Market Observations
June 2018

DISPARITIES

Financial markets have provided the good, the bad and the relatively mundane in the first five months of 2018. Amidst it all, however, and over longer periods of time, disparities among market sector returns wax and wane. These disparities provide opportunities to enhance portfolio returns over time. A review of some closely followed sector relationships can provide perspective.

Perspective

Return disparities between growth stocks (above average earnings growth, below average dividend rates) and value stocks (above average dividend rates, below average earnings growth) are shown in Chart I. For longer stretches of time, one sector has out-performed the other. More recently, the return advantage has been to growth stocks (e.g., Alphabet ("Google"), Amazon, Apple). The average 12-month return over the past 30 years has favored growth stocks at 11.8% versus 10.3% for value. In addition, the frequency of out-performance has favored growth stocks 64% of the time.

Chart I

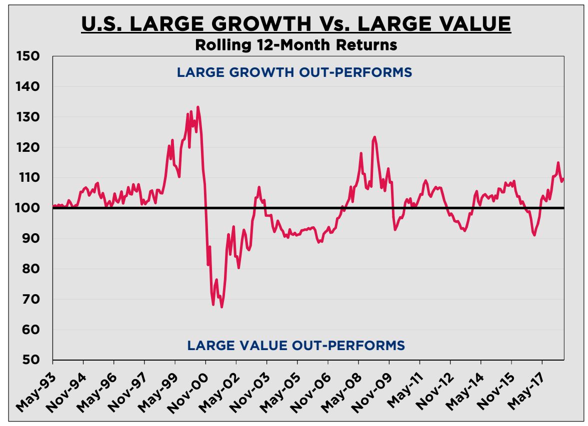
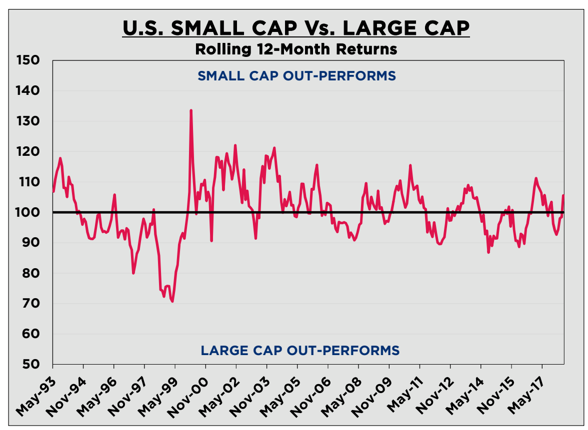


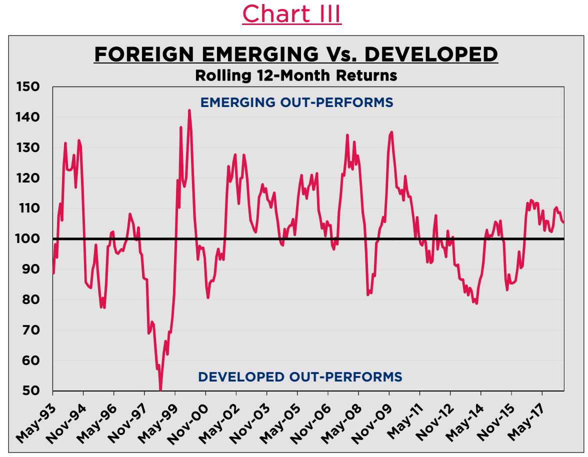
Chart II shows the return disparities between small cap stocks and large cap stocks. Here the return advantage of one sector over the other has shifted with more frequency over time. The return advantage turned to small cap in just the past month after several months of advantage to large cap. The average 12-month return over the past 30 years has been quite close, 11.3% for small cap versus 11.2% for large cap. Also close has been the frequency of small cap out-performance at only 52% of the time.

CHART II



The relative returns of foreign emerging market stocks and foreign developed market stocks, plotted in Chart III, show another and different pattern of disparity. The return advantage shifts between the two sectors with some frequency. More notable are the pronounced extremes of relative out-performance and under-performance. The average 12-month return over the past 30 years has favored emerging markets decidedly at 11.7% versus 8.3% for developed markets. The frequency of out-performance has favored emerging markets as well 59% of the time.

Chart III



Investment Implications

If sector returns were to merely mirror each other, little is to be gained from their analysis. They do not. Therein lie both challenges to and opportunities for portfolio management. Differing impacts of changes in fundamentals on market sectors often drive return disparities. When as now fundamentals such as interest rates, tax law and regulation are in states of flux, disparities can become more pronounced. A disciplined approach to assessing return disparities among market sectors is an important part of prudent portfolio diversification.