April 13, 2018
Volume 19, Number 1

Nauset Market Commentary
First Quarter 2018

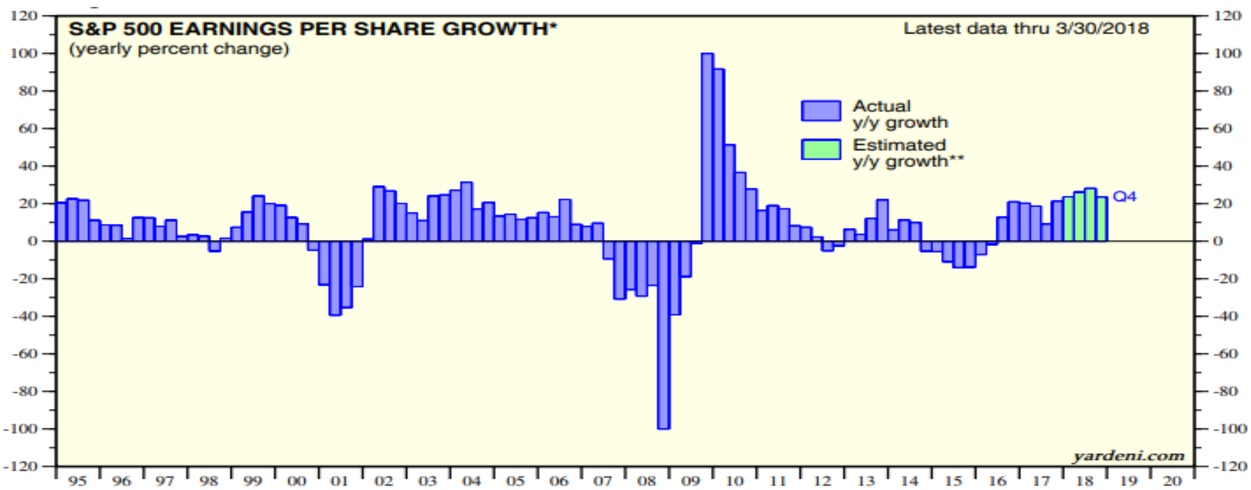
Market Performance Recap: **Stocks Stumble Amid Volatility**

The nine-quarter US stock market win streak is over. A choppy quarter signaled a return to normal volatility with stocks slightly off as the Russell 1000 US stock index fell -0.7% in Q1. Tech and consumer service were the only positive stock sectors, while telecom and real estate lagged the most. International stocks were split with developed country EAFE index off -1.5%, while the Emerging Markets index gained +1.4%. A rise in yields and a Fed rate hike in March hurt bond prices, causing a -1.0% decline in the Barclays Intermediate Gov't/Credit bond index.

Economic & Market Discussion: **Lower Rewards, Higher Risks**

In a return to normal market dynamics, up and down stock volatility is much sharper this year versus last. Following 2017's strong, smooth stock rally, any stock gains achieved this year will need to struggle through the headwinds of rising rates, higher valuations, trade issues and political dust-ups.

- All About Earnings – We remain constructive on US equity based on solid earnings growth expectations. Analysts estimate that S&P 500 corporate earnings will continue to be very strong in 2018, growing at +20% levels based on tax reform and positive momentum for US and global economies. Stock gains will depend on firms delivering on earnings expectations.



* Yearly growth rates capped at +100% and -100% due to extreme values.
** Industry analysts' consensus expected earnings growth.
Source: Standard & Poor's.

- Trade Tantrums – Much of recent market volatility is due to US trade tariff proposals and concerns about a trade war with China. We expect trade fears to continue to buffet markets as new trade terms and deals are negotiated. These developments bear close monitoring as any trade-limiting policies will likely hurt financial markets.
- Up, Up & Away? – While trade policy is important, rising rates and inflation remain the most significant investor concern regarding financial markets. The upward direction of rates makes borrowing more expensive, eating into corporate profits and consumer spending. While we believe that the Fed will move cautiously in raising rates, and inflation will not rise too quickly, any upward movement in rates or inflation is a negative, or at best, neutral for stocks.

Portfolio Strategy: **Proceed with Caution**

Based on strong earnings projections, our strategy continues to favor stocks over bonds. However, fully-valued stock levels and volatility from rising rates and trade policy uncertainties will likely mute returns.

- Diversified Equity Exposure – Our slight overweight to stocks emphasizes specific US sectors of tech, finance and health care coupled with both non-US developed and emerging markets areas.
- Defensive Fixed Income – In a rising rate environment, our fixed income position is underweight and allocated to multi-sector and hedged fixed income funds with short duration strategies.

NAUSET WEALTH MANAGEMENT

- Volatility Buffers – We manage risk using alternative and real asset investments that seek returns with low correlations to major market movements. We expect these two areas plus cash holdings to lessen portfolio volatility while providing different sources of return over time.

Market Performance **% Change for Periods Ended 3/31/2018**

Market Index	First Quarter	2018 YTD	1-Year	3-Year Annual.	5-Year Annual.
Russell 1000	-0.69	-0.69	13.98	10.39	13.17
MSCI EAFE – Non-US	-1.53	-1.53	14.80	5.55	6.49
Russell 2000	-0.08	-0.08	11.79	8.39	11.47
MSCI Emerging Markets Equity	1.42	1.42	24.93	8.81	4.99
DJ US Real Estate	-5.91	-5.91	0.13	2.88	6.28
NASDAQ 100	2.33	2.33	19.50	12.96	16.67
Barclays Gov't/Credit Interm. Bond	-0.98	-0.98	0.35	0.94	1.25
Wilshire Liquid Alternative	-0.99	-0.99	2.59	0.53	1.30
3-Month T-Bill	0.35	0.35	1.07	0.49	0.31