October 11, 2018

COLONY MARKET BRIEF

Global equity markets experienced a significant selloff yesterday. For example, the S&P 500 Index declined -3.3% on Wednesday—the largest daily decline since February 8, 2018. All sectors in the S&P 500 slumped Wednesday, with technology stocks down nearly 5%. It was also the fifth consecutive session of declines and longest losing streak in nearly two years. As we've acknowledged in the past, experiencing volatility is an expected byproduct of investing—but it can certainly be uncomfortable. As such, we wanted to share our perspective. We'll also be distributing a detailed market review/outlook commentary soon.

Nothing fundamentally changed yesterday, but clearly market sentiment can shift quickly. While no one factor triggered the drop, some investors are highlighting fresh news of damage to corporate earnings from the trade war, along with intensifying pressure from the global shift away from monetary stimulus.

Reminiscent of the equity market selloff in February of this year, recent weakness comes amidst a backdrop of higher bond yields. Last week Federal Reserve Chairman Jerome Powell said that the central bank is "a long way" from getting rates to neutral, a fresh sign that he believes more hikes are coming. Responding to both Powell's comments and stronger US economic data, government bond prices declined while the yield on the 10-year US Treasury rose to 3.2%, its highest level in seven years.

Also worth noting is that midterm election years in the US tend to be more volatile. Analysts often chalk it up to uncertainty since midterms typically see the incumbent president's party lose seats. Yet, historically markets have recovered as election day nears and in the aftermath of the vote, regardless of the outcome, as uncertainty begins to fade.

In the near-term, investor focus will likely shift to the third quarter earnings reporting season which kicks off on Friday. According to FactSet, S&P 500 companies are expected to report year-over-year earnings growth of 19%, but guidance for 2019 will be key. Large banks, such as JP Morgan, Citigroup, and Wells Fargo, are among the first companies to report. Strong bank

earnings could be a positive catalyst—it's often said that they set the tone for the rest of the earnings season as these companies are highly levered to the economy.

We'll continue to assess recent developments in order to determine any changes to our macro views and portfolio positioning. At this point, we still view the global economic backdrop as being in pretty good shape—but as we've previously communicated, the outlook has become more uncertain in the face of ongoing trade disputes and rising interest rates. Although it's certainly uncomfortable to experience, we do expect volatility to remain elevated as global central banks seek to tighten monetary policy and as geopolitical risks persist.

In terms of portfolio strategy, we continue to target a slight underweight position in US equities while emphasizing large cap, high quality stocks and more reasonably priced international and emerging markets. We've also continued to maintain an elevated cash/short-term fixed income position as "dry powder" that we could put to work if recent volatility presents what we think are attractive investment opportunities. Recent market action also reinforces the rationale for owning certain flexible/alternative strategies that have different risk and return drivers versus traditional stocks and bonds—and that can potentially benefit from elevated market volatility and increased dispersion.