.

The next scheduled FOMC meeting is in March after no meeting took place in February. The dovish tone by Chairman Powell in January continued to reverberate in February and an additional rate hike in 2019 has become a much lower probability event. Markets will remain very sensitive to comments by the Fed as investors try to determine if the Fed will remain dovish in 2019 or whether that tone changes throughout the course of the year.

Event	Period	Estimate	Actual	Prior	Revised
ISM Manufacturing	Jan	54	56.6	54.1	54.3
ISM Non-Manf. Composite	Jan	57.1	56.7	57.6	58
Change in Nonfarm Payrolls	Jan	165k	304k	312k	222k
Unemployment Rate	Jan	3.90%	4.00%	3.90%	—
Average Hourly Earnings YoY	Jan	3.20%	3.20%	3.20%	3.30%
JOLTS Job Openings	Dec	6846k	7335k	6888k	7166k
PPI Final Demand MoM	Jan	0.10%	-0.10%	-0.20%	-0.10%
PPI Final Demand YoY	Jan	2.10%	2.00%	2.50%	—
PPI Ex Food and Energy MoM	Jan	0.20%	0.30%	-0.10%	0.00%
PPI Ex Food and Energy YoY	Jan	2.50%	2.60%	2.70%	—
CPI MoM	Jan	0.10%	0.00%	-0.10%	0.00%

Event	Period	Estimate	Actual	Prior	Revised
CPI YoY	Jan	1.50%	1.60%	1.90%	—
CPI Ex Food and Energy MoM	Jan	0.20%	0.20%	0.20%	—
CPI Ex Food and Energy YoY	Jan	2.10%	2.20%	2.20%	—
Retail Sales Ex Auto and Gas	Dec	0.40%	-1.40%	0.50%	—
Industrial Production MoM	Jan	0.10%	-0.60%	0.30%	0.10%
Building Permits	Dec	1290k	1326k	1328k	1322k
Housing Starts	Dec	1256k	1078k	1256k	1214k
New Home Sales	Dec	Postponed	—	—	—

Event	Period	Estimate	Actual	Prior	Revised
Existing Home Sales	Jan	5.00m	4.94m	4.99m	5.00m
Leading Index	Jan	0.10%	-0.10%	-0.10%	0.00%
Durable Goods Orders	Dec P	1.70%	1.20%	0.70%	1.00%
GDP Annualized QoQ	4Q A	2.20%	2.60%	3.40%	—
U. of Mich. Sentiment	Feb P	93.7	95.5	91.2	—
Personal Income	Dec	0.40%	1.00%	0.20%	0.30%
Personal Spending	Dec	-0.30%	-0.50%	0.40%	0.60%
S&P CoreLogic CS 20-City YoY NSA	Dec	4.50%	4.18%	4.68%	4.58%

P = Preliminary; A = Advance

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