THE TRUST COMPANY

INVESTMENT & WEALTH MANAGEMENT UPDATE

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2018: FIRST QUARTER IN REVIEW

Michal Emory, CFA, Vice President & Chief Investment Officer, and Eli Sallman, CIMA®, CFP®, Vice President & Investment Officer – Portfolio Manager

The first quarter of 2018 began with strong market gains. The tech-laden Nasdaq led the way by the end of January, posting a monthly increase of almost 7.40%, followed by the large caps of the S&P 500 (5.62%) and Russell 1000 (5.39%).

The employment sector remained strong, with 239,000 new jobs added in January and average hourly earnings climbing 0.3%. Consumer prices rose 0.5% in January, while personal income increased 0.4%. The trade gap continued to widen, which has proven to be a focal point of the current administration. Nevertheless, consumer confidence in the economy increased in January with expectations for continued strengthening in the coming months.

Volatility returned to the stock market in February, with each of the benchmark indexes listed here posting notable losses from the prior month. Nasdaq, while down, fared better than the large caps of both the S&P 500 and the Russell 1000. Investor concerns over rising inflation and interest rates seemed to trigger volatility.

A strong labor report in February revealed a 2.9% increase in average hourly wages over a year earlier, the addition of 313,000 new jobs, and decreasing unemployment insurance claims. These factors combined to prompt investors to conclude that higher labor costs may eat into corporate profits, which might prompt the Fed to raise interest rates at a faster pace.

March was not a good month for the benchmark indexes listed here, except

Market/Index	2017 Close	As of March 29	Month Change	Quarter Change	YTD Change
S&P 500	2673.61	2640.87	-2.69%	-1.22%	-1.22%
DJIA	24719.22	24103.11	-3.70%	-2.49%	-2.49%
NASDAQ	6903.39	7063.44	-2.88%	2.32%	2.32%
Russell 2000	1535.51	1529.43	1.12%	-0.40%	-0.40%
Global Dow	3085.41	3026.70	-3.06%	-1.90%	-1.90%
Fed. Funds	1.25%-1.50%	1.50%-1.75%	25 bps	25 bps	25 bps
10-Year Treasuries	2.41%	2.73%	-13 bps	32 bps	32 bps

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for the small caps of the Russell 2000. Otherwise, each of the indexes closed March in the red, led by the Nasdaq, which was followed by the S&P 500, and the Russell 1000. March brought more concerns for investors with the administration's imposition of tariffs on steel and aluminum imports and the threat of a trade war with China. Much of the month saw retaliatory threats lobbed across the Pacific.

The first quarter saw only the Nasdaq post modest gains. The S&P 500 fell by 1.22% by the end of the quarter, with the Russell 1000 close behind with a decline of 1.14%. The Russell 2000 managed a very modest decline of 0.4%. Prices for 10-year Treasuries fell by the end of the quarter, pushing yields up by 32 basis points.

Eye on the Months Ahead

Moving to the second quarter of the year, the economy is expected to maintain its course of relative strength. However, if news out of Washington continues to concern investors, market volatility is likely to prevail. Our thought is that most of the volatility and recent downward pressure on stocks is self-inflicted. While the economy, in general, and companies, in specific, are growing at a nice clip, investors are being distracted by the constant barrage of noise coming from Washington and the media.

There are plenty of reasons to be excited about the economy as the effects of the new tax bill are working their way through it. Companies should see a boost to their earnings and cash flows not just from a strong economy but from the tax bill.

“Despite the noise from Washington and the increased volatility, we remain positive on the economy and stock market.”

Families should be seeing a boost, as well, as the lower tax rates put more in their pockets.

With the pullback that we have seen, the stock market no longer looks expensive. As of this writing, the Forward P/E for the S&P 500 was 17.1X next year's earnings. While that is not cheap neither is it expensive. We continue to see more value in stocks than most other asset classes which is reflected in our continued overweight position to equities. Growth continues to outperform value and we remain overweight growth for the time being.

We continue to overweight Foreign Developed Equity Markets and Emerging Equity Markets. Valuations overseas remain attractive and U.S. returns in Foreign Markets could continue to benefit from the weakening dollar. We have increased our U.S. Small Cap position to a neutral weighting. Between Small Caps underperforming the past couple of years and Small Caps, generally, being less impacted from a potential trade war, now looks to be a good time to increase our positioning in that asset class.

We continue to be underweight U.S. Fixed Income. As the Fed is raising rates on the short-end, the long-end of the yield remains stubbornly quiet. At the start of December 2015 when the Fed started its current rate hike campaign the 2-year Treasury was at 0.93% and the 30-year Treasury was at 2.97%. As of the close of the first quarter of 2018, the 2-year Treasury was at 2.27% and the 30-year was at, wait for it, 2.97%. There can be, and is, many reasons for this flattening of the yield curve. Since rising rates are bad for bond prices, longer maturity bonds have held up relatively better than shorter bonds thus far in 2018.

Despite the noise from Washington and the increased volatility, we remain positive on the economy and stock market.

Certainly, anything can and will happen but we remain vigilant in monitoring our asset allocation and security selection within that asset allocation.

AVERAGE RARELY HAPPENS BUT GREAT CAN HAPPEN OFTEN

BY MICHAL EMORY, CFA

Over the last 90 years the S&P 500 has averaged 9.37% annually including dividends. That sounds great but it is amazing how rarely the S&P 500 has been close to average. How rare? I am glad you asked.

If you look at the 12-month rolling periods since January 1928 (February 1928-January 1929, March 2017-February 2018, etc.) we have 1,072 such periods. Out of those 1,072 periods, how many times do you think the S&P 500 has had a previous 12-month return of 7.37% and 11.37% or 2% either side of the historical average? Would you be surprised to learn that it has only happened 8.6% of the time? Here are some other surprising numbers around how rarely "average" happens.

- 24.2% vs. 22.1% - Investors are more likely to have a 12-month period of returns over 25% (24.2% of the time) than to have returns within a 10% range (4.37%-14.37%) of average (22.1% of the time).

- 13.9% - The percent of the time investors would have just endured a 12-month period where returns were DOWN more than 10%.

- 44.7% - The percent of the time Investors would have just enjoyed a 12-month period where returns were UP over 15%. That means investors are more than twice as likely to have a 12-month period up over 15% than we are to be within a 10% range of average.

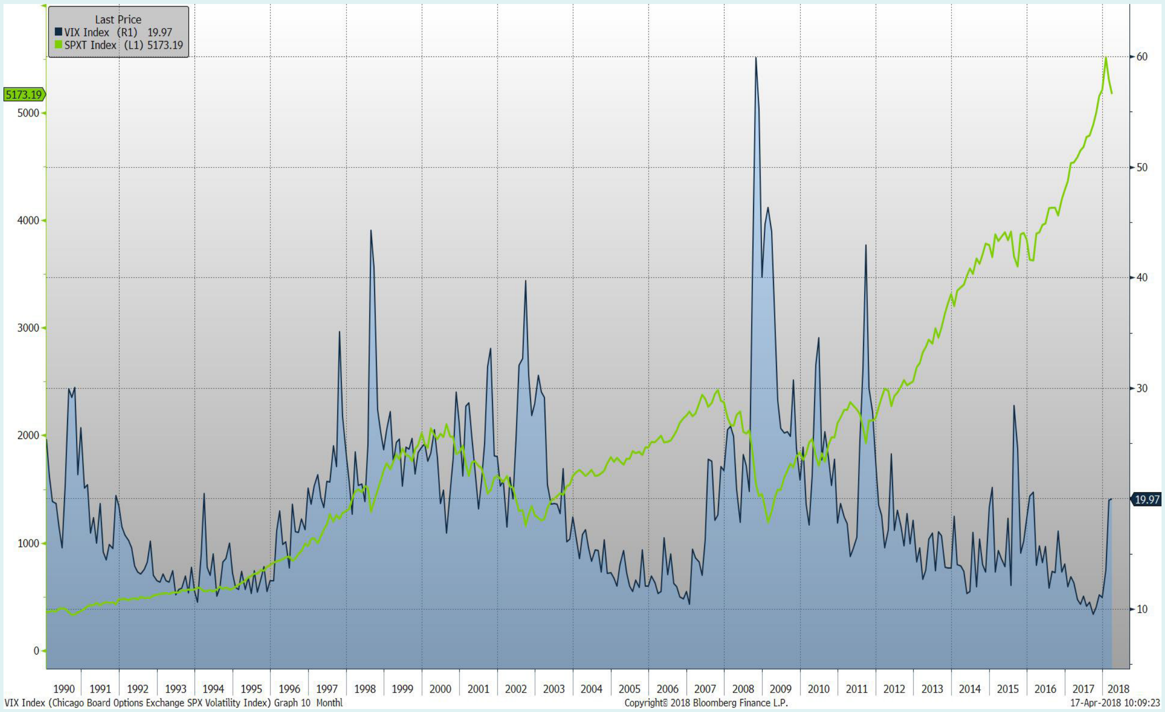
Why do I bring this up? I bring this up because it is easy for investors to forget that volatility is normal for the market—especially after a year like 2017, where investors experienced the least volatile year on record. The last couple of months have reminded investors that the stock market can be volatile at times.

The chart below is of the S&P 500 (includes dividends) versus the VIX Index (a common measure of volatility) from January 1990 to March 2018. As you can see, having big spikes in volatility is not unusual and can happen during good times and bad times; and those spikes can signal a change in market direction or mean "nothing."

One thing that makes this most recent bout of volatility seem more severe is the high price of the stock market, particularly the Dow Jones, which receives the lion's share of the financial press. Let us put the recent big declines in some historical context.

On October 15, 2008 the Dow Jones dropped 733 points, but that was a 7.87% decline. On August 8, 2011 the Dow Jones dropped 634 points, which was a 5.55% decline. In February of this year, the Dow Jones had not one but two drops of more than 1,000 points in a single day.

Those were the largest single day point drops in its history. But those drops were only the 26th and 33rd largest percentage drops in the last 50 years! And if we go back to the beginning of the Dow Jones, they become even less significant from a historical perspective. I am not saying that these drops do not matter or are not scary. But hearing that we had only the 26th largest percentage decline in the last 50 years does not sound as scary as saying the Dow Jones dropped 1,175 points in a day. Despite the two largest point drops in the Dow Jones history, it was only down 1.96% (including dividends) in the first quarter of 2018. And it is up more than 1%



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since the second 1,000+ drop.

Now that we have dissected how "average" stock market returns rarely happen, you may be wondering what I mean that "great" can happen often. I am not talking about great investment returns, though that is The Trust Company's goal. What I am talking about is having a great mentality. Let us discuss what having a great mentality entails.

An investor with a great mentality focuses on the three L's of their financial plan and ignores the surrounding noise. Here are the three L's they focus on:

1) Liquidity – Do you have the liquidity you need for your day-to-day life? Depending on your stage in life that liquidity may come from your job, your investments, or a combination of both.

2) Longevity – Does your financial plan meet your long-term needs and desires? Can you retire when you want? Can you have the type of retirement you want? Are you confident that you will not outlive your money?

3) Legacy – Will you be able to leave a mark the way that you want? Maybe that is paying for a child's or grandchild's college so they graduate with no debt. Maybe that is having the financial freedom to give to causes (with both money and/or time) that stir your heart. Whatever it is, it is our desire to help you reach them.

Another characteristic of a great mentality is realizing that the true risk is not volatility, but in potential failure to reach one of the goals within the three L's. If you look back at the chart, you will see times of high volatility, but with the stock market still trending upwards. During times of high volatility, the best question to ask is, *"does this higher volatility affect my goals to the extent that I need to make a change?"* You will find that most often the answer to that question is "no."

> An Investor with a great mentality focuses on the three L's of their financial plan and ignores the surrounding noise.

By now I hope you see that while average will rarely happen (only 8.6% of the time within a 2% plus/minus of average!), that usually works out in our favor. And that we can be great by adjusting our focus. If you have never taken the time to sit down with your Trust Officer and someone from our Financial Planning team, I encourage you to do so and see how you are doing in meeting your three L's. Eli and I also are happy to talk with you about your goals relative to your investment strategy.

At The Trust Company, we look forward to our continued relationship with you and thank you for allowing us to partner with you in reaching your financial goals.

Grow Green!

fun lunch fundraiser for GMCF

On Friday, April 20, from 11am to 1pm, The Trust Company will donate $5 to GMCF for every lunch purchased from Tasty Traveler, up to $500!

Join us!

Friday, April 20
11am - 1pm
The Trust Company
800 Poyntz Ave.

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