

## The Yield Curve Is Flattening Relentlessly

The spread between 5- and 30-year Treasury yields, as well as the gap for 2- and 10-year maturities, tumbled Wednesday to the lowest levels since 2007, at 37.2 basis points and 45.7 basis points, respectively. The flattening accelerated after consumer price index data came in largely as expected, perhaps bringing other market-moving events, like President Trump's threat of a [missile attack](#) on Syria, into focus. "CPI, or any other economic data release, is a back-burner item when you have so much geopolitical risk on the forefront," Tom di Galoma, managing director of government trading and strategy at Seaport Global Holdings, said in an email.



*Could the flattening of the Yield Curve cause the next Recession? We'll see! - Drew*

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## S&P warns of risks in leveraged loan market as deals surge

S&P Global has warned investors in the \$1tn leveraged loan market that weak lending terms pose a risk as the credit cycle approaches a peak and deal making has surged in recent months. While a number of high-profile investors have warned of the risks of leverage in the \$8.8tn US corporate bond market, money continues pouring into the US loan market, where interest rates are floating and adjust higher as the Federal Reserve tightens policy. Bank loan funds have attracted more than \$3bn of money this year, following 2017's \$15bn haul, according to EPFR.

That has bolstered confidence among dealmakers that they can finance mergers and acquisitions. Takeovers worth more than \$1.2tn have been announced so far this year, up more than 45 per cent from a year prior, Dealogic data shows.

The New York-based rating agency warned that leverage was approaching or exceeding levels seen before the financial crisis in the US and Europe, and that companies and private equity firms were willing to pay more to clinch deals than at any time since at least 2003 in the US.

### The Yield Curve Just Inverted

As we have told readers, we have been keeping our antennae up for signs that an economic downturn may be on its way. Well, the biggest one of all just showed its head, and investors need to take notice. An important part of the rates market just showed an inverted yield curve. The one-month U.S. overnight indexed swap rate is now inverted, and this implies some expectation of a lower Fed policy rate after the first quarter of 2020, says JP Morgan. The Bank summarizes the situation this way, saying "An inversion at the front end of the U.S. curve is a significant market development, not least because it occurs rather rarely ... It is also generally perceived as a bad omen for risky markets".

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### QUOTE OF THE WEEK

*"Innovation distinguishes between a leader and a follower."*

*- Steve Jobs*

# Taking a comprehensive look at the overall current stock market

Taking a comprehensive look at the overall current stock market, you can see the chart below representing eight major indices and their returns through the week ending April 13, 2018. In a truly diversified portfolio, the portfolio's total return is determined by the performance of all of the individual positions in combination – not individually.

So, understanding the combined overall performance of the indices below, simply average the 7 indices to get a better overall picture of the market. The combined average of all 7 indices is –0.76% year to date.

Index	Last Week			One Month		Year-to-Date	
	Close	Net Change	% Change	Net Change	% Change	Net Change	% Change
S&P 500 Index	2656.3	51.83	1.99%	-109.01	-3.94%	-17.31	-0.65%
Dow Jones Industrial Average Index	24360.14	427.38	1.79%	-646.89	-2.59%	-359.08	-1.45%
Nasdaq Composite Index	7106.65	191.54	2.77%	-404.36	-5.38%	203.26	2.94%
60/40 Portfolio (BAGPX)	13.03	0.14	1.09%	-0.21	-1.59%	-0.06	-0.46%
US Aggregate Bond Index	2011.83	-3.56	-0.18%	6.43	0.32%	-34.54	-1.69%
Markit iBoxx USD Liquid High Yield Index	269.95	2.57	0.96%	2.46	0.92%	0.82	0.30%
20+ Year Treasury Bond (TLT)	120.9	-0.2	-0.17%	1.96	1.65%	-5.44	-4.31%

Data Source: Investors FastTrack, Yahoo Finance

## Term of the Week: Sharpe Ratio

The Sharpe ratio is the average return earned in excess of the risk-free rate per unit of volatility or total risk. Subtracting the risk-free rate from the mean return, the performance associated with risk-taking activities can be isolated. One intuition of this calculation is that a portfolio engaging in “zero risk” investment, such as the purchase of U.S. Treasury bills (for which the expected return is the risk-free rate), has a Sharpe ratio of exactly zero. Generally, the greater the value of the Sharpe ratio, the more attractive the risk-adjusted return.

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# Dow Jones - Week Ending

## WEEKLY MARKET SUMMARY

**Global Equities:** For a week that included a no-knock raid on the office of President Trump's personal lawyer, a Presidential tweet threatening to start World War III, and Facebook (ticker: FB) CEO being grilled on privacy breaches by House and Senate members, equities traded in a relatively benign fashion when compared to prior weeks. Earnings season has begun as the major equity indices ended the week positive, led by the Nasdaq Composite with a 2.75% gain, followed by the S&P 500 up 2%, and the Dow Jones Industrial Average up 1.8%. Energy continued its impressive run and led all sectors with a nearly 6% increase, while interest rate sensitive sectors including Utilities and Real Estate lagged during the week. Developed International equities traded in tandem with US large-cap equities, as Emerging Markets underperformed though still managed close to a 1% rise.

**Fixed Income:** The yield on the US 10-Year Treasury Note increased to 2.82% after a choppy week, as inflationary pressures continue to show in US economic data. High-yield debt continued to be constructive in the face of deteriorating investor sentiment as spreads consistently tightened during the week. The iShares IBoxx High-Yield Corporate Bond ETF (ticker: HYG) ended the week up over 1%, while high-yield funds saw significant inflows after several weeks of outflows.

**Commodities:** Oil prices climbed all week, thanks to Trump tweets and rising Middle-East tensions. Brent Crude closed the week at \$72.43 per barrel, while the US benchmark West Texas Intermediate increased nearly 8% to \$67.27 per barrel. Even the EIA Petroleum

Status report indicating a whopping 3.3-million-barrel surprise increase in crude oil inventories, or the Baker Hughes increase in rig count, could not slow down the rally. Natural Gas prices also ended the week higher to \$2.74/MMBtu.

## WEEKLY ECONOMIC SUMMARY

**Consumer Price Index (CPI):** The CPI dropped for the first time since May 2017, as decreasing gasoline prices led to a .1% month-on-month (MoM) decrease for the month of March. A significant jump in the CPI year-on-year (YoY) increase of 2.4% was expected, because it was last March that wireless costs plunged when Verizon Communications Inc. (VZ) started offering unlimited data plans. The core measurement of CPI, that excludes food and energy, was in line with consensus estimates gaining .2% MoM and 2.1% YoY. Apparel prices helped put downward pressure on CPI, while dental care, medical care, and housing helped to contribute to higher prices for the month.

**Consumer Sentiment:** The University of Michigan Consumer Sentiment survey results on Friday were high, but surprisingly below expectations with the preliminary April reading of 97.8 versus 101.4 prior and the current consensus range of 99-102. The tariffs on steel and aluminum were mentioned by almost a third of respondents who had lowered their future expectations of economic conditions. While the reading wasn't terrible, it contrasted with the previous day's Bloomberg Consumer Comfort Index, which displayed high confidence stemming from strong employment conditions and higher paychecks from the tax cuts.

### Last Week's Manager Moves—

HIM #3 —Sold 14% fund to CASH on 4/12; Bought 14% dividend equities on 4/13

HIM #20 —Sold 15% ultra short bond & floating rate bond and bought 17% high yield, 15% high yield on 4/9

## Current Model Allocations

### Low Risk

HIM #2	25% municipal bonds/75% municipal bond mutual fund
HIM #1	15% high yield/85% high-yield Mutual fund
HIM #3	43% convertibles/14% NASDAQ 100/14% dividend equities/ 29% CASH
HIM #20	95% high yield/5% CASH
HIM #19	50% MBS/50% real estate mutual fund
JIM #23	100% intermediate government treasury

### Moderate Risk

HIM #2	100% mid-cap
HIM #9	20% long S&P /80% alternative equity mutual fund
HIM #8	100% trust
HIM #22	100% S&P 500
HIM #10	98% invested, 2% CASH
HIM #15	100% invested
HIM #11	85% (17) stocks/15% CASH
HIM #21	25% CASH/75% real estate mutual fund

# Summary

In utilizing an approach that seeks to limit volatility, it is important to keep perspective of the activity in multiple asset classes. We seek to achieve superior risk-adjusted returns over a full market cycle to a traditional 60% equities / 40% bonds asset allocation. We do this by implementing global mandates of several tactical managers with different risk buckets. For those investors who are unwilling to stomach anything more than minimal downside risk, our goal is to provide a satisfying return over a full market cycle compared to the Barclays Aggregate Bond Index. At Horter Investment Management we realize how confusing the financial markets can be. It is important to keep our clients up to date on what it all means, especially with how it relates to our private wealth managers and their models. We are now in year nine of the most recent bull market, one of

the longest bull markets in U.S. history. At this late stage of the market cycle, it is extremely common for hedged managers to underperform, as they are seeking to limit risk. While none of us know when a market correction will come, even though the movement and volatility sure are starting to act like a correction, our managers have been hired based on our belief that they can accomplish a satisfying return over a full market cycle, -- while limiting risk in comparison to a traditional asset allocation approach. At Horter we continue to monitor all of the markets and how our managers are actively managing their portfolios. We remind you there are opportunities to consider with all of our managers. Hopefully this recent market commentary is helpful and thanks for your continued trust and loyalty.



Chart courtesy of StockCharts.com. Commentary and opinions are those of Hanlon Investment Management.

## Chart of the Week:

The Chart of the Week shows the CBOE Volatility Index (\$VIX) for 2017 thru 2018 YTD. Much of the recent talk is of volatility returning to the markets; with this chart it is easy to see the contrast of the calm markets we experienced in 2017 versus the high volatility of 2018, where it seems every day produces a big move.

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