Fourth Street
Performance Partners
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December 2018: Market Review

Global equity prices sank in December as all major indices posted significant declines. The selloff was driven by fears of a global economic slowdown, earnings revisions, stretched valuations, Fed policy, and political tensions. The S&P 500 plunged -9.0%, the worst December since 1931. The index erased all gains for the year during the month, ending the year down -4.4%. December also saw heightened volatility as the S&P 500 was up or down more than 1% on nine trading days during the month, compared to just eight similar moves in the entirety of 2017. The Dow Jones Industrial Average tumbled -8.6% and was down -3.5% for 2018. The tech-heavy NASDAQ Composite fell -9.4% during the month (-2.8% for the year) as big tech was plagued by ongoing fears of slower growth and increased regulation.

In U.S. economic news, trade tensions began to cool as the U.S. and China delayed implementation of higher tariffs. The Fed raised the target interest rate range to 2.25 - 2.50% in December and signaled two additional increases for next year. The final reading of third quarter real GDP growth came in at 3.4%, down modestly from November's estimate. The most recent S&P/Case-Shiller National Home Price Index report showed that on a month-over-month basis, home prices were up +0.1% in October, while on a year-over-year basis, prices were +5.5% higher than a year ago. Among commodities, WTI crude oil ending December at $45 a barrel, down from November's closing price of $51 in response to continued oversupply and fears of a slowing global economy. Oil posted the first year of losses since 2015. Gold closed the month at $1,278 per troy ounce, up from $1,176 at the end of November.

Growth and value stocks performed relatively in line amongst all capitalization sizes, but growth slightly edged out value in December. For 2018, growth equities maintained their outperformance by a wide margin. Among large cap stocks, the Russell 1000 Growth Index fell -8.6% in December, returning -1.5% for the year. The Russell 1000 Value Index lost -9.6% for the month, which brought its return to -8.3% for 2018. For small cap stocks, the Russell 2000 Growth Index decreased -11.7% in December and ended 2018 down -9.3%. The Russell 2000 Value Index slipped -12.1% and declined -12.9% in 2018. In mid cap equities, the Russell Midcap Growth Index lost -9.1% in December, falling -4.8% for 2018. The Russell Midcap Value Index slid -10.5% for the month and declined -12.3% for the year.

While all major international equity indexes posted negative results in December, international equities edged out U.S. equities for the month. The MSCI EAFE Index fell -4.9% for the month, resulting in a loss of -13.8% for 2018. The MSCI Europe Index dropped -4.6% in December and posted a -14.9% return for the year. The MSCI Pacific Index lost -5.1% during the month and fell -12.0% in 2018. The MSCI Emerging Markets Index was the best relative performer in December, down only -2.7% for the month. Emerging market returns were negatively impacted by weakness in Pakistan (-12.4%) and China (-6.1%). The MSCI Emerging Markets Index declined -14.6% for the year.

In this risk-off environment, most major fixed income indexes posted positive results in December. The yield on the 10-Year Treasury closed December at 2.68%, down from last month's close of 3.01%. The Bloomberg Barclays U.S. Aggregate Bond Index added +1.8% for the month, essentially flat for the year. The Bloomberg Barclays U.S. Treasury Index gained +2.2% in December, rising +0.9% for 2018. The Bloomberg Barclays Treasury 20+ Year Index appreciated +5.6% during the month, ending with a return of -2.0% for the year. The Bloomberg Barclays Corporate High Yield Index lost -2.1% for both December and the year.

December's results made 2018 the worst calendar year for stocks since 2008. Giant tech stocks that have fueled this long bull market face concerns regarding slower demand and fears of greater regulation. Even with some indication that the U.S. and China plan to de-escalate trade tensions, it remains to be seen whether the two nations can find common ground. Corporate profits remain strong, but higher input costs may be problematic. Ongoing trade tensions, slow earnings growth, a tightening Federal Reserve, and a strong U.S. dollar could continue to be headwinds for global equity markets.