Resources Management Corp

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MARKET COMMENTARY

The United States equity markets have performed well over the last year, with the S&P 500 returning 19.4% for the year ended December 31, 2017. This strong performance was spread across the majority of sectors, led by technology with a 36.9% return for the period. As can be seen in *Figure 1*, valuations appear to be reasonably full across all sectors by historical standards. The S&P 500 is currently trading at 18.5x median expected earnings for 2018, which is 2.5 turns higher than the 20-year historical average of 16.0x. These valuations, however, exist within the context of a historically low interest rate environment, an economy that has finally returned to GDP growth in excess of 3.0% and an unemployment rate that is at a 17-year low. Given that this strong performance has been driven by fundamental improvements at the company level and a strengthening economic landscape, we do not view current valuations as exorbitant.

After several years of underperformance, European equity markets performed well in 2017 returning 26.2% (as measured by the MSCI Europe Index), and global equity markets followed suit, returning in excess of 23.0%. Much like in the United States, these returns were driven by fundamental improvements in the economic landscape, coupled with monetary policy that has been, and is expected to remain, highly accommodative for an extended period of time. With the exception of the impact of BREXIT, which remains unknown, global economic outlook remains strong.

As we consider 2018 and beyond, the impact of tax reform will be in focus. The reduction of the corporate tax rate from 35%, which was among the highest in the developed world, to 21% will provide a clear boost to earnings in both the near and medium term. While it remains to be seen what the long-term impact of this reduction will be, it is our expectation that this will be a net benefit for the U.S. economy overall. The repatriation holiday will allow companies to bring back overseas cash at a rate of 15.5% compared to the 35.0% rate it was at previously. This has already begun to have an impact, which can be seen through the announcement of additional domestic investment, increased wages and the expectation of increased buyback activity. All of this should provide a near term boost to both economic and market activity.

Monetary policy will also continue to be front of mind as Jerome Powell succeeds Janet Yellen as chairman of the Federal Reserve. It is our expectation that Mr. Powell's approach to raising rates will be very similar to that of Ms. Yellen, with very measured changes that are sensitive to economic developments and shifts in inflation expectations. We would view slow increases that coincide with economic strength as positive developments for the market. While the Fed has been effective, thus far, in communicating and executing their strategy, a policy misstep that either raises rates too quickly or allows for outsized inflation could cause a serious disruption. We remain keenly focused on the evolution of the Fed's policy, and will continue to adjust our interest rate expectations accordingly.

Overall, we view the state of the economy as strong and valuations as reasonable given the current landscape. While there are certainly risks to the strong performance the equity markets have experienced recently, we continue to view the risk / reward relationship as favorable. It is always the unexpected that shocks the security markets, but portfolios that are structured with diversified exposures should allow for an adequate return profile to persist over the long term.

FIGURE 1

Global Equity Overview

January 2018

	Stock Performance			Current Valuation			20 Year Historical Average[1]		
	YTD	1 Year	5 Year	Trailing P / E	Fwd. P / E	Div. Yld.	Trailing P / E	Fwd. P / E	Div. Yld.
S&P 500	19.4%	19.4%	87.5%	24.7x	18.6x	2.1%	19.6x	16.0x	2.0%
Consumer Discretionary	21.2%	21.2%	108.8%	27.4x	22.4x	1.8%	19.3x	18.1x	1.4%
Consumer Staples	10.5%	10.5%	62.8%	22.5x	20.2x	2.6%	21.0x	17.1x	2.6%
Energy	-3.8%	-3.8%	0.1%	N / A	23.7x	2.6%	17.0x	17.4x	2.3%
Finance	20.0%	20.0%	109.7%	19.5x	13.7x	1.8%	15.5x	12.9x	2.3%
Healthcare	20.0%	20.0%	106.6%	25.5x	17.6x	2.0%	24.1x	17.6x	1.8%
Industrial	18.5%	18.5%	94.0%	24.0x	19.7x	1.8%	20.0x	16.3x	2.1%
Materials	21.4%	21.4%	59.5%	26.1x	19.0x	1.8%	19.4x	13.8x	2.6%
REITs	7.2%	7.2%	34.8%	38.8x	20.5x	3.7%	35.4x	15.2x	4.4%
Technology	36.9%	36.9%	138.5%	27.4x	20.0x	1.7%	25.6x	20.8x	1.0%
Telecom	-6.0%	-6.0%	13.7%	16.0x	13.2x	5.1%	20.3x	16.6x	4.0%
Utilities	8.3%	8.3%	50.5%	19.8x	16.5x	3.6%	15.8x	14.0x	4.1%
Dow Jones Industrial Avg.	25.1%	25.1%	88.6%	26.4x	18.5x	2.0%			
Nasdaq 100	31.5%	31.5%	140.4%	27.9x	21.9x	N / A			
FTSE 100	7.6%	7.6%	30.3%	20.8x	14.8x	3.7%			
Nikkei 225	19.1%	19.1%	119.0%	19.8x	18.3x	1.5%			

(1) Source: J.P. Morgan Asset Management