2018 Weekly Portfolio Manager Commentary

January 29, 2018

Trustmark
Investment Advisors, Inc.

ECONOMIC HIGHLIGHTS

U.S. New Single-Family Home Sales came in at a 625,000 annualized unit rate for December. This was decently below expectations for a 680,000 unit rate and the 733,000 unit rate in November. The U.S. Index of Leading Indicators was up 0.6% for December, approximately as expected, with most strength in the new orders index. Durable Goods Orders were up 2.9% for December, for a yearly gain of a strong 11.5%. Finally, U.S. Real GDP growth came in at an annualized rate of 2.6% for the fourth quarter of 2017, a bit softer than expected. The price index was up 2.4% on an annualized basis for December.

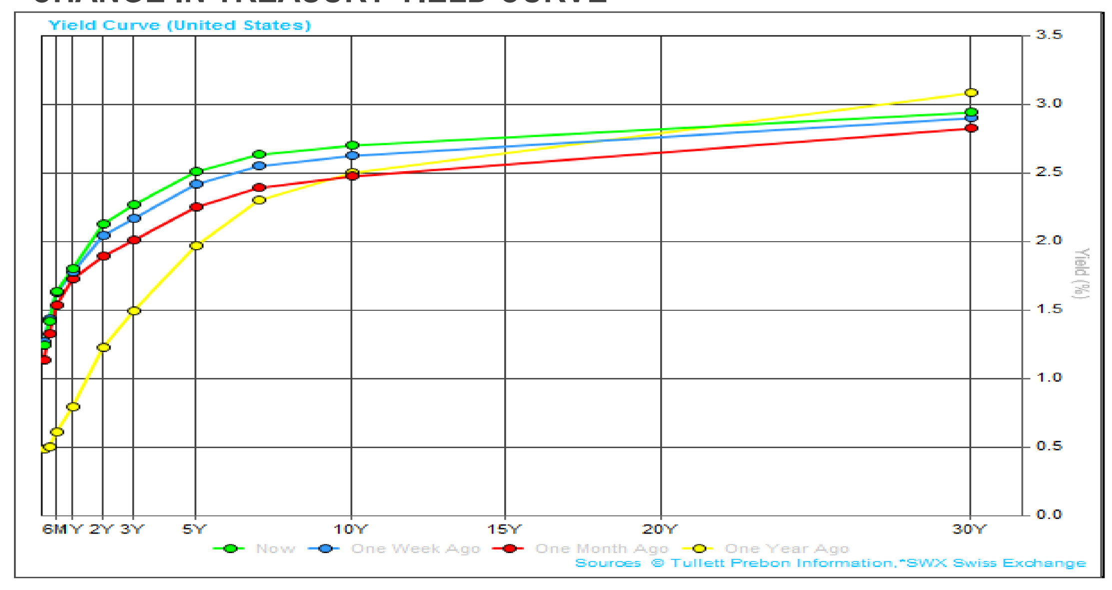
FIXED INCOME

The bond market has traded on inflation data and the prospect of rising sovereign-debt supply. The market has bet on Federal Reserve meetings and what the next chairman might do. And the market has wagered on jobs and wage growth that exceeded or missed projections. Now try doing it all in one week. With yields threatening to leap higher, bond traders will grapple this week with market-moving stimuli coming at breakneck speed. The sell-off in Treasuries less than a month into 2018 has already sparked calls of a bear market. U.S. domestic events are about to take center stage, after decisions by the Bank of Japan and European Central Bank left ten-year yields close to the highest since 2014. Traders will have a few things on their minds: Janet Yellen's final meeting as Fed Chair, the Treasury's plan to cover widening deficits, and, to cap it all off, an update on the U.S. job market. This week could wind up bolstering the prevailing view that yields are finally heading higher. While the Fed is seen standing pat, some Wall Street banks are bracing for a statement on January 31 that comes off as "more hawkish" than last month's, in part because of climbing inflation expectations. The ten-year breakeven rate is the highest since 2014, signaling demand for protections against accelerating inflation. Fed funds futures are pricing in more than 2.5 rate hikes by the central bank this year, close to policymakers' forecast for three. At the end of last week, options activity indicated growing interest in hedging against an extended sell-off. And then there's supply. The Treasury is expected to unveil bigger note sales this week for the first time since 2009. More issuance just as the Fed is trimming its balance sheet and has a green light from markets to keep raising rates? Sounds like a tough environment for bond investors. To be fair, not everyone's buying into the gloom. Dimitri Delis, senior econometric strategist at Piper Jaffray in Chicago, points to the deteriorating U.S. savings rate. As a share of disposable income, it fell to 2.6% last quarter, the third-lowest on record. This could lead to slower growth going forward.

CURRENT GENERIC BONDS YIELDS

TREAURIES		AGENCIES		CORPORATES		MUNICIPALS	
3 mo	1.41%	3 mo	1.45%	3 mo	1.82%	3 mo	1.25%
6 mo	1.63%	6 mo	1.48%	6 mo	1.93%	6 mo	1.31%
1 yr	1.78%	1 yr	1.62%	1 yr	2.02%	1 yr	1.38%
2 yr	2.12%	2 yr	2.09%	2 yr	2.28%	2 yr	1.50%
5 yr	2.47%	5 yr	2.37%	5 yr	2.75%	5 yr	1.83%
10 yr	2.66%	10 yr	3.00%	10 yr	3.29%	10 yr	2.39%
30 yr	2.91%	30 yr		30 yr	3.73%	30 yr	3.38%

CHANGE IN TREASURY YIELD CURVE



EQUITY

INDEX RETURNS	LAST WEEK	YTD
Dow Jones Industrials	2.09%	7.77%
S&P 500 (Large Cap)	2.23%	7.55%
S&P 400 (Mid Cap)	0.82%	5.03%
Russell 2000 (Small Cap)	0.66%	4.76%
NASDAQ Composite	2.31%	8.76%
MSCI EAFE (International)	1.51%	7.03%
iShares Real Estate	1.69%	-2.77%

The S&P 500 closed the week at yet another new all-time high – up for the ninth time in the last ten weeks. A little over three weeks into 2018 and several of the main sector groups are showing what would be considered strong annual returns – namely Consumer Discretionary and Health Care are both up over 10% and Technology is up over 8%. Income-oriented sectors – Real Estate and Utilities – are the only two sectors with year-to-date losses. Those two groups have been pressured by the rise in interest rates.

Bespoke wrote in a report last week that through the first 15 trading days of 2018, the S&P 500 is up 6.1% - this ranks as the 7th best start to a year going back to 1928, and the best start to a year since 1987's gain of 11.53%. The report noted that in years where the index is up at least 5% or more through January 23 – returns for the remainder of the year are all over the place, ranging from a loss of over 50% to a gain of over 25%.

Shares of Netflix rose over 10% on Tuesday after the company reported blowout subscriber metrics driven by original content and secular streaming tailwind.

Wynn Resorts fell over -10% on Friday after the Wall Street Journal reported a decades-long pattern of sexual misconduct by CEO Steve Wynn, citing dozens of people interviewed.

While it is early, this quarter's earnings reports have been positive. According to the latest *Earnings Insight* report from FactSet, 81% of the companies that have reported results so far have reported sales that have topped estimates. This is higher than the 64% average beat rate over the prior four quarters.

For the week ahead, it will be a full week of earnings reports. Notable companies expected to release results include: Pfizer, McDonald's, Facebook, Apple, and Amazon. Also of note is the President's State of the Union address Tuesday night and the FOMC rate decision on Wednesday.

The S&P 500 closed last week at 2872 marking a new all-time high. Support levels continue to rise along with the index and now stand at 2705, 2620, and 2530. The S&P 500 is now nearly 6% above its 50-day moving average and almost 12% above its 200-day moving average.

ASSET ALLOCATION

CURRENT SENTIMENT	
Cash	Neutral
Short Fixed Income	Neutral
Intermediate Fixed Income	Neutral
Inflation-Adjusted Fixed Income	Unfavorable
High Yield Fixed Income	Neutral
International Fixed Income	Neutral
Equity Income	Favorable
Large Cap Equity	Favorable
Mid Cap Equity	Favorable
Small Cap Equity	Neutral
International Equity	Neutral
Emerging Markets Equity	Favorable
Real Estate	Favorable
Commodities	Unfavorable

Below is a summery of our current stance on most asset classes:

Cash - Holding as little as possible given the miniscule yields in money market instruments. Any exposure is for defensive positioning.
Short Term Bonds - Relative to Intermediate Bonds, the reduced duration is preferable given the outlook for higher interest rates.
Intermediate Term Bonds - The current trading range of intermediate bonds warrants a neutral position with limited upside potential. Some opportunities still remain present in spread products.
Inflation-Adjusted Bonds - Low inflation expected in near-term providing zero real return.
High Yield Bonds - Spreads have tightened; however, still remain attractive versus Treasuries.
International Bonds - Emerging market bonds offer good diversification qualities while providing higher yield opportunities relative to domestic fixed income.
Equity Income - High quality and higher-dividend-paying companies remain attractive for long-term investors given their favorable risk-adjusted profile and current yield curves.
Large Cap Stocks - A favorable weighting is recommended. Growth has reemerged as a more favorable style and should be overweighed versus Value.
Mid Cap Stocks - Mid cap exposure along with a value tilt is preferred. Mid cap stocks continue to provide the "sweet spot" of market capitalization - large enough to provide stability, but small enough to be more nimble.
Small Cap Stocks - In broad market corrections, small cap stocks will suffer most with increased volatility. However, a recent divergence of relative strength between small caps and large caps warrants a neutral exposure.
International Stocks - Given most foreign investment is in developed markets and European countries, until sovereign debt concerns are alleviated, an underweight to neutral weight is recommended.
Emerging Market Stocks - Stronger balance sheets, less debt, and better growth potential make emerging markets more fundamentally attractive than developed countries longer-term. Recent relative performance versus developed markets support the stronger fundamental backdrop and positions have been added.
Real Estate - Pricing has stabilized and long-term valuations appear attractive. Real Estate has performed well of late and should continue to be a strong alternative to other asset classes.
Commodities - Global demand should support higher prices if the global recovery remains on track. Although, volatility will be higher and commodities will be susceptible to short-term price shocks, if used in conjunction with other asset classes, risk can be reduced substantially to a diversified portfolio. However, used alone is not recommended as the short-term outlook is not favorable.

Sources of statistical information are Bloomberg and Ned Davis Research.