NCM's Global Funds

2018 Year-To-Date Performance and the Outlook for the Second Half of 2018

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We have been bullish throughout 2018, and most major markets are now slightly positive on a year-to-date basis. However, when you look beneath the reasonably calm surface and do some analysis, there are strong undercurrents moving in several directions. What follows is a discussion of some of the market's moving parts so far this year, along with some thoughts on the prospects for the second half of 2018.

2018 Year-To-Date

Currency

First, so far this year, the Canadian dollar has been weak versus most major international currencies which has significantly impacted returns.

Index	Currency	YTD Total Return	Difference
S&P 500	USD	2.65%	-5.06%
S&P 500	CAD	7.71%	

Source: Bloomberg, as of June 30, 2018

Many of our global equity competitors are unhedged, so the falling Canadian dollar has had a significant positive impact on their returns. Our global equity funds are mostly currency hedged and have currency hedged benchmarks, so we have not benefitted from the Canadian dollar weakness year-to-date (YTD). However, in our view, this is a short-term phenomenon.

Small caps have outperformed large caps

Second, in the U.S., small and mid caps have significantly outperformed large caps so far this year.

Index	Currency	YTD Total Return
S&P 500	USD	2.65%
Russell 2000	USD	7.67%
S&P Small Cap 600	USD	9.37%

Source: Bloomberg, as of June 30, 2018

Given the conservative, lower volatility, and dividend focus of our global funds, we haven't received much of a benefit from this small cap outperformance year-to-date. However, we think our portfolio continues to be well positioned for longer term performance.

Only three sectors have outperformed

Third, differences in sector performance have been significant this year. YTD ended June 30th, only 3 of 11 sectors have outperformed the S&P 500 Index.

Sector	YTD Total Return
Consumer Discretionary	11.5%
Technology	10.9%
Energy	6.8%
Health Care	1.8%
Real Estate	0.8%
Utilities	0.3%
Materials	-3.1%
Financials	-4.1%
Industrials	-4.7%
Telecom	-8.4%
Consumer Staples	-8.6%
S&P 500 Index	2.7%

Source: Bloomberg, as of June 30, 2018

2018 has really been a story of the strong performance from the technology, consumer discretionary (Amazon, Netflix, and Trip Advisor are all classified as consumer discretionary stocks), and energy sectors. Every other sector has underperformed so far this year. We continue to find our broadly diversified portfolio strategy attractive and think this is the best way to provide superior, risk-adjusted performance over time.

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Narrow stock leadership

Fourth, stock leadership has also been very narrow, with just 6 stocks responsible for the YTD return of the S&P 500 Index.

Company	Percent of S&P 500 YTD Return	Percent of Nasdaq 100 YTD Return	YTD Percentage Change
Amazon	35	41	49
Netflix	21	21	117
Microsoft	15	15	19
Apple	12	12	13
Alphabet	8	8	11
Facebook	8	8	16

Source: CNBC, July 10, 2018

History shows us that this type of narrow stock or sector performance phenomenon is not likely to last long term.

Looking Ahead

While all of the above has had a meaningful impact on our global equity fund returns so far this year, the above is also history, and the data is only good for the history books. What do we see going forward? We see some encouraging signs that things are changing.

The Canadian dollar weakness appears to have stabilized. The Canadian economy is doing reasonably well, oil prices are firm, the oil price outlook is strong, and the Bank of Canada is hiking rates. We could soon see the Canadian dollar strengthen rather than weaken. If this happens, we will not be negatively impacted as our currency exposure remains largely hedged, unlike many of our competitors.

U.S. small & mid-caps have outperformed, but are now expensive. The outlook for the U.S. small cap asset class has recently been downgraded by three major brokerage firms (Morgan Stanley, Barclays, and Bernstein). Bernstein noted that small caps look more expensive than large caps, even though their growth potential is similar. U.S. small caps now trade at 26 times forward earnings, compared with a multiple of 17 for the S&P 500 Index. Bernstein said large companies “offer cheaper and similarly robust earnings growth, (and) better margin sustainability.” So while U.S. small cap performance has been very strong so far this year, this may not continue in the second half of 2018.

Conservative sectors are starting to outperform. Morgan Stanley recently highlighted that June was the first month in over two years where defensive sector and stock leadership prevailed:

Sector	June 2018
Staples	4.5%
Utilities	4.4%
Real Estate	4.0%
Discretionary	2.9%
Telecom	2.0%
Health Care	0.4%
Energy	0.2%
Materials	-1.2%
Tech	-2.3%
Financials	-3.0%
Industrials	-4.4%
S&P 500 Index	-0.5%

Source: Morgan Stanley

Should this continue, it should benefit our funds given the current composition of our portfolios.

Stock leadership is beginning to broaden. Anecdotally, we can confirm that leadership has started to change, and a number of our long held positions have been rebounding recently.

Overall, we retain our positive outlook for the global equity markets in general, and for our global equity funds in particular. Global GDP growth rates are strong. Global earnings growth is also strong and experiencing positive earnings revisions, instead of the typical negative earnings revisions. Furthermore, valuations continue to be at reasonable levels in our view.

And finally, in addition to our positive outlook, don’t forget: **We own numerous businesses on your behalf that have a history of compounding your money.** We fully expect them to continue to compound your money over time.

For more information on the NCM Global Funds, contact your local NCM Sales Representative or visit Norrep.com.