2018 Weekly Portfolio Manager Commentary

August 31, 2018

Trustmark Investment Advisors, Inc.

ECONOMIC HIGHLIGHTS

U.S. Real GDP came in at 4.2% for the second quarter of 2018, with the GDP Price Index up 3.0%. This compares with Real GDP being up 4.1% the prior quarter. Pending home sales were down 0.7% for July and down 2.3% year-over-year. The West is bearing much of the negative price action. Personal Income was up 0.3% for July with the CORE PCE Index up at a 2.4% annualized rate. The Core PCE Index was up 2.0% year-over-year. Finally, the August Chicago PMI reading was 63.6, reflecting a strong U.S. economy.

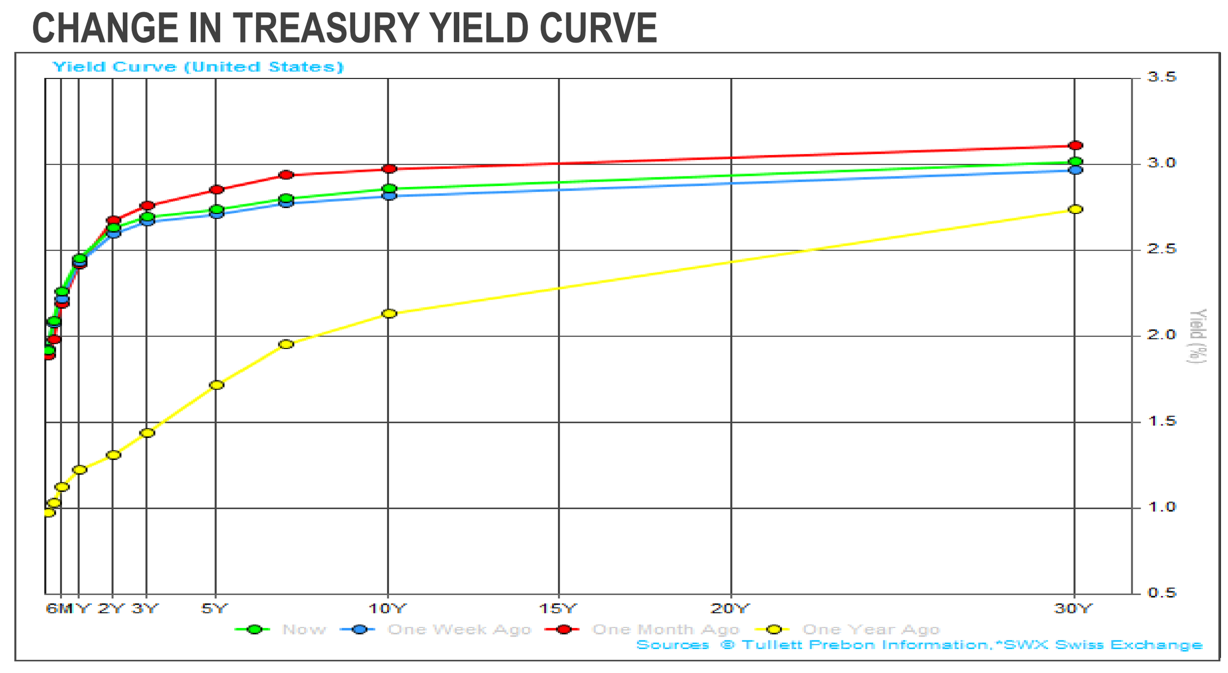
FIXED INCOME

This year's relentless climb in short-end U.S. rates may be about to take a break as the Treasury dials back Treasury bill auctions for a change. But any dip in rates may prove short-lived with another Federal Reserve rate hike looking imminent. The Treasury will sell a combined $145 billion of bills this week when the market reopens after the Labor Day holiday. The total is down $16 billion from the previous week, for the first across-the-board cut in bill supply since April. Bill rates have climbed steadily this year, pushing three-, six- and twelve-month yields above 2% for the first time in a decade. The drop off in supply probably won't last long. Traders anticipate increased issuance across the curve to finance the nation's ballooning budget deficit and offset the Federal Reserve's balance-sheet unwind. What's more, Friday's release of the latest labor-market data may solidify expectations for a quarter-point Fed rate hike this month as job growth likely accelerated in August, according to analysts surveyed by Bloomberg. "This is the breather," said Thomas Simons, a money-market economist as Jefferies LLC. "Treasury is going to have to build up supply quite a bit beginning in October." The Treasury will issue $55 billion of one-month bills, $48 billion of three-month bills and $42 billion of six-month bills. The auctions will pay down $18 billion of outstanding supply, part of the $61 billion decline in supply that some economists expect over the next month, in part as the government's cash flow picks up as quarterly tax payments ramp up. But come October, Wall Street predicts issuance to pick back up. That's why analysts, including at Citigroup Inc. and Deutsche Bank, have recommended wagering that short-term funding costs will rise again, from repurchase agreements to the London interbank offered rate. That renewed pressure on short-end rates could play into bets on further yield-curve flattening in the coming months. For Simons at Jefferies, with the Fed still projecting gradual rate increases, maybe the only thing that could derail the flattening trend is a potential shift on Treasury's part to lean more heavily on longer maturities in upcoming auctions. "I don't see how the long end breaks out until there's a lot more pressure from issuance," he said. Other factors that remain in play include the U.S. being poised to put tariffs on an additional $200 billion in Chinese imports, and Beijing is expected to retaliate immediately, soon after the Trump administration's public comment period expires later this week. There are several Fed president's speaking this week which could affect the markets depending upon the tone of their messages. There is basically a 100% change of another rate increase later this month so many markets participants will be dissecting the message of what may be in store from the Fed for the remainder of the year.

CURRENT GENERIC BONDS YIELDS

TREASURIES		AGENCIES		CORPORATES		MUNICIPALS	
3 mo	2.09%	3 mo	2.14%	3 mo	2.35%	3 mo	1.47%
6 mo	2.26%	6 mo	2.29%	6 mo	2.46%	6 mo	1.52%
1 yr	2.45%	1 yr	2.43%	1 yr	2.57%	1 yr	1.58%
2 yr	2.63%	2 yr	2.64%	2 yr	2.85%	2 yr	1.72%
5 yr	2.74%	5 yr	2.82%	5 yr	3.21%	5 yr	2.09%
10 yr	2.86%	10 yr	3.17%	10 yr	3.63%	10 yr	2.63%
30 yr	3.02%	30 yr		30 yr	4.09%	30 yr	3.57%

CHANGE IN TREASURY YIELD CURVE



EQUITY

INDEX RETURNS	LAST WEEK	YTD
Dow Jones Industrials	0.79%	6.73%
S&P 500 (Large Cap)	0.98%	9.94%
S&P 400 (Mid Cap)	0.51%	8.67%
Russell 2000 (Small Cap)	0.91%	14.26%
NASDAQ Composite	2.07%	18.32%
MSCI EAFE (International)	0.03%	2.30%
iShares Real Estate	0.81%	4.54%

U.S. stocks dropped this past Friday on news that further trade war clashes with China were on the horizon. Despite the disparaging news, the S&P 500 is on pace to notch the best August since 2014. The Nasdaq is on track for the best August gain since 2000.

Last week, the Dow was up 0.8% and the S&P 500 is up 0.98% and the Nasdaq is up 2.07%. For the month of August, the Dow gained 2.38%, the S&P 500 rose 3.26%, and the Nasdaq climbed 5.85%.

Last week Thursday, Bloomberg reported that President Trump intended to move forward with his $200 billion tariff plan in additional Chinese imports as early as next week. In addition, the president threatened to withdraw the U.S from the World Trade Organization. On the positive note, the U.S and Canada were able to conclude trade negotiations last week Friday.

Coca-Cola (KO) announced last week Friday that the conglomerate will buy British coffee chain Costa, for $5.1 billion. Shares of Coke dropped 0.3%.

Lululemon Athletica (LULU) announced better-than-expected second-quarter earnings last week Thursday and also raised its full-year outlook. The stock was up 14% last week Friday and is up nearly 100% this year alone.

Year to date, Information Technology accounts for more than half of the gains (Technology companies account for one quarter of the Large cap index) in the S&P 500 according to Bespoke Research group. This is twice as much as the next highest sector – Consumer Discretionary. The only other sector with any meaningful contribution after Tech and Discretionary companies has been Health care, which is up 18.4%. The gains in small caps, on the other hand, are more evenly distributed across sectors, with Health Care contributing the most.

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.