FLEURUS INVESTMENT ADVISORY

May 4, 2019

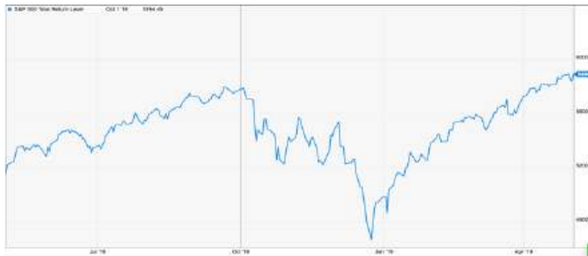
Overview

April was another good month for equity investors! It seems as if the end of 2018 was just a bad and now distant dream.

The S&P's 500 rose 4.05% in March. The Nasdaq Composite added 4.77% while the Russell 2000 (US Small Caps) rose 3.81%.

Most international markets replied in kind but with less gusto. The S&P EPAC BMI (developed markets) was up 2.30%, while the MSCI EM (emerging markets) went up 2.11% and the Frontier Market index rose a meager .25%. A slightly stronger USD explains in part this relative international underperformance vs. US indices.

The S&P's 500 has now recovered all of the ground it lost in the last quarter of 2018, as illustrated below.



Meanwhile, in the US fixed income markets, the long bond retreated -2.25% in April. The Investment Grade sector was up a small .54%, while High Yield bonds rose a stronger 1.42%, as the market saw the risk of a recession receding.

In April, our client portfolios were up from 1.37% to 2.13%. This compares to a monthly performance of 1.61% for a portfolio consisting of 50% ACWI (World Equity Index ETF) and 50% AGG (US bond aggregate proxy). On a Year-To-Date (YTD) basis, our portfolios are up from 8.72% to 12.55% (net of fees) vs. 9.51% for our benchmark.

As a reminder, the equity allocation in our clients' portfolios ranges currently from 30% to 60%, depending on their risk profiles.

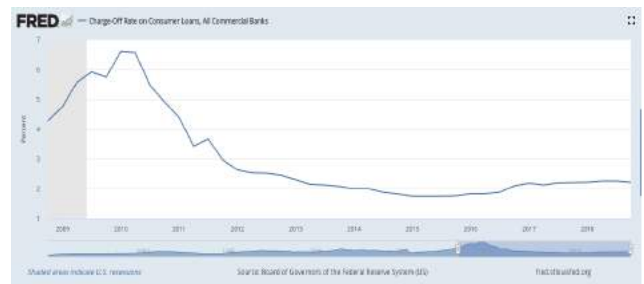
Market developments

April was rich in economic data points. All of them supportive for equities. The month started with a good Purchasing Manager Index (a measure of industrial activity), followed by better than expected first quarter earnings from JPMorgan and a few other banks.

Then came the financial settlement between Qualcomm and Apple, in the middle of the month, and the quasi simultaneous release of more supportive earnings from several corporations. The month ended on a strong note with the release of the GDP number for the first quarter at 3.2%. The number was substantially above expectations and helped reassure investors that fears of a recession were unsubstantiated for now. Adding to the positive mood, the CPI number released on April 29, showed no acceleration and relatively benign wage pressures.

The economic environment, as reflected in the data releases in April, is improving and fears of recession, inflation, trade wars are all receding, pushing equity indices up.

All of this is happening while the average US consumer remains in relatively good financial health, supported by a strong job market. Below is a chart that tracks the level of consumer loan defaults:



Consumer loan defaults, a measure of financial stress, are at about 2.25% of total loans outstanding and remain well below crisis levels. Although they have ticked up in the past two years, their level remains relatively constant and rather re-assuring for now.

It is unlikely that this important measure of the health of the US economy will deteriorate in the coming month, unless the employment picture darkens rapidly. An unlikely development at this stage.

Tilts and Allocations

After increasing moderately our exposure to growth US equities in March we refrained from adding to our positions in these sectors in April, awaiting confirmation of an improving economic picture before committing. We have had this confirmation in April and will likely increase our US equities exposure in the coming weeks.

A note of caution though. We are entering a season of generally lower performance. More often than not, the period from May to the end of August is one were US equity indices do worse than during other periods of the year. This does not mean that the next four months will be difficult but rather than the exceptional pace of performance since the beginning of the year is likely to slow. While I intend to deploy more of our liquidities to US equities soon, I will do so with an awareness of the seasonality factor just mentioned.

In April, we continued to add carefully to our exposure to German equities, on the belief that they would benefit from a positive resolution of the US-China trade negotiations. So far, we are happy with this decision. Below is a chart for EWG, a German ETF that we use as a proxy for investments in German equities.

Since early March EWG is up close to 5% and has outperformed other Eurozone and Japanese equities. It is likely that this positive momentum will endure as China and the US arrive, finally, at a resolution of their trade entanglements. Germany's export driven manufacturing sector is significantly impacted by the health of the Chinese economy. Any improvement on the trade front between China and the US should benefit it disproportionately.

Concluding remarks

First quarter earnings have been good. Better than expected. Inflation remains benign and the Federal Reserve appears happy to maintain a neutral stand for now. Neither eager raise interest rates nor eager to reduce them.

We seem to have arrived at a rather pleasant point in this economic cycle with no recession in site, moderate inflation, quasi-full employment, a strong financial sector and an improving global trade environment.

The skeptic in me wonders what could go wrong with this picture but will try to enjoy this moment while it lasts. After a particularly trying end to 2018, I encourage you to do the same and to not worry too much.

Thank you again for your continued trust.

Jeff de Valdivia