consequent capital management

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Capital Markets Review and Outlook

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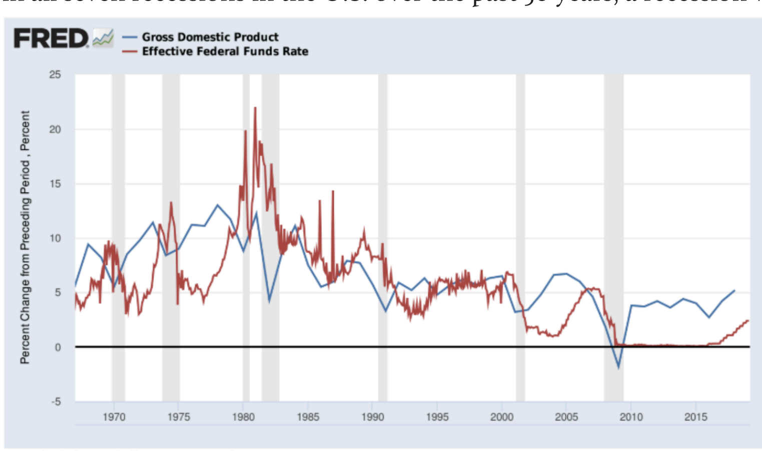
Economy and Outlook

In February, concerns waned further about an impending recession in the U.S. The first release of GDP growth for the 4th quarter of 2018 showed an annualized increase of 2.6%. Although this pace is slower than the growth for the preceding two quarters, it represents a 3.1% increase in real GDP from the 4th quarter of 2017 making it the strongest year-over-year growth for the U.S. economy in over 4 years. While global economic growth has undoubtedly slowed down, in large part due to the trade war between the world's two largest economies (the U.S. and China), the underpinnings for continued global economic expansion remain in place. Labor markets around the world are sturdy with year-over-year employment gains of 1% to over 2%. Despite the firmness in labor markets, inflation remains under control due to intense global competition together with the downward pressures on pricing from the widespread adoption of technological innovations across a wide swathe of industries. As a result, global central banks monetary policies remain accommodative. The U.S. Federal Reserve has reiterated its 'patient' and 'data-dependent' stance regarding further hikes in interest rates. At the same time, official interest rates of central banks in major developed regions such as the Eurozone and Japan are zero and negative respectively. The magnitude of loose central banks' monetary policies in developed markets is reflected in the approximately $8 trillion in global bonds with negative interest rates. Additionally, monetary policy easing is taking place even in major developing countries like China and India. One of the primary catalysts for the global economic recovery from the Great Financial Crisis over 10 years ago was the unprecedented monetary stimulus from central banks and the ensuing low interest rate environment. Therefore, despite a deceleration in economic growth, low inflation and low interest rates are likely to continue providing a positive tone for the risk markets. Additionally, the likelihood of a recession remains low in a low interest rate environment. The chart on the left shows that in all seven recessions in the U.S. over the past 50 years, a recession was preceded by a period when the Federal Reserve had raised interest rates to a level that was higher than the growth rate of nominal GDP. The current 2.5% federal funds rate is well below the most recent 5.2% growth rate in nominal GDP.



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Equity Markets

For the month of February, risk markets added to their strong gains from the prior month, while volatility continued to decline. The Russell 3000 Index, a broad representation of the domestic equity market, had a return of +3.5% in February bringing its return for the first two months of 2019 to a remarkable +12.4%. With over 95% of the S&P 500 companies reporting 4th quarter earnings, the earnings growth rate is +13.1% based on FactSet. This represents the fifth consecutive quarter of double-digit earnings growth underscoring the resilience of the markets investment performance. The strong equity market returns were accompanied by a reversal of the defensive positioning by capitalization and style in the last quarter of 2018. The Small and Mid Cap asset classes outperformed Large Cap, while Growth outperformed Value across the capitalization spectrum, most noticeably in Small Cap and Mid Cap. Performance differentiation was similarly reflected at the sector level with defensive sectors such as utilities, consumer staples and health care underperforming the cyclical sectors such as industrials, information technology and consumer discretionary. Outside the U.S., emerging markets were relatively unchanged for the month, taking a breather after strong performance since the end of October 2018. Developed markets, however, added another +2.5% in February which resulted in a +9.3% return for the first two months of 2019.

Fixed Income Markets

Despite the Federal Reserve's stated patient stance on further interest rate hikes, the second consecutive month of strong equity market returns reversed the prior quarter's flight to safety and pushed Treasury yields higher by 7 to 10 bp across the yield curve. The absence of Fed action in the near-term caused the Treasury yield curve to steepen by 3 bp as the brunt of the selling fell on longer maturity securities. The positive tone in the equity markets was reflected in the corporate bond market and spreads narrowed for the month. The high yield market was the biggest beneficiary as spreads tumbled -44 bp resulting in a return of +1.7% for the month, and +6.3% for the first two months of the year. The corporate credit curve steepened as intermediate corporate bonds outperformed longer maturity issues across the major sectors.by 2 to 5 bp in relative spread tightening. On the other hand, the corporate quality curve flattened by 3 to 6 bp in spread tightening as BBB-rated issues outperformed Single-A and higher rated securities. The non-dollar fixed income markets underperformed in February. Although there was little change in the value of the dollar as represented in the Federal Reserve's broad priced-weighted dollar index, the U.S. dollar was higher versus the euro and the Japanese yen, both of which have material weights in the non-dollar global bond market.

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			Returns as of 2/28/19 (In %)			
		Month	YTD	1 Year	3 Years	5 Years
Russell 3000®	US AllCap Equity	3.5	12.4	5.0	15.5	10.2
Russell 1000®	US Large Cap Equity	3.4	12.0	5.0	15.4	10.4
Russell 1000® Growth	US Large Cap Growth	3.6	12.9	6.6	18.0	12.6
Russell 1000® Value	US Large Cap Value	3.2	11.2	3.2	12.8	8.1
Russell Midcap®	US Mid Cap Equity	4.3	15.5	5.6	14.5	8.6
Russell Midcap® Growth	US Mid Cap Growth	5.9	18.0	9.8	17.2	10.2
Russell Midcap® Value	US Mid Cap Value	3.2	13.8	2.6	12.6	7.4
Russell 2000®	US Small Cap Equity	5.2	17.0	5.6	16.7	7.4
Russell 2000® Growth	US Small Cap Growth	6.5	18.8	6.7	18.3	8.2
Russell 2000® Value	US Small Cap Value	3.9	15.2	4.4	15.0	6.5
MSCI ACWI ex-US	Global Equity ex-US	2.0	9.7	-6.5	10.7	2.5
MSCI EAFE	Global Developed Mkts Equity	2.5	9.3	-6.0	9.3	2.1
MSCI EM	Emerging Mkts Equity	0.2	9.0	-9.9	15.0	4.1
Bloomberg/Barclays US Agg	US Core Fixed Income	-0.1	1.0	3.2	1.7	2.3
Bloomberg/Barclays US Interm. Agg	US Intermediate Fixed Income	0.0	0.9	3.4	1.4	2.0
Bloomberg/Barclays US Credit	US Corporate Bonds	0.2	2.4	2.7	3.5	3.1
Bloomberg/Barclays US MBS	US Mortgage Backed Securities	-0.1	0.7	3.6	1.4	2.3
Bloomberg/Barclays US Corp HY	US High Yield	1.7	6.3	4.3	9.8	4.5
FTSE Non-US WGBI	Global Fixed Income ex-US	-1.3	0.6	-3.6	1.9	-0.2