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Manager Commentary – 1st Quarter, 2018

After a strong year for equity markets in 2017, the S&P 500 continued the trend into January, rising almost 6%; however, as the calendar turned to February and President Trump announced future tariffs and fears of a potential trade war between the US and China progressed, accompanied by concerns over interest rate rises (LIBOR particularly) the markets took a negative, and volatile, step back. Of note, the first quarter saw *twenty-three* days of a +/- 1% gain/loss, which can be compared to two such days in the first quarter of 2017. Going further, the markets saw *six* days of +/- 2% gain/loss, which can be compared to zero in the first quarter of 2017. The first quarter showed a marked increase in volatility, which has been generally absent since 2011. February saw a selloff that was triggered by strong wage growth numbers from the US as it appeared to accelerate from 2.5% to 2.9% year-over-year (YoY), which caused investors to worry that interest rates would rise faster than anticipated. As the S&P 500 rose almost 6% in January to a high on January 26th, stocks soon retreated and as of February 8th were down -10% peak to trough. In the beginning of March, it appeared a degree of calm had returned; however, global equities proceeded to demonstrate increased volatility due to growing fears of a global trade war.

Despite all the headlines and volatility, the US markets ended relatively flat, down -0.8% for the quarter, while MSCI Europe ex UK returned -3.0%, the Japan TOPIX -4.7% and the UK FTSE 100 was the worst major market, down-7.2%. The European Central Bank (ECB) appears to be in no rush to raise interest rates and while the removal of quantitative easing by the end of the year still seems likely, there does not seem to be short term urgency for the ECB to begin raising rates.

U.S. Equity Strategy

In March, the Belridge U.S. Equity Strategy outperformed its benchmark, returning -1.9% versus -2.1% for the Russell 3000 NR Index. The strategy saw strong performance in the Energy, Financials, and Information Technology (IT), while the Industrials and Consumer Staples sectors were challenged. Despite the volatility, Energy returns remained positive as the sector returned 3.7% as standouts were, Marathon Petroleum 14.1% and Phillips 66 6.1%. In Financials, MarketAxess, had a positive month, returning 7.5%. The Industrials holdings were the most challenged for the month, mainly by American Woodmark, which was caught up in the volatile month, and for the quarter returned -23.3%.

In the first quarter, the U.S. Equity Strategy outperformed its benchmark, as it returned -0.3% versus -0.8% for the Russell 3000 NR Index. The quarter saw strong relative performance from the Energy, Financials, and Health Care sectors while, much like the month of March, the Consumer Staples and Industrials sectors were challenged. The strongest contributors in the Financials sectors were Mastercard, which returned 15.9% and S&P Global, which gained 13.1%. In Health Care, Progenics Pharmaceuticals gained 25.4% and AMN Healthcare returned 15.2%. The Consumer Staples sector struggled for the quarter as CVS Health lost -13.7%, while one of our largest and longest-term holdings, PepsiCo, lost -8.3%. There were a few significant changes to the strategy during the quarter as we added, Microsoft and Amazon, in the IT and Consumer Discretionary sectors, respectively. Also, there was a sale of a long-term Consumer Discretionary holding, Best Buy, in early March. In Health Care HMS Holdings was sold, and Laboratories Corp of America was purchased. The strategy maintains a cash level of approximately 3% and as of March 31, held 74 companies.

International Equity Strategy

In March, the Belridge International Equity Strategy outperformed its benchmark, as it returned -0.1% versus -1.8% for the MSCI ACWI ex USA NR Index. The strategy saw strong relative performance from all sectors; in particular, Consumer Staples, Energy, and Financials. In the Consumer Staples sector, Unilever returned 7.8%, Reckitt Benckiser Group gained 4.2%, and Heineken NV returned 3.7%. In Energy, Total SA gained 3.1%, while Eni SpA returned 6.5%. Most major sectors had top contributors which led the strategy to a solid outperformance in a generally negative environment.

In the first quarter, the International Equity Strategy outperformed its benchmark, as it returned 0.1% versus -1.2% for the MSCI ACWI ex USA NR Index. Information Technology, Financials, and Consumer Staples led the way while Consumer Discretionary and Telecom slightly underperformed. In Information Technology, Yandex returned 21.3%, Taiwan Semiconductor gained 10.4%, and Tencent Holdings gained 2.6%. Erste Group Bank and Sberbank of Russia led the way in Financials as they gained 15.9% and 10.0%, respectively. Despite solid performance across the strategy, Consumer Discretionary was slightly challenged as Technicolor lost -52.3%, which led to 30 bps lost in the Consumer Discretionary sector. Towards the end of the quarter we made several changes to the strategy as we sold a long-term Information Technology holding, Yandex, as well as a sale of Vestas Wind Systems in the Industrials sector. We added a few new stocks in the Consumer Staples (Coca-Cola European Partners PLC), Financials (Close Brothers Group PLC), and Industrials (Embraer SA) sectors to bring our total number of securities up in the strategy. The International Equity strategy maintains a cash level of approximately 3.5% and as of March 31, held 64 companies.

Health Care Strategy

In March, the Belridge Health Care Strategy outperformed its benchmark, returning -1.8% versus -3.1% for the Health Care Select SPDR. The strategy saw solid relative outperformance yet it showed a mixed bag within and amongst the industries. The biotechnology industry provided two of the largest gainers in the strategy, Regeneron and Progenics Pharmaceuticals, which gained 7.5% and 11.7%, respectively; however, biotechnology also provided the three biggest laggards in AbbVie, FibroGen, and Ionis Pharmaceuticals, which returned -18.3%, -16.2%, and -16.6%, respectively. Pharmaceuticals generally had a strong month led by The Medicines Co, which returned 7.6%.

In the first quarter, the Health Care Strategy outperformed its benchmark, as it returned 2.7% versus -1.3% for the Health Care Select SPDR. The Health Care Providers/Services and Health Care Equipment/Supplies industries showed strong outperformance during the quarter while the Biotechnology industry, much like March, was mixed. In Health Care Providers/Services, AMN Healthcare Services returned 15.2% and Quest Diagnostics returned 2.3%. In the Health Care Equipment/Supplies industry, Stryker Corp returned 4.2% and Masimo Corp gained 3.7%. In Biotechnology, Progenics gained 25.4% and Macrogenics gained 32.4%. On the other side of Biotechnology, Regeneron struggled as it lost -8.4%, while Ionis Pharmaceuticals lost -12.4%. HMS Holdings was sold in March and Laboratories Corp of America, a Health Care Providers/Services holding was added. As of March 31, the Belridge Health Care Strategy held 15 companies.

All Belridge Strategies outperformed this quarter, remain concentrated in nature, and include exposure across small-, mid-, and large-capitalization stocks. We continue to seek and own securities of high quality companies with long term earnings potential. As always, we emphasize security selection through our portfolio construction process.

Best Regards,

Daniel B. Wanzenberg, Chief Investment Officer

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