

Cherry Bekaert Wealth Management

# Market Update: The Quarter in Review

Useful Information for Your Business & Financial Success

## 2018 Summary

In the US, small cap stocks underperformed large cap stocks, and value stocks underperformed growth stocks using Russell indices. The Russell 2000 Index declined -11.0% for the year vs. -4.8% for the Russell 1000. The Russell 3000 Value Index returned -8.6% in 2018 vs. -2.1% for the Russell 3000 Growth Index. The variation in returns between these indices is within historical norms. Since 1979, there has been an annual return difference of 6% or greater 60% of the time.

In developed ex US markets, small cap stocks underperformed large cap stocks and value stocks underperformed growth stocks. Despite underperformance in 2018, over both five- and 10-year periods, small cap stocks, as measured by the MSCI World ex USA Small Cap Index, have outperformed large caps, as measured by the MSCI World ex USA Index. Growth stocks, as measured by MSCI World ex USA Growth Index (IMI), returned -13.8%, outperforming value stocks, which returned -15.6% in 2018, as measured using the MSCI World ex USA Value Index (IMI).

In emerging markets, small cap stocks, as measured by the MSCI Emerging Markets Small Cap Index, underperformed large cap stocks, as measured by the MSCI Emerging Markets Index. However, over the past 10 years, small caps returned an annualized 9.9%, outperforming large caps, which returned 8.0%.

Value stocks returned -11.5% as measured by the MSCI Emerging Markets Value Index (IMI), outperforming

growth stocks, which returned -18.4% using the MSCI Emerging Markets Growth Index (IMI). This was the sixth largest outperformance of value over growth in emerging markets since 1999.

The complementary behavior of size (small vs. large) and relative price (value vs. growth) in emerging markets in 2018 is a good example of the benefits of diversification. While small cap stocks underperformed, diversified portfolios were buoyed by outperformance among value stocks. This integration can increase the reliability of outperformance and mitigate the impact of an individual asset group's underperformance.

Despite recent years' headwinds, the size, value, and profitability premiums remain persistent over the long term and around the globe. It is well documented that stocks with higher expected return potential, such as small cap and value stocks, do not realize outperformance every year. Maintaining discipline to these parts of the market is the key to effectively pursuing the long-term returns associated with size, value, and profitability.

Over the full year, the return on the US fixed income market was relatively flat; the Bloomberg Barclays US Aggregate Bond Index returned 0.0%. Non-US fixed income markets posted positive returns in 2018, contributing to the return of the Bloomberg Barclays Global Aggregate Bond Index (hedged to USD) at 1.8%.

*Source: MSCI. Past Performance is not a guarantee of future results. All non-US equity market returns are in USD, net dividends, unless otherwise noted. Index is not available for direct investment. Performance does not reflect the expenses associated with management of an actual portfolio.*

*Past performance is no guarantee of future results. This information is provided for educational purposes only and should not be considered investment advice or a solicitation to buy or sell securities. Please see page 4 for additional footnotes and disclosures.*

# 2018 Summary (Continued)

Yield curves were upwardly sloped in many developed markets for the year, indicating positive expected term premiums. Realized term premiums were negative in the US as long-term maturities underperformed their shorter-term counterparts and positive in developed markets outside the US. For example, the FTSE Non-USD World Government Bond Index 10+ (hedged to USD) returned 4.4% for the year vs. 3.0% for the 1-10 Index.

Credit spreads, which are the difference between yields on lower quality and higher quality fixed income securities, widened during the year, as measured by the Bloomberg Barclays Global Aggregate Corporate Option Adjusted Spread. Realized credit premiums were negative both globally and in the US, as lower-quality investment-grade corporates underperformed their higher-quality investment-grade counterparts. Treasuries were the best performing sector globally, returning 2.8%, while corporate bonds returned -1.0%, as reflected in the

Bloomberg Barclays Global Aggregate Bond Index (hedged to USD).

In the US, the yield curve flattened as interest rates increased more on the short end of the yield curve relative to the long end. The yield on the 3-month US Treasury bill increased 1.06% to end the year at 2.45%. The yield on the 2-year US Treasury note increased 0.59% to 2.48%. The yield on the 10-year US Treasury note increased 0.29% during the year to end at 2.69%. The yield on the 30-year US Treasury bond increased 0.28% to end the year at 3.02%.

2018 included numerous examples of the difficulty of predicting the performance of markets, the importance of diversification, and the need to maintain discipline if investors want to effectively pursue the long-term returns the capital markets offer.

## Exhibit 1: World Stock Market Performance

MSCI All Country World Index (IMI) with selected headlines from 2018



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# Impact of Diversification

## 2018 Index Returns

These portfolios illustrate the performance of different global stock/bond mixes and highlight the benefits of diversification. Mixes with larger allocations to stocks are considered riskier but have higher expected returns over time.

### Ranked Returns for 2018 (%)

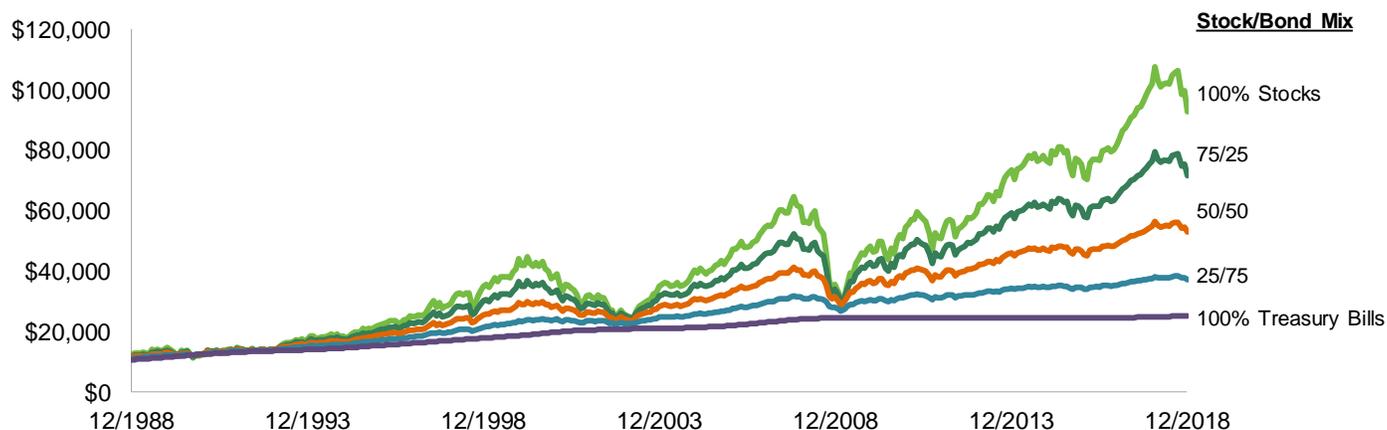


### Period Returns (%)

\* Annualized

Asset Class	1 Year	3 Years*	5 Years*	10 Years*	10-Year STDEV <sup>1</sup>
100% Treasury Bills	1.81	0.93	0.57	0.32	0.16
25/75	-0.82	2.57	1.73	2.88	3.65
50/50	-3.49	4.16	2.82	5.36	7.32
75/25	-6.19	5.70	3.86	7.75	10.98
100% Stocks	-8.93	7.18	4.82	10.05	14.65

## Growth of Wealth: The Relationship between Risk and Return

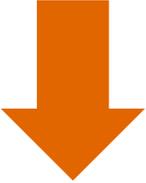
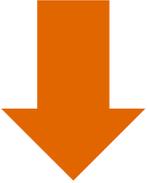


1. STDEV (standard deviation) is a measure of the variation or dispersion of a set of data points. Standard deviations are often used to quantify the historical return volatility of a security or portfolio.

Diversification does not eliminate the risk of market loss. **Past performance is not a guarantee of future results. Indices are not available for direct investment. Index performance does not reflect expenses associated with the management of an actual portfolio.** Asset allocations and the hypothetical index portfolio returns are for illustrative purposes only and do not represent actual performance. Global Stocks represented by MSCI All Country World Index (gross div.) and Treasury Bills represented by US One-Month Treasury Bills. Globally diversified allocations rebalanced monthly, no withdrawals. Data © MSCI 2018, all rights reserved. Treasury bills © Stocks, Bonds, Bills, and Inflation Yearbook™, Ibbotson Associates, Chicago (annually updated work by Roger G. Ibbotson and Rex A. Sinquefeld).

# Market Summary

## Index Returns

	US Stock Market	International Developed Stocks	Emerging Markets Stocks	Global Real Estate	US Bond Market	Global Bond Market ex US
<b>2018</b>	<b>STOCKS</b>				<b>BONDS</b>	
	<b>-5.24%</b>	<b>-14.09%</b>	<b>-14.58%</b>	<b>-5.90%</b>	<b>0.01%</b>	<b>3.17%</b>
						
<b>Since Jan. 2001</b>						
Avg. Annual Return	7.6%	5.8%	13.1%	10.1%	4.5%	4.4%
Best Year	33.6% <b>2013</b>	39.4% <b>2003</b>	78.5% <b>2009</b>	37.4% <b>2006</b>	10.3% <b>2002</b>	8.8% <b>2014</b>
Worst Year	-37.3% <b>2008</b>	-43.6% <b>2008</b>	-53.3% <b>2008</b>	-45.7% <b>2008</b>	-2.0% <b>2013</b>	1.2% <b>2013</b>

Market segment (index representation) as follows: US Stock Market (Russell 3000 Index), International Developed Stocks (MSCI World ex USA Index [net div.]), Emerging Markets (MSCI Emerging Markets Index [net div.]), Global Real Estate (S&P Global REIT Index [net div.]), US Bond Market (Bloomberg Barclays US Aggregate Bond Index), and Global Bond ex US Market (FTSE WGBI ex USA 1-30 Years [hedged to USD]). S&P data copyright 2018 S&P Dow Jones Indices LLC, a division of S&P Global. All rights reserved. Frank Russell Company is the source and owner of the trademarks, service marks, and copyrights related to the Russell Indexes. MSCI data © MSCI 2018, all rights reserved. Bloomberg Barclays data provided by Bloomberg. FTSE fixed income © 2018 FTSE Fixed Income LLC, all rights reserved. Indices are not available for direct investment. Index performance does not reflect the expenses associated with the management of an actual portfolio.

Past performance is not a guarantee of future results. This information is provided for educational purposes only and should not be considered investment advice or a solicitation to buy or sell securities. There is no guarantee an investing strategy will be successful. Diversification does not eliminate the risk of market loss.

Investing risks include loss of principal and fluctuating value. Small cap securities are subject to greater volatility than those in other asset categories. International investing involves special risks such as currency fluctuation and political instability. Investing in emerging markets may accentuate these risks. Sector-specific investments can also increase these risks.

Fixed income securities are subject to increased loss of principal during periods of rising interest rates. Fixed income investments are subject to various other risks, including changes in credit quality, liquidity, prepayments, and other factors. REIT risks include changes in real estate values and property taxes, interest rates, cash flow of underlying real estate assets, supply and demand, and the management skill and creditworthiness of the issuer.

Dimensional Fund Advisors LP is an investment advisor registered with the Securities and Exchange Commission.

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