STONEBRIDGE
Capital Advisors

The Stonebridge Market Commentary

November 1, 2018

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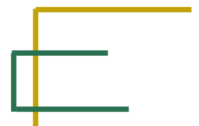
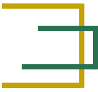
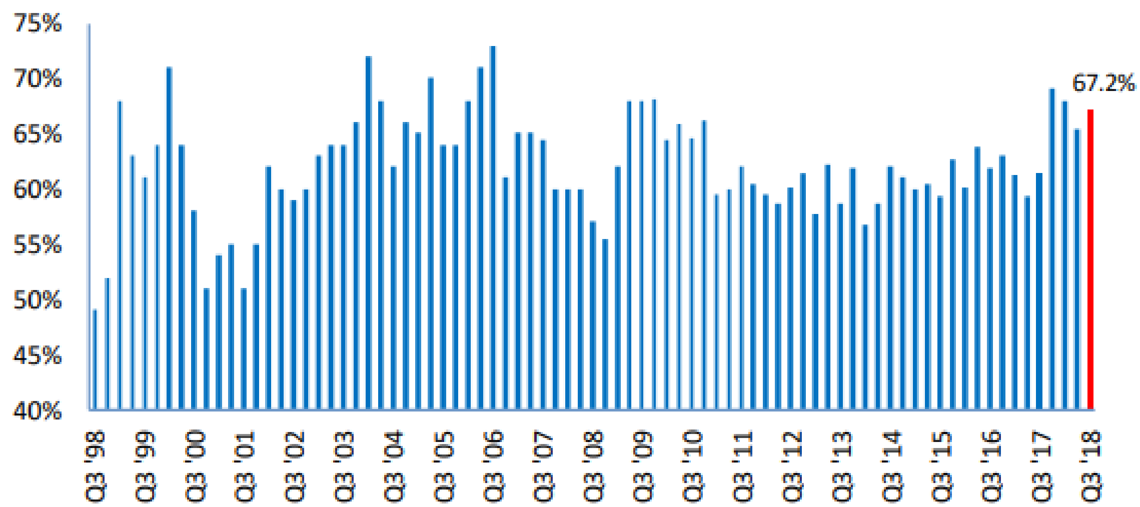


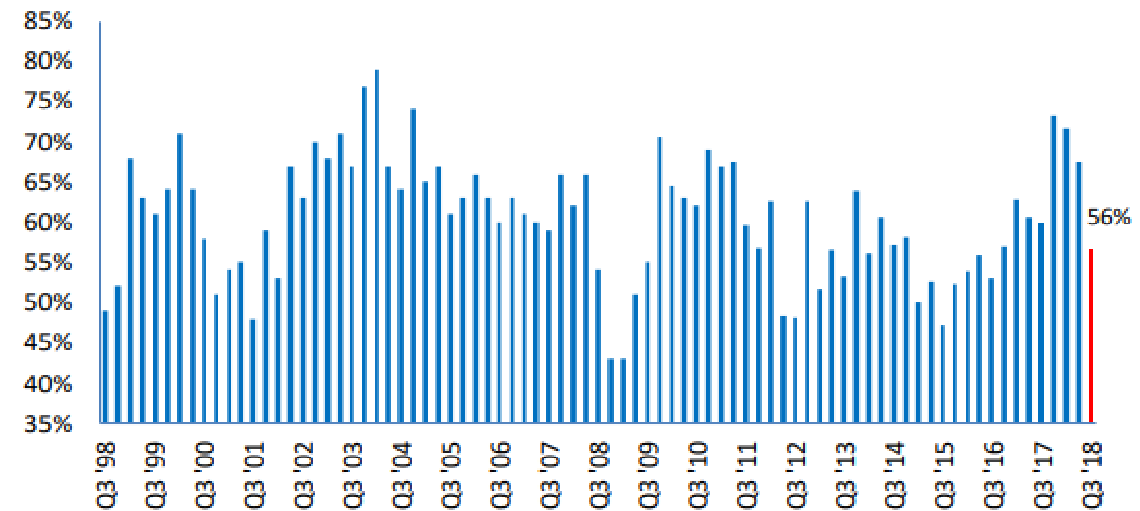


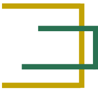
Equity Market Commentary

We are experiencing a corrective phase in the market. It is to be expected as we have not experienced any correction since February particularly in growth stocks. After having months of no volatility, we were paid back in spades in October. Seasonally, October has proven to be problematic in the past.

Of course, October is the third quarter reporting season. While earnings have been generally good, revenues have been lighter than expectations in some spots. When some of those are the over owned and over loved FAANG stocks there has been an outsized reaction all along the tech sector.







So what to expect now? These type of breakdowns are rare and unnerving. The thing is, we are in a growing economy (3.5% last quarter), have low unemployment (3.7% in September), high consumer confidence (137.9 October 30 report, an 18 year high), high corporate profitability (growing at a mid-teens rate), inflation is largely in check and tax laws & deregulation are still working in favor of the markets. Amid this background, should we have the worst October since 2008? Really?

This feels like a sharp but relatively normal 10% pullback and absent any new information to the contrary, should be an investable dip. This turndown in the market will likely take a few months to work through and we are unlikely to have a "V" bottom. The key to this correction is to stay focused on the fundamentals of the economy, markets and companies. We believe this correction has now created buying opportunities in companies with lower prices yet remaining strong in revenue and earnings growth.

As bad as October was, down 6.94%, the S&P is thanks to a month end two day rally still up 1.43% for the year. 2018 has been a year where growth greatly outstripped value. This disparity had to be narrowed at some point and it did in October.

Our bout of volatility probably will continue especially until the mid-term elections are past. This uncertainty is part of the markets' unease. Whether or not that particular event still causes unease after the election depends on the results and perhaps the reaction to them by voters.

We believe we could be in the topping process in the market. If so, it could last for another 2 years if the fundamentals of the economy and markets remain favorable. Stonebridge will remain focused on companies with quality revenue & earnings and rotate out of companies where fundamentals are weakening.

Fixed Income Market Commentary

The month of October brought us some rather dramatic spikes in interest rate levels. Yet by the time the dust settled and we closed out the month, we were mostly back to the levels we started at. Earlier, a weakening in bond prices drove yields up rather significantly, particularly for 10-year Treasury yields. Then, in the last half of the month as volatility spiked in equities, we saw a flight to safety in bonds that moderated the earlier run up in yields. 2-year Treasuries started the month at 2.82% and jumped as high as 2.92% before settling back at 2.87%. 10-years had a similar ride starting at 3.09% before peaking at 3.23% and then settling back down at 3.14% after dropping as low as 3.08% in the last week.

High-yield taxable bonds fell to two-year lows, mostly led by the correction in stocks, still yield spreads compared to benchmarks remain fairly tight historically. Tax-exempt bonds turned in flat to slightly negative performance for the month. iShares National Muni Bond ETF (MUB), which often serves as somewhat of a proxy for the wider municipal bond market, was down (0.36)% for the month. The shorter duration ICE BofA Merrill Lynch 1-5 year bond index was flat. Both new investment grade corporate and municipal bond issuance fell short of expectations for the month. That was likely helpful in buoying pricing or at least keeping yields from drifting even higher.

Sources
Data sourced through Bloomberg
Charts provided by Bespoke Investments

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