Capital Market Review

Third Quarter 2018

By Jack Peluso, Allegheny Research Team

Building on a solid second quarter, the broad market [as represented by the S&P 500 Index] continued its upward trend with three more months in the black. The looming threat of an all-out trade war might have spooked investors slightly during the first three months of the year. However, just like last quarter, market fundamentals remain too strong to ignore and continue to drive an increasingly positive view of the economy. Second quarter earnings figures were strong, with 80% of the companies in the S&P reporting EPS above estimates, according to FactSet [the highest percentage since they began tracking this data in 2008]. Q2 also marked the second quarter in a row with year-over-year earnings growth of 25%. So far in Q3, companies in the index aren't showing signs of slowing. As of October 17th, with just over 10% of the S&P 500 reporting earnings for the third quarter, 88.2% have beaten EPS expectations, with 66.7% beating revenue estimates. Obviously, this alone is too small of a sample size to draw any meaningful conclusions, but some analysts are already predicting a third consecutive quarter with 20%+ year-over-year earnings growth.

The S&P index gained 3.7% during the month of July, 3.3% during August, and 0.6% during September, leading to a cumulative gain of 7.7% for the third quarter. As of 9/30/2018, the six-, nine-, and twelve-month returns for the index were all positive, coming in at 11.4%, 10.6%, and 17.9% respectively. As the broad market continues its upward climb, we believe it's prudent to remember that this extended bull market environment is not typical. Remember, over the past two years, we've witnessed multiple market anomalies; the S&P 500 was positive every single month during 2017, marking the first time in history that this has ever occurred. Furthermore, this January's gain tied the index's longest streak of positive monthly returns [15 consecutive months]. To reiterate once more just how rare these types of occurrences really are, the S&P managed 11/12 positive months back in 2006 [which was over 11 years ago], and the index saw 15 positive months in a row during 1958-1959 [which was nearly 60 years ago!].

Following a second quarter in the red, the bond market [as represented by the Bloomberg Barclays Aggregate Bond Index] managed to improve slightly during the third quarter of 2018, producing a three-month gain of 0.2%. After first- and second-quarter hikes to the Fed Funds Rate, new Fed Chair Jerome Powell led the decision to raise rates once again during the September 26, 2018 meeting. The September hike marked the fourth increase in just under twelve months, and the eighth increase since December 2015 [when we hit the lowest possible rate, 0.25%, or effectively zero]. As implied multiple times over the past few quarters, these consistent increases to the Fed Funds rate are likely part of the reason bond market returns have remained in flat/negative territory. During the six-, nine-, and twelve-month time periods ending 9/30/2018, the bond index saw losses of -0.1%, -1.6%, and -1.2% respectively.

Inflation [as expressed by the Consumer Price Index] has been positive each month this year, which continues to serve as yet another factor adding to the positivity of the current economic outlook. With the twelve-month CPI return remaining slightly above the Fed's inflation target of 2.0%, and PCE (Personal Consumption Expenditures, which is another key measure of inflation) finally picking up as well, we believe at least one more rate hike is likely during the final quarter of 2018. President Trump continues to be vocal regarding his opinions on Fed policy, calling for restraint on behalf of Fed Chair Powell. Despite the epic failures we've witnessed in the past regarding presidential influence of the Fed, Trump persists, recently being quoted saying that the Fed has "gone crazy," and that his single greatest threat to a second term in office is Chairman Powell's aggressive policy. Trump believes the ultimate arbiter of his success is the stock market and doesn't think it can sustain its momentum given the Fed's current course. However, these ongoing outcries from Trump create an obvious issue, as the Fed is now pressured to show that they remain independent. That being said, we believe that the Fed's approach has been measured and responsible. Given how low rates remain, and the depth of the current bull market, continued hikes seem only prudent as lowering rates is one of only a few levers that the Fed can pull to assist in a recession. It makes sense for them

to continue raising rates [while there is still time to do so] in order to create a buffer for the next recession. For the one-, three-, six-, and nine-month periods ending 9/30/2018, the index saw increasingly positive returns of 0.1%, 0.2%, 1.2%, and 2.4% respectively.

The Stock Market

We saw mixed results across the stock market, as two [out of seven] of the major market averages produced negative results during the third quarter. The Russell 2000, an index of small-company stocks, landed near the middle of the pack with a 3.6% gain during the quarter. The S&P 500, an index of large company stocks, was up 7.7% for the three-month period, while the Dow Jones Industrial Average led the pack, gaining 9.6% during the quarter. The Dow Jones US Select REIT, an index representing real estate companies, dropped off dramatically from last quarter's +10% gain, finishing the quarter with a meager three-month increase of 0.7%. The MSCI EAFE, an index representing international stocks from developed markets, gained 1.4%, while the Bloomberg Commodity Index [playing the laggard] fell by -2.0%. Lastly, the MSCI Emerging Markets, an index representing the international stock of emerging countries, improved from last quarter but remained in the red, coming in with a three-month drop of -1.1% for the period ending 9/30/2018.

Both six- and nine-month returns ending 9/30/2018 came back mixed, with two [of seven] indices producing negative results during the six-month period, and three [of seven] during the nine months. As we saw last quarter, the Russell 2000 Index took over the lead during both the six- and nine-month periods, gaining 11.6% and 11.5% respectively. The S&P 500 followed closely, increasing 11.4% and 10.6%, while the DJ Industrial Average came next, gaining 11.0% and 8.8%. Aided by a strong second quarter [but hurt by a weak first quarter], the DJ REIT Index returned a solid 10.8% during the six-month period but increased by only 2.6% during the nine months. The MSCI EAFE continued trending downward, finishing the third quarter with a six-month gain of 0.1% and a nine-month loss of -1.4%. The Commodity Index remained in negative territory during the six- and nine-month periods, falling by -1.6% and -2.0% respectively. Meanwhile, the MSCI EM Index fell to the laggard position, producing six- and nine-month losses of -9.0% and -7.7% respectively.

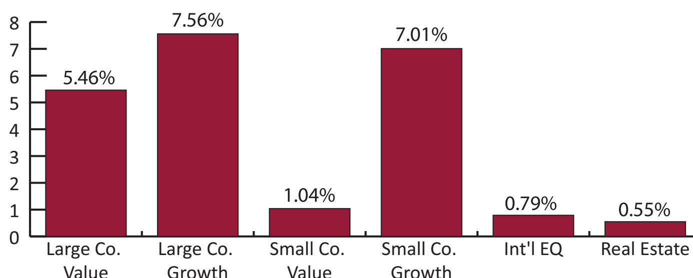
Just like the other time periods, results came back mixed for the trailing twelve months ending 9/30/2018. The Russell 2000 Index lost the lead, but remained in the top three, with a double-digit annual increase of 15.2%. The S&P 500 finished the twelve months just ahead of the Russell by gaining 17.9%, while the Dow Industrial Average retook the lead, producing an annual increase of 20.8%. Once again, the DJ REIT Index landed near the middle of the pack, gaining 4.6% over the trailing twelve-month period ending 9/30/2018. Meanwhile, the MSCI EAFE Index posted a 2.7% gain, the Bloomberg Commodity rose by 2.6%, and our laggard, the MSCI EM Index, was down -0.8%.

Market Returns

	3 months ending 9/30/2018	12 months ending 9/30/2018
S&P 500	7.7%	17.9%
Dow Jones Industrial Avg	9.6%	20.8%
Russell 2000	3.6%	15.2%
MSCI EAFE	1.4%	2.7%
MSCI Emerging Markets	-1.1%	-0.8%
DJ US Select REIT	0.7%	4.6%
Bloomberg Commodity Index	-2.0%	2.6%

Comparison of Equity Styles

3 months ended 9/30/2018



The value/growth trend we've witnessed over the past several quarters continued, with value companies trailing growth companies across all four periods ending 9/30/2018 [the trailing three-, six-, nine- and twelve-month periods]. As we discussed last quarter, some of our managers are attributing this extended trend to what they call the "momentum effect"; essentially, they maintain the view that the ongoing upswing in stock prices has evolved into a momentum rally that is significantly disconnected from underlying equity fundamentals. We tend to agree with this point of view, and though predicting inflection points is nearly impossible, as firm believers in reversion to the mean, we encourage all of our advisors to continue thinking long-term and remember, "Trees don't grow to the sky."

During the three-month period ending 9/30/2018, Large Value gained 5.5%, trailing Large Growth at 7.6%. Small Value increased by 1.0%, trailing Small Growth at 7.0%. The average Real Estate manager played the laggard during the

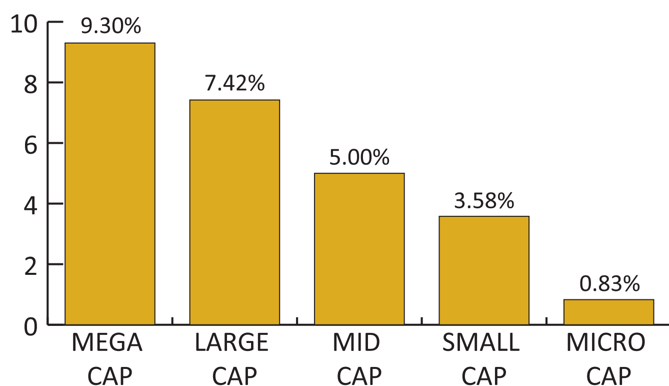
three-month period with a gain of 0.6%, trailing the average International Equity manager's gain of 0.8%.

Six-and nine-month returns followed a nearly identical pattern, though Real Estate and International Equities [now the laggard] swapped places. Large Value stocks continued to underperform Large Growth – gaining 7.2% [vs. 13.1%] for the six months and increasing 4.5% [vs. 15.6%] for the nine months. Similarly, Small Value stocks continued to underperform Small Growth – gaining 7.7% [vs. 16.1%] during the trailing six-month period and 4.7% [vs. 18.8%] during the trailing nine-month period. Aided by a robust second quarter [after being hurt by a weak first quarter], the average Real Estate manager finished the 9/30/2018 period with a decent six-month gain [8.6%] but landed near the bottom of the pack with a much weaker nine-month increase [1.2%]. International Equities took-over the laggard position for the six- and nine-month periods ending 9/30/2018, falling into the red with returns of -1.4% and -2.2% respectively.

The twelve-month returns followed the same pattern as the six- and nine-month figures. Large Value produced an annual gain of 10.7%, while Large Growth increased by 23.1%. Small Value produced a yearly gain of 8.4%, while Small Growth increased by 24.3%. The average Real Estate manager gained 3.3% during the trailing twelve-month period, while the average International Equity manager clawed back into positive territory with an annual gain of 1.7%.

Return by Market Cap

3 months ended 9/30/2018



During the first quarter of the year we finally noticed a bit more volatility; however, with second-quarter earnings figures coming back stronger than expected, this trend did not continue. Looking at U.S. stocks by market cap, third-quarter results came back positive across the all four periods [the trailing three-, six-, nine- and twelve-month periods ending 9/30/2018]. Notably, the small/large trend we've witnessed frequently over the past several quarters has once again reverted, with Large-cap stocks outperforming Small-caps almost across the board. Also, worth noting, the Mid-cap segment continues to underperform both Small/Large, regardless of the trend mentioned above.

Only one [out of five] segments outpaced the broad market return of 7.7% during the third quarter. Mega-cap stocks led the pack, finishing the three-month period with a gain of 9.3%, while Large-caps followed with a three-month gain of 7.4% [coming in just behind the broad market]. Mid-cap and Small-cap stocks also underperformed the broad market, finishing September with quarterly returns of 5.0% and 3.6% respectively. Meanwhile, up only 0.8% during the trailing three months, Micro-cap stocks underperformed the broad market as well, finishing the third-quarter as the laggard.

Two [out of five] market segments outpaced the broad market's six-month return of 11.4% for the period ending 9/30/2018. Maintaining the top position, Mega-cap stocks finished the trailing six-month period with a gain of 13.9%, while Small-cap stocks leapfrogged the Mid- and Large-Cap segments with an increase of 11.6% [edging out the broad market as well]. The Large-cap segment came in just below the broad market, gaining 11.3%. Micro-Caps followed closely, increasing 10.9%, while Mid-caps finished the third quarter as the laggard with a gain of 7.5%.

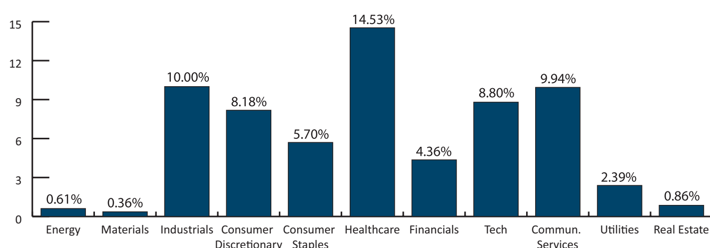
Nine-month returns came in very similar to [or in most cases, slightly lower than] six-month figures, which can be attributed to the volatility we observed during the first quarter. Overall, three [out of five] market segments managed to outperform the broad market's return of 10.6% for the nine-month period ending 9/30/2018. Once again landing in the top-spot, Mega-cap stocks produced a decent 11.7% gain for the trailing nine months, while Small- and Micro-cap stocks followed closely behind, finishing the third quarter with nine-month gains of 11.6% and 11.5% respectively. Just barely underperforming the broad market's return, the Large-cap segment gained 10.5%, while Mid-Caps remained the laggard with a nine-month increase of 7.5%.

As has recently been the case, for the trailing twelve-month period, all market segments finished with double-digit annual returns; though this time, only one [out of five] market segments managed to outperform the broad market's annual return of 17.9%. Mega-cap stocks [as represented by the Russell Top 50 Mega Cap Index] finished the quarter above the broad market, producing an annual gain of 19.9%. Large-cap stocks [as represented by the large-cap Russell 1000 Index] came in just behind the broad market, producing an annual increase of 17.8%. Mid-cap stocks [as represented by the Russell Mid Cap Index] finished

the quarter with a substantial twelve-month gain of 14.0%, while Small-cap stocks [as represented by the small-cap Russell 2000 Index] outperformed the Mid-Cap segment by producing an annual increase of 15.2%. Meanwhile, Micro-cap stocks [as represented by the Russell Micro Cap Index] rounded out the group, ending the third quarter with an annual gain of 13.7%.

Stocks by Sector

3 months ended 9/30/2018



As of 9/30/2018, the GICs sector methodology was updated, and the old "Telecom" sector has officially been replaced by the new "Communication Services" sector. Stocks from the Technology and Consumer Discretionary sectors have been repositioned, resulting in nearly $3 trillion in market capitalization movement. We recently posted an exhibit detailing this change. To summarize, according to GICs, the changes to the sector name and broadening of the sector are a result of changes in how communication occurs. While Telecom was [previously] a traditional defensive higher-yielding sector, these changes will lead to higher beta names [such as Alphabet and Facebook] becoming the largest weights in the sector.

With Real Estate separated from the Financials sector last year, the S&P 500 Index now has eleven individual sectors. These sectors, along with their respective quarter-end weightings in the index [as of 9/30/2018], are as follows: Energy 6.0%, Materials 2.4%, Industrials 9.7%, Consumer Discretionary 10.3%, Consumer Staples 6.7%, Healthcare 15.0%, Financial Services 13.3%, Technology 21.0%, Communication Services 10.0%, Utilities 2.8%, and Real Estate 2.7%.

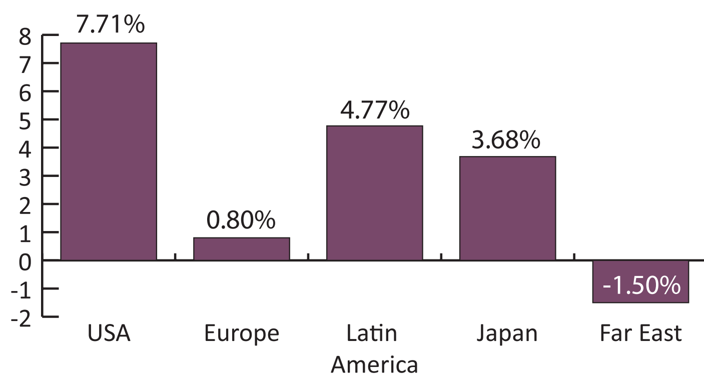
Though a handful were nearly flat, all eleven sectors finished the three months ending September 30, 2018, in positive territory; this figure has dramatically improved each quarter this year, as only two [out of eleven] managed positive results during the first three months of the year, and seven [out of eleven] managed positive results during the second three months. Energy was up 0.6% during the third quarter and fell near the bottom of the pack [despite leading the group last quarter], while Materials, playing the part of the laggard, increased by 0.4%. Industrials were up 10.0% and landed near the top of the pack [despite being in the red last quarter], while Consumer Discretionary increased by 8.2% [which was identical to the sector's second-quarter return]. Consumer Staples finished the third quarter with a three-month gain of 5.7%, while Healthcare led the group with a three-month gain of 14.5%. Meanwhile, Financial Services increased 4.4%, Technology gained 8.8%, and Communication Services rose 9.9%. Lastly, Utilities and Real Estate both increased over the trailing three-month period ending 9/30/2018, coming in with gains of 2.4% and 0.9% respectively.

Six-month results came in strong, as once again, all eleven sectors produced positive results. However, looking at the nine-month results, we can still see the effects of some first-quarter volatility, as two [out of eleven] sectors came back with negative returns. Furthermore, as compared to the six-month period, nine-month returns are lower across the board [except for Consumer Discretionary and Technology]. Energy increased by 14.8% during the six-month period, but only gained 7.5% during the nine months given the impact of the first quarter. Materials increased by 2.9% during the six-month period and were also impacted negatively by the first quarter, as the nine-month result was a decrease of -2.7%. Industrials followed a similar pattern, gaining 6.5% during the six-month period, and slightly less [4.8%] during the trailing nine. Unaffected by the first quarter shake-up, Consumer Discretionary tallied a significant gain [17.0%] during the six-month period and an even more substantial return [20.6%] for the nine-month period. On the flip-side, Consumer Staples was another sector impacted by the first quarter, as the sector increased by 4.1% during the six-month period, but then fell by -3.3% over the trailing nine months [landing in last place over that period]. The Healthcare sector came in with a six-month gain of 18.1%, leading all other sectors, but fell to third-place with a nine-month increase of 16.6%. Financial Services rose 1.1% during the six-month period but was barely flat [0.1%] over the trailing nine months. One other area that was seemingly unaffected by the first quarter's bout of volatility, Technology, which rose by 16.5% during the six months [third-place], and 20.6% over the trailing nine [tied for first]. The Communication Services sector returned to the more familiar pattern, gaining 8.9% during the trailing six-month but only 0.8% during the nine-month period. The Utilities and Real Estate sectors joined most of the sectors, finishing the quarter with six-month returns outpacing the nine-month numbers. Utilities managed a six-month gain of 6.2%, while Real Estate increased by 7.0%. Nine-month results came in lower, with those sectors gaining 2.7% and 1.7% respectively.

Looking at the trailing twelve-month period ending September 30, 2018, [as we factor in the final quarter of 2017] results look strong across the board. Once again, all eleven sectors produced positive results for the period, making the nine-month period the outlier. The Energy sector finished the third quarter with a substantial annual gain of 13.9%, the Materials sector rose by 4.0%, and the Industrials sector increased by a respectable 11.2%. Leading the group again, the Consumer Discretionary sector put up an annual gain of 32.5%, while Consumer Staples remained at the bottom with an annual increase of 2.9%. The Healthcare sector remained near the top of the pack, rising by 18.4% during the trailing twelve-month period, while the Financial Services sector produced an annual return of 8.7%. The Technology sector fell to second-place, finishing the second quarter with a hefty twelve-month gain of 31.5%, while Communication Services rebounded with a twelve-month increase of 4.4%. The Utilities and Real Estate sectors were both up for the twelve-month period ending 9/30/2018, coming in with gains of 2.9% and 5.0% respectively.

Stocks by Region

3 months ended 9/30/2018



Looking at average stock market returns across five main regions [USA, Latin America, Europe, Japan, and the Far East], only the U.S. and Japan were able to produce positive results during all four time periods [the trailing three-month, six-month, nine-month, and twelve-month periods ending September 30, 2018]. During the three-month period ending 9/30/2018, we can see almost unified growth, as four [out of five] regions were up. However, looking beyond the most recent quarter, results came in mixed across the board.

The United States [as represented by the S&P 500 Index] not only produced entirely positive results but led all other regions during each period ending 9/30/2018, gaining 7.7%, 11.4%, 10.6%, and 17.9% over the trailing three, six, nine and twelve months.

Latin America [as represented by the MSCI EM Latin America Index] had a decent third quarter, nearly leading the pack with a three-month gain of 4.8%. However, if we extend our scope beyond the most recent three-month period, the region trailed all others [significantly], producing six-, nine-, and twelve-month losses of -13.8%, -6.9%, and -9.1%. Meanwhile, Europe [as represented by the MSCI Europe Index] followed a somewhat similar pattern, producing returns of 0.8%, -0.5%, -2.5%, and -0.3% over the three-, six-, nine-, and twelve-month periods. However, despite being mainly negative, Europe did not play the laggard during any of the four time periods.

The Japanese region [as represented by the MSCI Japan Index] finished the quarter with gains of 3.7%, 0.7%, 1.6%, and 10.2% over the trailing three, six, nine, and twelve months – making Japan the only other region [besides the United States] to produce positive returns across all four time periods ending 9/30/2018.

The Far East [as represented by the MSCI AC Far East Ex-Japan Index] finished the quarter with three, six-, and nine-month losses of -1.5%, -7.3%, and -5.9%, but managed a gain of 1.5% over the trailing twelve months. Like Europe, the region produced negative results in three [out of four] time periods yet did not play the laggard in any one period.

Please note, all data is quoted in U.S. Dollar terms, any change in currencies may, therefore, influence actual returns.

Bonds Market

Rates increased fairly evenly across the yield curve rising [20-30 basis points] from their 6/30/2018 positions, though just like last quarter, shorter-term rates rose slightly more than longer-term rates – with the 2-year increasing 29 basis points quarter-over-quarter, while the 10-year rose by only 20. Staying true to the course he has projected, Chairman Powell has led the Fed to raise rates each quarter so far this year, with the September rate-hike marking the fourth increase in just under a year's time [and the eighth increase since December 2015, when we hit the lowest possible rate, 0.25%, or effectively zero]. As we've discussed in prior quarters, during a non-inflationary environment in which there have been multiple increases to the Fed funds rate, one would generally expect longer-term rates to begin to dip. However, now that inflation has seemingly picked-up, the fact that longer-term rates are exclusively higher than they were a year ago makes much more sense than it did just a few quarters ago.

Remember, the main reason for the Fed's cautious approach to raising rates over the past few years has been due to the [essentially unexplained] lack of inflation. The Fed's

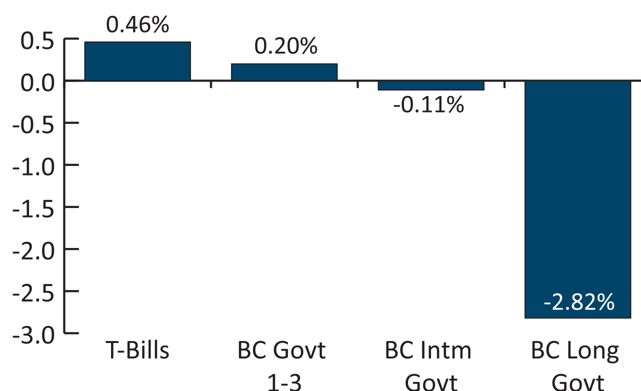
framework for forecasting inflation applies a version of the Phillip's Curve, which posits an inverse relationship between unemployment and inflation. This means that when the unemployment rate falls, wages will go up, thereby leading to higher prices, which leads to higher inflation. Over the past few years, there seemed to be a breakdown in this relationship. While we've seen lower and lower unemployment in the United States, it has taken much longer than expected for this to lead to higher inflation. There are several theories regarding the reasoning behind this breakdown, such as anti-inflationary trends, or a simple lag in the Phillip's curve [the latter seems to be the more likely explanation, especially now that we've seen inflation pick up in the U.S.].

Inflation [as represented by the Consumer Price Index], has consistently hit the 2% target three quarters in a row, and strong underlying fundamentals continue to persist in the United States. With these considerations, one would generally expect the Fed to start acting a bit less cautiously [as they have over the past year or so], especially when we consider the length of the current bull market – after all, lowering rates is one of the only levers the Fed can pull to aide in the event of a recession. With that being said, isn't it only logical for them to raise rates [while they still can] to prepare a buffer for the next [inevitable] downturn? Many experts would say yes; however, some critics of the Fed [including our president, as well as some liberal Democrats, like Elizabeth Warren and Bernie Sanders], believe continued tightening is not necessary at this point in time. The main concern of these critics (particularly President Trump) appears to be the implication that continued rate hikes have the potential to drive the dollar higher, ultimately driving the trade deficit higher, which appears to be a focal point for the current administration. Contrary to the view of these critics, we think that the Fed's measured [data-dependent] approach has been nothing but responsible and ultimately expect them to maintain their current course. We believe the Fed will continue to raise rates gradually, likely once more this year and up to four more times next year, regardless of outspoken critics. Currently, the chances of a fourth rate-hike before the end of the year seems likely, though it may not come until December. The CME group is presently predicting the probability of a fourth hike in November to be about 5.9%, and a fourth hike in December to be almost 70%.

Treasury	*9/30 2018*	*6/30 2018*	*3/31 2018*	*12/31 2017*	*9/30 2017*
2 Year	2.81%	2.52%	2.27%	1.89%	1.47%
5 Year	2.94%	2.73%	2.56%	2.20%	1.92%
10 Year	3.05%	2.85%	2.74%	2.40%	2.33%
30 Year	3.19%	2.98%	2.97%	2.74%	2.86%

Bonds by Maturity

3 months ended 9/30/2018



As interest rates continued to rise across the board, the various maturity sectors of the government bond market saw flat-to-negative results predominately during all four time periods [trailing three, six, nine, and twelve months ending 9/30/2018] with the longer-maturity sectors hit harder than shorter-maturity sectors. Considering multiple rate-hikes in the recent past, along with the fact that long-maturity government bonds are generally the most sensitive to changes in interest rates, we would typically expect them to be hit the hardest. On the flip-side, U.S. Treasury Bills [unsurprisingly] managed to maintain positive [albeit modest] results during each period.

Three- and six-month returns for the period ending 9/30/2018 looked similar, with shorter-maturity sectors producing positive results and longer-maturity sectors landing in the red. The U.S. T-Bill Index led the group, finishing the quarter with a three- and six-month gains of 0.5% and 0.9%, while the Bloomberg Barclays 1-3 Year Government Index increased by 0.2% and 0.4% [outpacing the Aggregate Bond Index during both periods]. Looking at intermediate-to-long maturity government bonds, the Bloomberg Barclays Intermediate Government Index finished the third quarter with three- and six-month losses of -0.1%. Meanwhile, the Bloomberg Barclays Long Government Index was the clear laggard, ending the quarter with three- and six-month drops of -2.8% and -2.6%.

Nine- and twelve-month returns [as of 9/30/2018] followed a very similar pattern, with U.S. Treasury Bills leading the group during both periods, increasing by 1.2% and 1.5%. Short Government finished the quarter with a nine-month gain of 0.3% and was flat for the trailing twelve months, producing an annual return of zero. Meanwhile, the Intermediate and Long Government [which, as we mentioned, are generally more sensitive to interest rate shifts] finished the nine- and twelve-month periods in the red once again. Intermediate Government fell -0.8% over the

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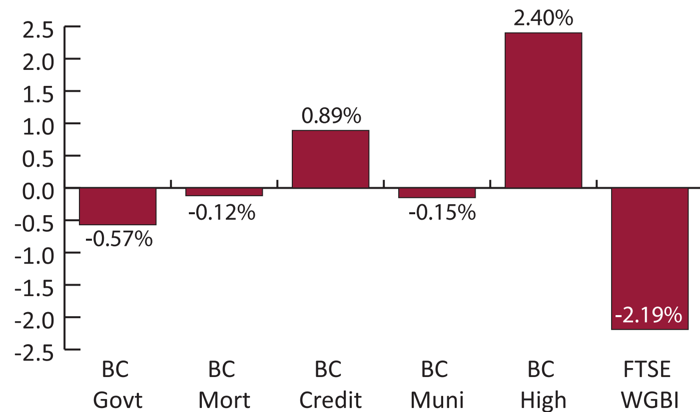
nine months and -1.2% over the trailing twelve, while Long Government maintained the last-place position, falling by -5.7% during the nine-month period and -3.5% during the trailing twelve.

Bonds by Sector

3 months ended 9/30/2018



Looking across all six major sectors of the bond market as of September 30th, 2018, we can see once again that the first three months of the year proved to be much tougher than the following six, at least for most of the bond market. In the nine-month period, five [out of six] sectors produced negative returns, while four [out of six] were down over the three- and twelve-month periods and only two [out of six] were down during the trailing six-month period ending 9/30/2018. U.S. High Yield was the only sector to remain positive across all four time periods.

Though not as bad as the nine-month period, the trailing three months ending 9/30/2018 were certainly not pretty. Four [out of six] sectors underperformed the Aggregate Bond Index, which was flat! The High Yield sector led the pack with a three-month gain of 2.4%, while U.S. Credit was the only other sector to produce positive results, finishing the quarter with a three-month increase of 0.9%. Finishing just behind the Aggregate Index, the U.S. MBS [Mortgage-Backed Securities] and Municipal Debt sectors produced three-month losses of -0.1% and -0.2%, respectively. Landing at the bottom of the group, the U.S. Government Debt sector and the WGBI [World Government Bond Index] also experienced three-month declines, finishing the quarter down -0.6% and -2.2%, respectively.

As of 9/30/2018, the six-month period showed the most promising results, as this time four [out of six] sectors finished with positive returns. As compared to the three-month period, only the WGBI looked worse during the trailing six months. High Yield [as represented by the Bloomberg Barclays Corporate High Yield Index] rose by 3.5% over the six months, leading the group once again, while U.S. Credit [as represented by the Bloomberg Barclays US Credit Index] remained mostly flat. The MBS [as represented by the Bloomberg Barclays U.S. Mortgage-Backed Securities Index] and Municipal [as represented by the Bloomberg Barclays Municipal Index] sectors both increased during the trailing six months, posting gains of 0.1% and 0.7%, respectively. Lastly, landing at the bottom yet again, the U.S. Government [as represented by the Bloomberg Barclays U.S. Government Index] and WGBI [as represented by the non-USD FTSE WGBI] sectors finished the quarter with losses of -0.5% and -7.2%, respectively.

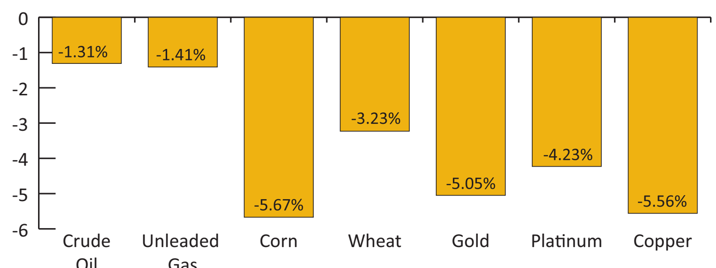
Clearly impacted by the first three months of the year, we can see a drastic difference between the six- and nine-month results, as five [out of six] sectors finished the quarter in the red. Only High Yield produced a return, leading the group yet again with a nine-month gain of 2.6%, while the U.S. Credit sector dropped -2.1%. The MBS sector experienced a nine-month decrease of -1.1%, while the Municipal sector fell by -0.4%. Meanwhile, the U.S. Government and WGBI sectors both fell during the trailing nine-month period, producing losses of -1.6% and -3.1% respectively.

Just like the three-month period, four [out of six] bond sectors came in with negative results during the trailing twelve months ending 9/30/2018. Unsurprisingly, the U.S. High Yield sector led all others, finishing the quarter with an annual gain of 3.1%. The U.S. Credit and U.S. Mortgage-Backed sectors [still impacted by a rough first quarter] finished up September with annual losses of -1.1% and -0.9%, respectively. The Municipal sector, up 0.4% for the year, was the only other sector [aside from High Yield] that managed to produce an annual gain. Meanwhile, the U.S. Government and World Government tied for last-place, as both sectors closed out the quarter with annualized losses of -1.6%.

Please note, the Citi indices were purchased by FTSE, and the Citi WGBI Non-USD was officially renamed the FTSE WGBI Non-USD.

COMMODITIES MARKET

3 months ended 9/30/2018



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Looking at the Bloomberg Commodity Index, we can observe that the second-quarter bump was short-lived, as the index finished September with a three-month loss of -2.0%. When we factor in the second-quarter increase [0.4%], the index return was slightly better [but still negative], coming in at -1.6% over the trailing six-month period. Considering the first-quarter decrease [-0.4%], nine-month results appear identical to the three-month period with the index down -2.0%. The Commodity Index managed a much stronger result for the twelve-month period ending 9/30/2018, finishing the quarter with an annual gain of 2.6%.

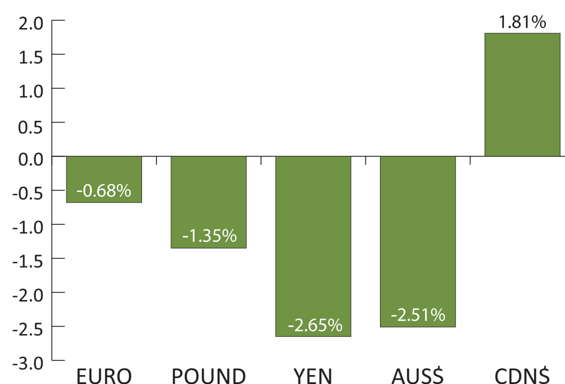
There is no shortage of volatility within the energy commodities, as Crude Oil and Unleaded Gas prices reversed course yet again, this time falling in tandem, with three-month losses of -1.3% and -1.4%, respectively. Last quarter, Oil and Gas were the only two commodities to produce positive three-month results, as all other commodities came in negative. This quarter, all tracked commodities fell in unison. Corn decreased by -5.7% [playing the laggard of the group], while Wheat fell by -3.2%. Gold dropped by -5.5%, and Platinum decreased by -4.3%, while Copper posted a loss of -5.6%.

For the six- and nine-month periods ending as of September 30th, 2018, we witnessed a very similar pattern. Crude Oil and Unleaded Gasoline not only led the other commodities across both time periods but were also the only to remain in positive territory, finishing the quarter with six-month gains of 12.8% and 11.7%, respectively, and nine-month gains of 21.0% and 16.8%, respectively. Corn decreased -12.8% over the six-month period and -4.8% over the trailing nine, while Wheat fell by -9.4% during both [the six- and nine-month] periods. Gold decreased by -10.3% during the six months and -8.0% over the trailing nine-month period. Platinum dropped by -12.9% during the six months [landing in the last place for the period] and -11.9% over the trailing nine-month period. Meanwhile, Copper decreased by -7.7% over the course of six months and -15.0% over the trailing twelve [landing in the last place for the period].

Looking at the twelve-month period ending 9/30/2018, we can observe the same pattern as six- and nine-month periods, with energy prices rising in tandem and all other commodities falling. Leading the pack again, Crude Oil finished September with an impressive annual return of 41.6%, while Unleaded Gasoline prices increased by a modest 9.2%. All food prices came back negative with corn prices falling -3.0%, while Wheat prices dropped -5.9%. Metals prices came in negative as well, with Gold producing an annual loss of -7.5%, Platinum finishing [in the last place] with a -11.4% loss over the twelve-month period, and Copper dropping by -5.2% during the trailing twelve months.

CURRENCY MARKET

3 months ended 9/30/2018



As we noted last quarter, during 2016 and most of 2017, foreign currencies were [generally] appreciating versus the U.S. Dollar. However, this trend began slowing down in 2017, with the rate of appreciation for most currencies dropping off dramatically to start 2018. Looking back at the June-end figures, it would seem apparent that not only did this trend slow to a halt, but it actually reversed course. This reversal can likely be attributed to a handful of factors: recent U.S. Foreign Policy [tariff war, the threat of a trade war, etc.]; the U.S. Federal Reserve [continued rate hikes]; and generally strong fundamentals in the U.S. [as compared to the rest of the world]. Because all of these factors are still relevant, it should come as no surprise that, as of 9/30/2018, most foreign currencies continue to depreciate versus the U.S. Dollar [aside from the Canadian Dollar]. Overall results look the same as last quarter, with four [out of five] currencies producing negative results. However, unlike last quarter, the Japanese Yen was hit while the Canadian Dollar was not. Excluding the outlier's [Canadian Dollar] three-month return, returns were negative across all four time periods [the trailing three, six, nine, and twelve months ending 9/30/2018] for all five currencies.

Though exclusively negative, the Euro managed to stay near the middle of the pack during all four time periods, finishing September with three-, six-, nine-, and twelve-month losses of -0.7%, -5.8%, -3.1% and -1.8%. The British Pound followed a very similar pattern [as usual], but was hit a bit harder than the Euro, with the British currency falling -1.4% during the three months, -7.0% during the six months [landing in the last place for the period], -3.4% during the nine months, and -2.8% during the trailing twelve-month period.

The Australian Dollar [which is strongly influenced by commodity prices along with the Chinese economy], saw its currency fall by -2.5% during the third quarter and -6.0% during the trailing six months. Factoring in the hits this currency

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took during the first quarter of this year and final quarter of last year, nine-and twelve-month results land in the laggard territory, as the currency fell by -7.5% and -7.8%. The Canadian Dollar experienced a strong third quarter, managing to produce the only positive results [for any of the five currencies, in any of the four time periods], with a three-month gain of 1.8%. Results quickly shift as we extend our scope beyond the last three months. The Canadian currency finished the quarter flat over the six-month period and then went on to tally nine- and twelve-month losses of -2.7% and -3.3%.

The Japanese Yen [like most of the other currencies] was stricken last quarter, but thanks to a decent first quarter this year [and a strong fourth quarter last year], the currency only saw negative results for the three-month period. The Yen was hit hard again this quarter and this time [despite the previous spikes], the Japanese currency depreciated versus the U.S. Dollar during all four time periods ending 9/30/2018 [the trailing three, six, nine, and twelve months]. The Yen fell by -2.7% over the three months [landing in the last place for the period], dropped -6.5% over the six-month period, was down -0.9% over the nine-month period, and dropped by -1.1% during the trailing twelve months.

The information included herein was obtained from sources which we believe reliable.

Past performance is not a guarantee of future results. Any mention of specific investments is not intended to be an offer of sale. Please refer to a fund's prospectus for investment objective, risks, charges, and expenses before investing. For more information, contact your Allegheny Advisor.

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