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MARKET *minute*

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Hartland is an independent institutional and wealth advisory firm that seeks to meet clients' investment objectives with appropriate risk and in a low-cost manner. Once this has been achieved, we seek superior returns compared to client-specific, market-based and peer group benchmarks. We believe broad diversification reduces portfolio volatility and enhances the opportunity for superior risk-adjusted returns.

The U.S. economy remains in a fairly positive state with the second reading on U.S. Q1 GDP growth of 2.2%[1]. U.S. economic growth slowed slightly more than initially thought amid downward revisions to inventory investment and consumer spending. The labor market continued to tighten with the headline unemployment rate declining to a new post crisis low of 3.8%[2]. The May jobs report beat expectations as the U.S. economy created 223,000 new jobs. Wage gains were also above expectations as the average hourly earnings rose 0.3% over the prior month and 2.7% year-over-year.

Geopolitical tensions in Europe resurfaced particularly in Italy amid concerns of the challenges a populist government presents. Trump also unexpectedly canceled the planned summit with North Korean leader Kim Jong Un. Albeit somewhat of a short-term trend, recent PMI readings suggest some divergence of growth between U.S. and global economic growth. U.S. Manufacturing PMI registered 56.4 in May with noted sharp increases in production and new business along with lengthening delivery times based on stretched supply chains signaling a pick-up in growth[3]. The IHS Markit's Eurozone Flash Manufacturing Purchasing Managers' Index (PMI) declined to 55.5[3]; though still at a solid level, the rate of expansion is weaker than earlier in the year amid signs of cooling demand and output.

U.S. EQUITY MARKETS

Index	1 Month	Year-to-Date	1 Year	3 Year
DJIA	1.4	-0.2	18.9	13.5
S&P 500	2.4	2.0	14.4	11.0
Russell 2000	6.1	6.9	20.8	11.0
Russell 1000 Growth	4.4	6.2	21.0	13.9
Russell 1000 Value	0.6	-1.9	8.2	7.4
FTSE NAREIT U.S.	3.5	-2.8	2.7	6.2
Bloomberg Commodity	1.4	3.6	11.0	-2.8

Earnings season is about wrapped up with 97% of the S&P 500 companies having reported as of month-end. The markets were not as captivated by macro events for most of May and were able to refocus on fundamentals and earnings which have been strong. The blended first quarter year-over-year earnings growth rate is 24.6% with strength across sectors[4]. 78% of companies surpassed analysts' earnings expectations, and if that figure holds, it would mark the highest percentage since the third quarter of 2008. In aggregate, earnings are 7.5% above the estimates with revenues 1.1% above estimates.

Despite the good earnings reports, the markets did not substantially reward those companies beating expectations, and those missing estimates were punished. The S&P 500 Index returned 2.4% for the month, while small caps as measured by the Russell 2000 Index advanced 6.1%, hitting a new all-time high. Small caps tend to have a greater percentage of their revenues generated domestically and may be better isolated from trade tensions.

The Technology sector was the clear leader during May, returning 7.4%, while Energy and Industrials were also strong and returned 3.0%. The Alerian Energy MLP Index after being battered during the first quarter have returned 13.6% quarter-to-date. On the other end of the spectrum were Consumer Staples, Telecom, Utilities and Financials. Given this sector performance, growth styles again trumped value with the return dispersion being particularly meaningful in large cap.

INTERNATIONAL EQUITY MARKETS

Index	1 Month	Year-to-Date	1 Year	3 Year
MSCI ACWI ex USA	-2.3	-1.9	9.7	4.7
MSCI EAFE	-2.2	-1.5	8.0	4.3
MSCI Emerging Markets	-3.5	-2.6	14.0	6.2
MSCI EAFE Small Cap	-0.9	0.9	15.1	10.7

International equity markets were mostly negative during May and currency movements also proved to be a headwind. The MSCI EAFE Index and MSCI Emerging Markets Index declined 2.2% and 3.5%, respectively. The combination of U.S. dollar strength and higher U.S. bond yields pressured emerging market assets.

The Bank of England opted to maintain their current interest rate policy and lowered its 2018 growth forecast. The BOE Governor expressed optimism that the recent slowdown would be transitory and the market is still expecting a rate hike by the end of the year[6].

FIXED INCOME MARKETS

Index	1 Month	Year-to-Date	1 Year	3 Year
BarCap US Aggregate	0.7	-1.5	-0.4	1.4
BarCap Global Aggregate	-0.8	-1.0	1.7	2.6
BarCap US High Yield	0.0	-0.2	2.3	4.9
JPM Emerging Market Bond +	-1.6	-5.1	-3.7	3.7
BarCap Muni	1.1	-0.3	1.1	2.8

Interest rates moved higher for most of the month but the geopolitical tensions in Europe late in the month led to a sharp decline in U.S. Treasury yields as a flight to safety trade ensued. The 10-year U.S. Treasury crossed the 3% psychological barrier again and hit 3.11%, its highest point since 2011, before declining to 2.86% at month-end[5]. The fairly flat treasury yield curve remains as evidenced by the narrow spread, 0.42%, between the 2-year and 10-year U.S. Treasury yield. There was a general downward parallel shift of the yield curve during the month, with the 10-year U.S. Treasury yield declining 9 basis points to 2.86%, the 30-year declining 9 basis points to 3.03%, and the 2-year U.S. Treasury yield decreasing 6 basis points.

The Bloomberg Barclay's Aggregate Index total return for May was 0.7% whereas the longer duration Bloomberg Barclay's Long Gov't/Credit Index returned 1.1%. Corporates underperformed relative to Treasuries for the month as spreads widened. High Yield was essentially flat in May and Bank Loans returned 0.2% for the month. The JPM Emerging Market Bond+ Index declined 1.6% in May.

Expectations are for two additional quarter point rate hikes by the Federal Reserve in 2018[5]. The building expectations of a 4th rate hike in December declined given the fixed income market jitters surrounding Italy and the EU.

Sources:
1 Bureau of Economic Analysis – U.S. Department of Commerce, 5/30/18
2 Bureau of Labor Statistics – U.S. Department of Labor, 6/1/18
3 IHS Markit, 6/1/18
4 Factset Insight, 5/25/18
5 Bloomberg

Definitions:
Markit U.S. Manufacturing Purchasing Managers' Index: The U.S. PMI is based on original survey data collected from a representative panel of around 600 manufacturing firms.
Markit Eurozone Manufacturing Purchasing Managers' Index: The Eurozone PMI is based on original survey data collected from a representative panel of around 3,000 manufacturing firms.

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