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WealthManagement

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Market Insights

A periodic newsletter from Idaho Trust Bank

The global financial markets have struggled so far this year. Volatility levels have increased from the exceptionally low levels experienced last year. Uncertainties surrounding the global political landscape have clearly begun to impact the investment environment. Most central banks around the world are maintaining an accommodative policy outlook. However, the U.S. central bank has been boosting interest rates as the domestic economy continued to expand at a healthy rate.

Interest Rates

At the mid-March meeting, the Federal Reserve Bank (Fed) raised interest rates for the first time in 2018 (marking the 6th increase in the past 10 years). The target range of the Fed funds is now 1.50% – 1.75%. The domestic economy experienced a notable improvement towards the end of last year and the Fed members currently project that they will increase rates two additional times in 2018. Presently, inflation appears manageable, although it has ticked up a bit in the past six months. If inflation pressures move higher, it is possible that the Fed will increase rates three more times in 2018. However, at this stage we do not think this is a likely outcome.

The Fed appears to want to act before there are actual signs of inflation. The central bank has made an effort to convey the idea that economic activity levels

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will determine the path and timing of future interest rate increases. During the previous tightening cycle of the Federal Reserve, it raised interest rates by 0.25% at 17 straight meetings. This time, the Fed has made it clear that there will be no predetermined path.

First-Quarter Recap

Of the major U.S. indices, the Nasdaq Composite, which contains a large portion of technology companies, had the strongest returns in the first quarter. The Dow Jones Industrial Average and S&P 500, each containing a broader composition of companies, registered modest losses, as investors fretted over the economic impact of trade tariffs. International stock indices experienced similar struggles, although emerging market equities have experienced a small gain so far this year.

2018 Market Returns

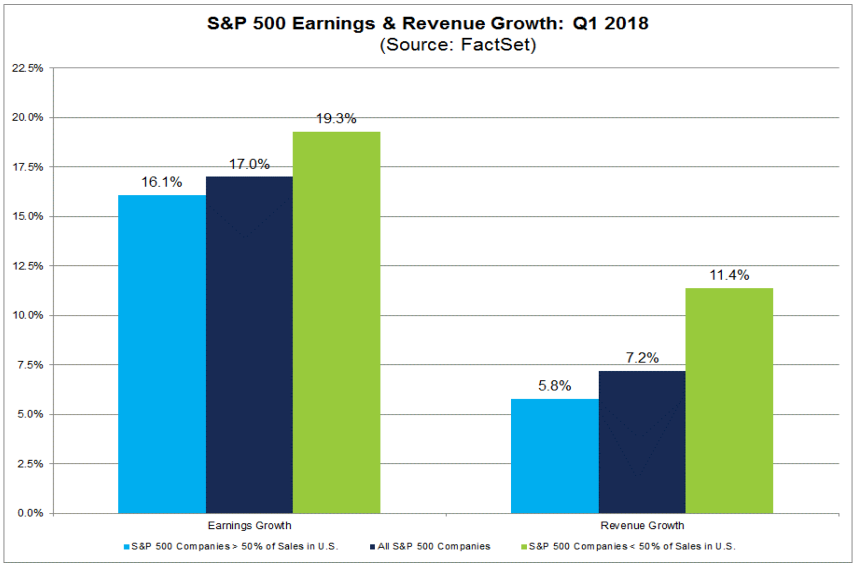
(Year to Date)

as of: March 29,2018:

Broad Market Returns	
S&P 500	-0.76%
Dow Jones Industrial Average	-1.96%
Nasdaq	2.59%
Russell 2000 - small cap	-0.08%
MSCI EAFE	-1.70%
MSCI Emerging Markets	1.28%
US Bond Index	-1.46%
Treasuries	-1.18%
Corporate Bonds	-2.32%
Municipal Bonds	-1.11%
Foreign Bond Index	3.51%
Commodities	-0.40%
Domestic Stock Sectors	
Information Technology	3.53%
Financials	-0.95%
Health Care	-1.22%
Energy	-5.88%
Consumer Discretionary	3.08%
Consumer Staples	-7.12%
Industrials	-1.56%
Utilities	-3.30%
Materials	-5.52%
Telecommunication Services	-7.48%
Real Estate (REITs)	-5.02%

Despite the challenges so far in 2018, a strengthening of the corporate earnings outlook helped boost returns last year. Other contributing factors, in our opinion, were an improving economic picture as well as continued support from most major central banks around the world.

Europe in particular has been the beneficiary of surprisingly stronger-than-expected economic conditions. Many sentiment indicators from Eurozone businesses and consumers have moved to some of their highest levels since before the financial crisis. In the U.S., strong earnings growth has been a crucial underpinning of the markets' performance. And a resilient tech sector, led by U.S. and Chinese giants, has had an increasing influence on markets domestically and in Asia.



The S&P 500 trades at about 16.5 times projected earnings over the next 12 months, a reduction from the over 18 times the index sold for at the start of the year. Despite the reduction, this valuation metric is still high by historical standards but is well below its forward multiple at the dot-com bubble's peak (of 26 times) in 2000. Valuations are more modest elsewhere around the globe. In Germany, the DAX trades at less than half its peak multiple in 2000. The forward earnings multiple for the Nikkei is around its 5 year average.

Strong performance from Technology companies has been an important contributor to the overall market returns. During the first three months of this year, the U.S Tech sector rose 3.5%. The Telecommunication Services sector was the biggest loser over the same time frame, declining 7.48%. The Energy sector also experienced a decline, falling 5.88%. A sharp decline in oil prices was a major factor and had a negative impact on the Dow Jones Industrial Average.

Conclusion

Given the relatively healthy state of the domestic economy, the pace of Fed interest rate increases will certainly have an impact on the financial markets. Another important variable will be the changing political and fiscal policy environment, which has created many uncertainties; from spending priorities to the impact of tariffs. Uncertainty surrounding these issues could add to the volatility this year, but the underlying foundation of economic health remains strong. We also think another important variable will be inflation expectations. If inflation rates begin to accelerate, the Fed will become more aggressive in tightening monetary policy.

S&P 500 Index

3 Month	-0.76%
Year-to-Date	-0.76%
1 Year	13.72%
3 Year	10.45%
5 Year	13.28%

MSCI EAFE Net Index

3 Month	-1.70%
Year-to-Date	-1.70%
1 Year	14.05%
3 Year	5.08%
5 Year	6.45%

Barclays Aggregate Bond Index

3 Month	-1.46%
Year-to-Date	-1.46%
1 Year	1.33%
3 Year	1.25%
5 Year	1.82%

As of 3.29.2018

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