STONEBRIDGE
Capital Advisors

The Stonebridge Market Commentary

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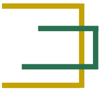
Equity Commentary provided by David A. Eckenrode
Director of Equity Management

Fixed Income Commentary provided by Jon F. Lynn
Senior Analyst & Portfolio Manager

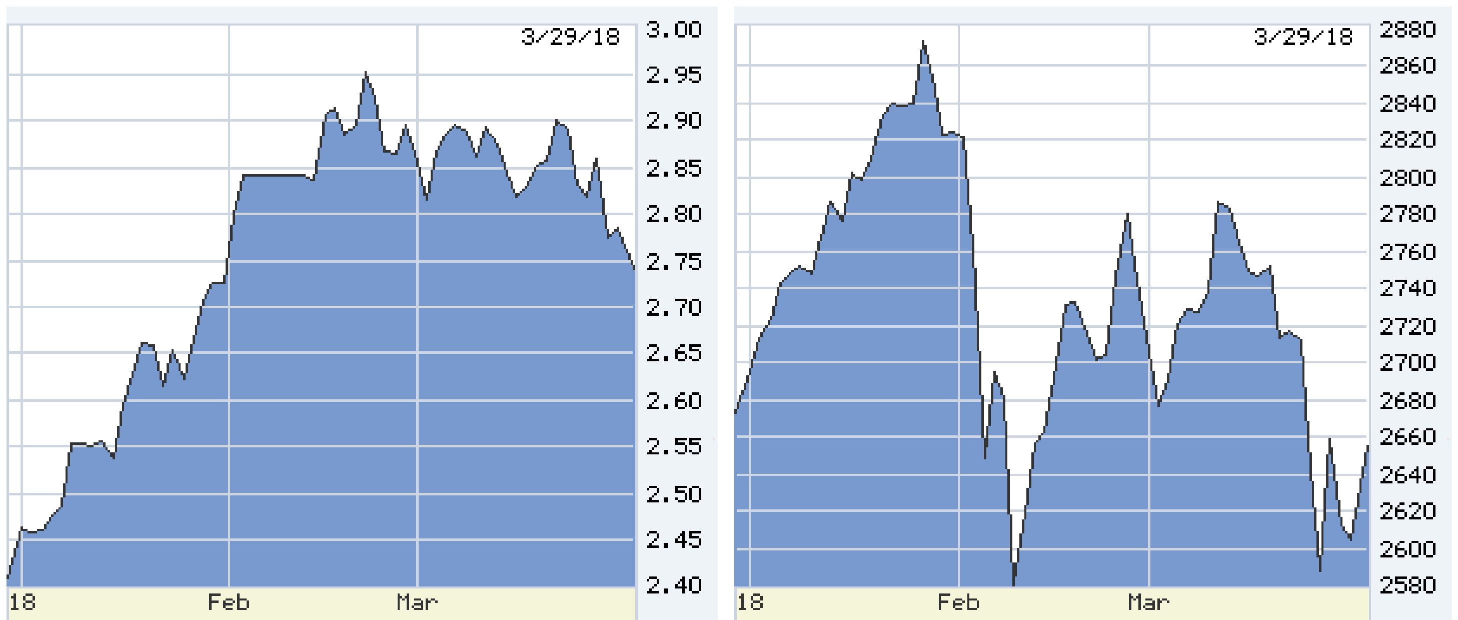


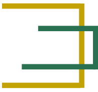
Equity Market Commentary

Well we have managed to make it to Spring, the end of March and with it, the end of the first quarter. After a great January, the markets have taken a downward turn. We have had now two months in a row down and the first quarter overall, as well. The last time that happened was the 3rd quarter of 2015 and the last time we had two or more down months in a row was August, September, October of 2016. We have had quite a ride, indeed. So, the quarter was down 1.17% for the S&P, 2.26% for the Dow and up 2.33% for the NASDAQ. Interestingly, there remains a big divergence between growth stocks and value stocks with the Russell Growth Index up 1.42% for the quarter and The Russell Value Index losing 2.83%. These divergences happen, of course, but bear watching. They may converge on the way to the value side being more loved.

So, what exactly happened? It seemed to begin after the new Fed Chair made some comments in testimony that essentially said that the economy was strengthening. Cue the move up in interest rates and inflation fear. Cue the fear about an overaggressive Fed pushing rates up too high. That set of events set us on a very quick 10% drop, a level that we are still dealing with. So, after the initial drop, the market recovered some lost ground before having a test of the February lows on the Facebook privacy news. This Facebook drop has spread to a number of major names in techland like Twitter, Amazon, Google, Apple and Microsoft. We now have another meme to deal with, namely the "Techwreck." Below, you can see charts for the Ten Year Treasury (chart 1) and the S&P (chart 2) respectively.

Chart 1 & 2





A decline of 10% is entirely normal in the market and happens with regularity in any long bull market. So, this nothing to get overly concerned about at this point. The techwreck aspect of it bears some examination. The aforementioned tickers FB, MSFT, AMZN, AAPL and TWTR have been a very big part of the market run up the last 5 quarters. If investors abandon them in favor of more staid names, we will likely have some trouble attaining the January highs.

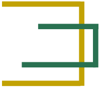
Then there was the mini meltdown over the "Trade War." First it was tariffs on steel and aluminum which quieted down when many of our trade partners were exempted. Then it was the trade with China. We levied some tariffs on some Chinese imports and they retaliated somewhat. Now it seems that the whole kerfuffle was the beginning of a negotiation. Quelle horreur!

Our guess is that some investors will pull back a bit to see where this leads. They may trade a few tech names for higher dividend payers but will be back when they see these names making money for investors again.

Facebook will probably change some procedures, apologize and pay a fine to the FTC. Zuckerberg will be dragged before Congress and lectured with faux outrage (it is an election year after all). Amazon, likewise being pilloried for tax issues by the President, will make some agreement like all of the times they have come under fire and be allowed to go their merry way. The EU, ever in need of tax revenue, will fine them both and maybe more over some faintly defined "anti-competitive behavior." This will take time to roll out but the pattern seems set based on what we know at this point.

One thing that we can say with some certainty is that the era of extremely low volatility has come to a screeching halt. We are likely to stay elevated for a while more it seems. In chart 3, you will see the most recent fear gauge. Investors just got a taste of risk in their investment portfolios that they have largely been insulated from for more than a year.

Chart 3



As usual, we will have to see how this change in attitude plays out. We suspect that this is a correction in a bull market and with earnings season just around the corner, we may be on to a better news cycle. The tax cuts are going to be mentioned in a positive way in many earnings conference calls.

Fixed Income Market Commentary

Rates have continued to march higher over the last month, at least on the shorter end of the curve. Further out, yields finished the month largely where they started it. Despite touching a high of 2.90% mid-month on the 10-year Treasury, the yield actually fell slightly to end at 2.74%. 6-month Treasuries rose about 10 basis points to 1.95%. A testament to just how flat the yield curve has become, 6-month Treasuries now yield about 65% of 30-years. Our fixed income strategy (whether taxable or tax-exempt) continues to focus on shorter bond maturities where most of the yield is offered on the curve. For example, this week we were buying 1-year Travelers Insurance Company bonds (A-rated) at a yield of 2.60%. Just for comparison, its 20-year bonds are currently only yielding around 4.00%. On the tax-exempt side, we bought a bit longer St. Louis bond with a 7-year final maturity. That is callable in 2 years to yield 2.15% to the call and 3.06% if it remains outstanding until maturity. That is over 5% on a taxable equivalent basis for investors in the top tax bracket and it is just 7 years, at most!

Sources

Charts provided through Wall Street Journal and Market Watch

Performance sourced from Bloomberg

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