Monthly Scorecard

August 6, 2018

Portfolio Advisory Group – U.S. Equities

Performance (Total return % change)

Index	7/31/18	1 mo.	3 mos.	YTD	1 yr.	2 yrs.
Dow (DJIA)	25,415.19	4.83	5.80	4.07	18.75	44.65
S&P 500	2,816.29	3.72	6.87	6.47	16.23	34.87
NASDAQ	7,671.79	2.19	8.87	11.78	22.17	52.13
Russell 2000	1,670.81	1.74	8.69	9.54	18.73	40.61
Russell 3000	1,670.96	3.32	6.93	6.64	16.38	35.15
S&P 500 Equal Wgt.	4,253.92	3.21	5.67	5.03	13.74	30.03
MSCI AC World	519.82	3.05	2.73	2.90	11.56	31.33
MSCI Europe	132.00	3.38	-0.69	0.35	6.03	28.15
MSCI EAFE	2,006.06	2.48	-0.95	0.02	6.97	26.68
MSCI Asia-Pacific	166.98	0.86	-3.27	-2.34	7.11	29.51
MSCI Emerg. Mkts.	1,087.46	2.28	-5.36	-4.43	4.73	31.21
60/40 Allocation[1]	N/A	2.24	4.37	3.24	9.42	20.4
S&P 500 Sector	**7/31/18**	**1 mo.**	**3 mos.**	**YTD**	**1 yr.**	**2 yrs.**
Consumer Disc.	885.15	1.83	7.61	13.54	23.48	40.65
Consumer Staples	549.60	4.07	7.10	-4.83	-0.59	3.78
Energy	569.16	1.42	5.25	8.32	19.72	19.94
Financials	463.85	5.27	2.32	0.97	13.43	50.79
Health Care	1,028.39	6.61	8.59	8.57	13.31	22.38
Industrials	645.78	7.32	6.90	2.29	12.97	33.64
Information Tech.	1,243.45	2.09	9.23	13.19	28.48	66.35
Materials	374.38	2.96	5.46	-0.21	11.44	27.69
Real Estate	203.92	1.08	7.95	1.90	4.90	2.17
Telecom.	149.60	2.33	2.37	-6.22	-2.46	-9.32
Utilities	268.11	1.86	3.50	2.19	2.83	8.69
FI, FX, & Commod.	**7/31/18**	**1 mo.**	**3 mos.**	**YTD**	**1 yr.**	**2 yrs.**
U.S. Treasuries[2]	2.96%	-0.42	0.50	-1.49	-1.23	-3.75
Invest-Grade Credit[3]	3.99%	0.83	0.78	-2.47	-0.73	0.81
High-Yield Credit[3]	6.31%	1.09	1.47	1.25	2.60	13.83
WTI Crude Oil[4]	$68.76	-7.27	0.28	13.80	37.05	65.29
Dollar Index[4]	$94.55	0.09	2.95	2.64	1.82	-1.02
Gold[4]	$1,224.09	-2.32	-6.94	-6.06	-3.57	-9.39

[1]60% S&P 500 and 40% Bloomberg Barclays U.S. Aggregate; [2]Yield reflects 10-year U.S. Treasury, total returns reflect Bloomberg Barclays U.S. Treasury Index; [3]Yield and total returns reflect that of the respective Bloomberg Barclays Index; [4]Spot prices and price returns.
Source - Bloomberg, RBC Wealth Management

Summer rotation

The unloved sectors from the first half of the year made a sharp course correction in July as three of the four worst-performing groups through the mid-year mark easily outpaced their peers. Industrials led the market, appreciating 7.3% on a total-return basis as transports and capital goods performed well on the back of pricing power gains in excess of rising input costs.. Health Care was the second-best performer, with its 6.6% return driven by resilience from pharma, biotech, and life sciences. Financials took home the third spot at 5.3% as the banks industry gained 7.4%, and Consumer Staples reversed some of the year's losses with its 4.1% gain.

Laggard is a relative term regarding last month's results, as the Real Estate, Energy, and Consumer Discretionary sectors gained 1.1%, 1.4%, and 1.8% at the bottom of the market. Tech was in the middle of the pecking order with its 2.1% gain despite some headline earnings season disappointments (Facebook and Twitter). Speaking of earnings season, the S&P 500 is on track for revenue growth of 8.8% and EPS growth of 23.8%. Energy (22% rev., 110% EPS), Materials (14%, 32%) and Tech (14%, 26%) are delivering the best revenue and organic EPS growth. Financials, Health Care, and Industrials round out the remaining sectors demonstrating organic EPS growth greater than 10%.

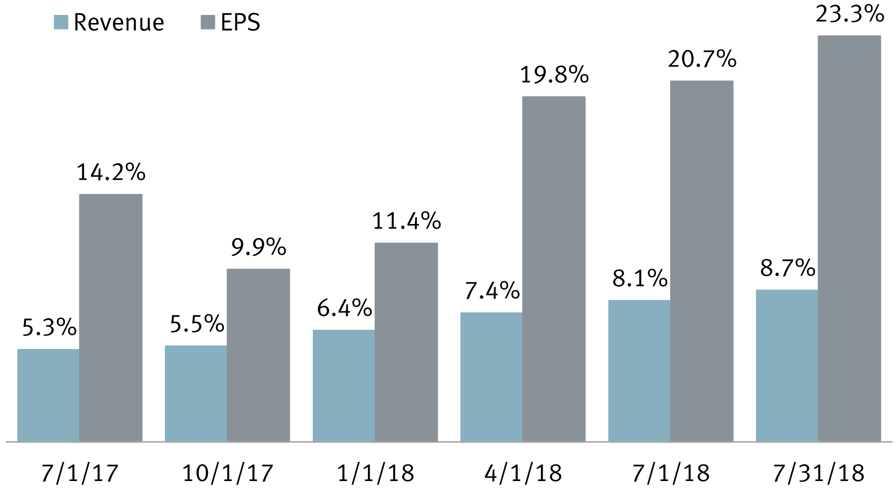
Pivoting to global markets, the U.S. led her international peers, as the Dow Jones and S&P 500 gained 4.8% and 3.7%, respectively, on a total-return basis. Europe was on the U.S. indexes' heels at 3.4% while tariffs and a slowing Chinese economy held the Asia-Pacific region to a muted 0.9% gain. Emerging markets bucked its worst-in-2018 trend to gain 2.3%. The MSCI All Country World Index appreciated 3.1%.

Priced (in USD) as of July 31, 2018, market close (unless otherwise stated).
Click here for authors' information and important disclosures.

Wealth Management

Second-quarter estimates are demonstrating a clear acceleration as better-than-expected growth materializes.

Q2 EPS and revenue growth estimates over time



Source - RBC Wealth Management, Thomson Reuters I/B/E/S

Mythbusters: Inversions don't signal an immediate "game over" for equities

For perspective, a yield curve inversion has preceded the last five recessions and as such is leaned on as an indicator of a potential recession. With all of the uncertainty surrounding the yield curve at the moment and investor concerns of an inversion, we thought it prudent to examine what the actual data tells us about equity market performance in advance of and in the immediate aftermath of an inversion. The data points to continued performance of equities, well after inversion.

First, despite the fear of an inversion, the 6 and 12 months prior to the yield curve inverting actually deliver above-average equity market returns. In fact, during the run-up to the five yield curve inversions since 1978, the S&P 500 has earned 16.3% on average in the 12 months prior to the yield curve inverting. Each instance saw the S&P 500 deliver positive gains with a high water mark of 39.8% in 1998 and a low of 7.5% in 1978.

Second, despite the 6 months immediately after the inversion showing mixed return data, likely attributable to knee-jerk reactions, the average return in the 12 months immediately following the inversion has been a relatively robust 11.1%. Furthermore, in the five occurrences we measured, the S&P 500 delivered positive returns in four of the five periods with a maximum return of 27.5% after the December 1988 inversion. The worst 12-month return post inversion was -3.2%

The five inversions since 1977 have seen major U.S. indexes deliver positive gains, on average, in the 6 and 12 months prior to and immediately following the first inversion, as measured by the spread between the 2Y and 10Y Treasury.

Average returns in the months preceding and immediately after inversion

Inversion	S&P 500	DJIA	NASDAQ	Russell 2000
12 months prior to	16.3%	10.2%	25.6%	22.1%
6 months prior to	11.9%	10.2%	14.2%	10.1%
6 months after	2.0%	1.1%	1.9%	1.6%
12 months after	11.1%	8.9%	14.2%	4.1%

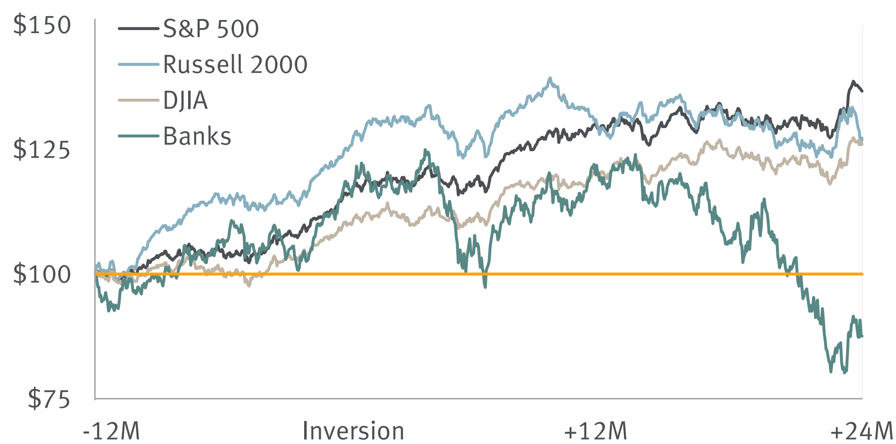
Source - RBC Wealth Management, Bloomberg after the inversion of September 1980. In our view, this represents a positive risk/reward scenario in the marketplace.

That said, all good things must eventually come to an end, and the data shows that the likelihood of positive returns begins to deteriorate approximately 15 months after the inversion itself. There have been instances when positive returns continued for nearly 30 months after inversion, and other periods when the returns worsened much earlier.

For the sake of clarity, our position is that we remain unconcerned about the yield curve's effect on equities until the actual moment of inversion. Then, the clock starts ticking, but we would not shift portfolios immediately. Rather, we'd begin a gradual shift over a period of 6–24 months after an inversion toward a more defensively positioned portfolio aligned with the portfolio's objectives and intended to weather a potential recession that has typically followed a yield curve inversion with a lag of approximately 14 months, per Global Portfolio Advisory Committee research.

U.S. equities hold up better than many expect in the months preceding and following the first instance of inversion in a given cycle.

Average U.S. equity index performance and inversions



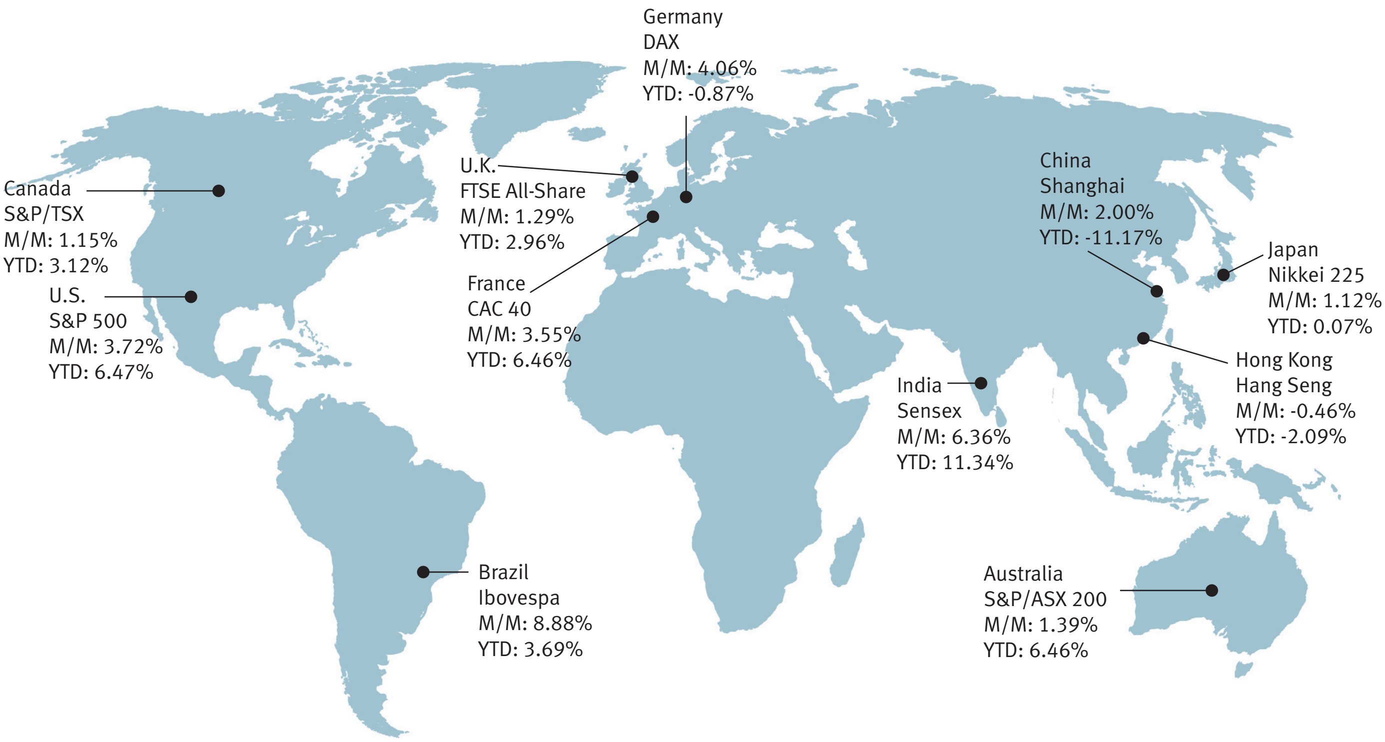
Note: Number of inversions since 1978 for which data is available, by index: S&P 500/Dow Jones, five each; Russell 2000, four; Banks, two.
Source - RBC Wealth Management, Bloomberg

So, where are we now? The only thing we can say for certain is the curve has not inverted and historical returns around inversion have actually been pretty good. While certainly a simple statement, it has profound impacts on equity decisions. For investors, it means that inversion fears should not influence equity decisions at this time. For us, it means we're able to focus on company fundamentals and the earnings seasons. Interestingly, it appears Q2 earnings may disprove the widely held belief that Q1 2018 EPS growth is bound to be this cycle's peak and that growth rates are already on a trajectory of steady decline from here.

In fact, despite some noticeable Tech disappointments, second-quarter earnings have been quite strong. Per our national research correspondent, Q2 2018 GDP growth of 4.1% is manifesting itself in quarterly earnings releases where revenues are expected to grow 8.8% y/y and 89% of companies are beating or meeting consensus revenue forecasts. Furthermore, S&P 500 EPS growth is tracking toward 23%+ with a mid-teens organic growth rate (pre-tax reform). Those numbers don't appear to indicate an economy or equity market teetering on the edge of recession or a bear market. While all good things must eventually come to an end, it does not appear to us that now is the time to make that call for stocks.

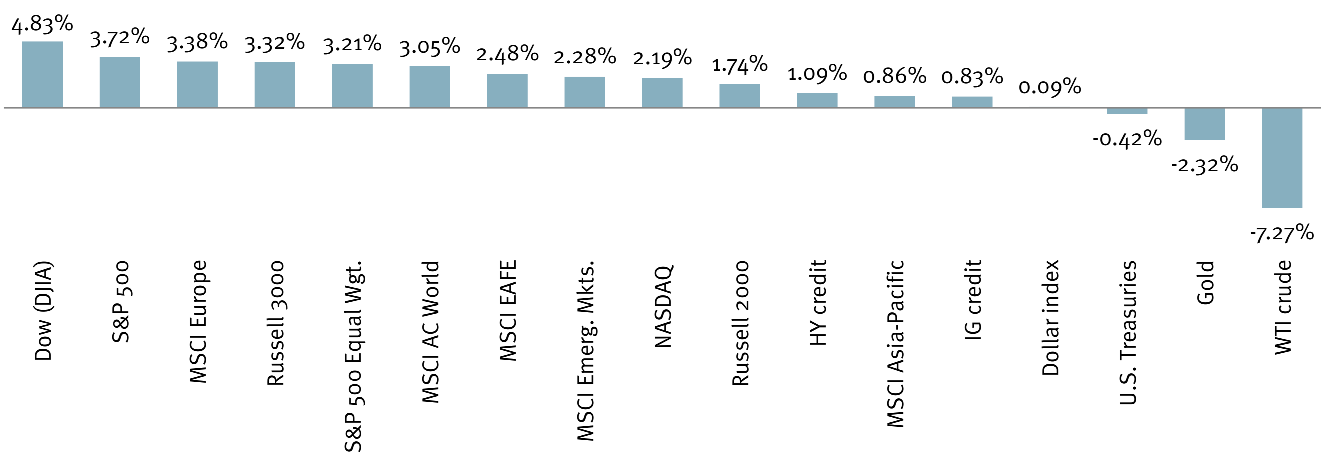
World markets

July month-over-month and year-to-date total return



Source - Bloomberg; priced in local currency

Total monthly returns for select indexes – July 2018



Source - Bloomberg

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