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“In like a lamb out like a lion.” Most of us instantly recognize this as part of a maxim regarding the trend of the weather in the month of March. However, you could be forgiven for thinking it was related to the domestic equity market in 2018.

The historic tranquility of the 2017 market carried over into the early days of 2018. The calm was short-lived, however, as the S&P 500 (SPX) declined around 9% between January 26th and February 8th, and did not regain its January high until late August. The S&P 500 peaked again in late September, before beginning a new slide in October, which was attributed to trade tensions and concerns that the Fed’s telegraphed pace of interest rate increases was too rapid and could precipitate a recession. These fears continued largely unassuaged through the end of the year - the S&P 500 had its worst December since 1931, bringing its Q4 decline to nearly 14%, and making 2018 the worst year for the index since 2008 with a dismal return of -6.2%.

Between 2018’s placid start and furious conclusion, there were a number of other developments, in both the domestic equity market and elsewhere. Contrary to 2017, during which technology, basic materials, industrials, and consumer discretionary were among the best performing domestic equity sectors, 2018 saw the traditionally more-defensive utilities and healthcare sectors turn in the strongest performances as investors sought safety in the final months of the year. Meanwhile, energy, financials, and industrials were among 2018’s weakest performers.

International equities enjoyed a strong 2017, with both developed and emerging equities outpacing the S&P 500; however, both hit the skids in 2018 with no shortage of factors acting as headwinds. The U.S. dollar, which had weakened fairly steadily in 2017, rebounded in 2018, diminishing returns on foreign assets to domestic investors.

Turkey’s high level of foreign-currency debt and President Erdoğan's refusal to raise interest rates to combat high inflation raised concerns about the nation’s ability to meet its obligations to international lenders. The Turkish lira declined more than 45% against the U.S. dollar from February to mid-August and fears of contagion roiled international currency and equity markets, especially among emerging economies. Meanwhile, the same trade worries that weighed on US markets were also a major headwind for the Chinese equities market, which makes up the lion’s share of many emerging market indexes. Most broad emerging markets funds finished the year in deeply negative territory.

The year was not much better for developed international markets as other geopolitical concerns, including Brexit negotiations, were unfavorable for these markets. Finishing down more than 16.5% for 2018, the MSCI EAFE Index gave up nearly all of the gains it had made

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since the year 2000 – from December 31, 1999, through December 31, 2018, the index returned -0.12% on a price return basis.

2018 also saw significant movement within fixed income. US Treasury rates increased markedly in the first two months of the year and the yield on the 10-year note peaked near 3.25% in September - its highest level in more than five years. Yields then declined sharply in the final months of the year, as the sell-off in the US equity market was accompanied by a spike in demand for US Treasuries and municipal bonds. The late-year bond rally did not extend to credit, as spreads on investment grade and high yield corporate bonds widened. International bonds, which had been a safe haven for investors as rates climbed at the beginning of the year, reversed course as the US dollar strengthened, causing many international bond funds to finish the year in the red. Meanwhile, weakness in the equity markets weighed on convertible bonds, which had been amongst the best performing fixed income segments in 2017 and early 2018.

Coming into the year, Energy was the strongest area of the commodities market, however, amidst concerns of a glut in the supply of crude oil and uncertainty about OPEC's willingness or ability to cut production levels, crude prices tumbled in the final months of the year, finishing 2018 in negative territory. The market for industrial metals also weakened, as the trade dispute fostered worries about slowing demand, the same concerns also hampered some agricultural markets, such as soybeans.

While the overall story for 2018 was decidedly negative, the final days of December and the first few days of 2019 have provided some cause for optimism. The Bullish Percent for the NYSE and the Bullish Percent for the S&P 500, which each measure the percentage of stocks in within their respective universes that are on Point & Figure buy signals, have each reversed up from near-historic lows, indicating that we have begun to see demand return to the market. Similarly, the NYSE High Low Index, which measures the percentage of stocks on the New York Stock Exchange hitting new 52-week highs vs. those hitting new 52-week highs and lows, has also begun to climb after reaching extremely washed out levels, also indicating that the US equity market may have found its footing.

As always, we will continue to monitor your portfolios and make any necessary changes as leadership changes within the market. If you would like to become more familiar with my investment process and the tools I use to identify market leadership across major asset classes and within asset classes, please contact me at your convenience.

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P.S. If you think this type of information would be of benefit to anyone you know, please share this communication with them.

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