Global stock markets rose on the news that Emmanuel Macron and Marine Le Pen finished first and second in the voting of France’s first round of presidential elections. Equity markets had declined ahead of the election, as some investors grew concerned that the communist candidate, Jean-Luc Melenchon, could sneak into the top two slots, as some polls suggested. Investors feared that Mr. Melenchon could beat Mr. Macron in round two of voting (In France, if no candidate receives more than 50% of the vote, a second round is held between the top two vote getters). With Mr. Macron and Ms. Le Pen set for a second-round showdown in early May, markets spiked, anticipating a Macron victory. Mr. Macron is viewed as the most market friendly, as Ms. Le Pen has threatened to pull France out of the Eurozone. In addition, first quarter earnings growth for S&P 500 companies, while still early, continued the strong rebound of the two prior quarters. In fixed income, riskier parts of the markets rose the most, while Treasuries received a safe-haven bid, in reaction to the uncertainty leading up to the French election, lack of passage of significant legislation by Congress and the Trump Administration and continued skepticism over the actual strength of the US economy. Commodity markets broadly declined, driven lower by a sharp decline in crude oil.

Global investors turned their attention to the French election, viewed by many as the most important barometer of rising populism in Europe. Leading that effort is Ms. Le Pen, who heads the National Front party. Ms. Le Pen has vowed to remove France from the Eurozone, an event that would effectively end the European project. Mr. Macron, on the other hand, is a centrist politician, who has stated that he believes France should remain part of the Eurozone. Meanwhile, the communist party candidate received a late rise in the polls and some believed he could beat Mr. Macron should he make it into the second round, which would have increased geopolitical risk. After the ballots were counted, however, Mr. Macron and Ms. Le Pen finished as the top two vote getters, a market-friendly outcome as it is widely expected that Mr. Macron will easily defeat Ms. Le Pen in the second round.

In response to the election result in France, global equity markets surged, erasing what had been up to that point monthly declines. With Macron leading in the
second round polls, geopolitical risks from Europe have subsided, providing some relief to equity markets as the region has been dealing with higher levels of uncertainty for much of the post-crisis period. This can perhaps best be seen in the reaction to yields from safe-haven countries like Germany and Switzerland, which rose dramatically. US markets were led by small cap stocks, up over 1.0% for the month. International markets performed better than their US counterparts, with developed international markets up over 2.5% and emerging market equities up more than 2.0%.

Equity markets in the US also reacted positively to the improved earnings growth numbers being reported thus far for the first quarter of 2017. As of April 27, approximately 48% of S&P 500 companies have reported quarterly earnings, with growth ticking in at over 11% for earnings and nearly 6% for revenues. This acceleration in earnings growth continues a trend seen over the prior two quarters, a reversal of the earnings declines experienced for much of 2014, 2015 and early 2016. The Energy sector has exhibited the largest increase in earnings growth, up over 64%, a consequence of the rise in oil prices over the last 12 months. Other sectors that were also showing strong growth rates, include Technology and Financials, two sectors that should benefit from a lower regulatory burden and lower repatriation taxes proposed by the Trump administration. The Consumer Discretionary sector, on the other hand, posted a decline in earnings. This may be the beginning of a worrisome sign that suggests consumers no longer have the same appetite for non-essential goods. Looking deeper into the numbers, however, shows that the decline in earnings was concentrated in the automobile sector, a development that should come as no surprise given that auto sales exceeded their prior peak recently and have likely topped out. Should the quarter finish with earnings growth at or above the 11% noted above, it will be the first quarter since 2011 that the S&P 500 has registered double-digit earnings growth. Even when the rebound in Energy sector earnings is taken out, aggregate growth from the remaining sectors currently stands at an impressive 8.3%.

Fixed income markets posted positive returns in April, led by the riskier portions of the bond market. The election in France helped to push non-US bond markets higher, again a sign that the geopolitical risk overshadowing international markets had diminished. Yields for safe-haven bonds like those in Germany and Switzerland rose sharply in the aftermath of the election. Riskier high yield bonds in the US outperformed higher quality corporates and Treasuries for the month, as spreads tightened as the month came to a close, yet another sign that risk appetite was increasing. The Treasury market, however, remained skeptical of the market picture. While economic data since the US election has generally been running ahead of expectations, it has largely been the “soft,” or sentiment survey data, while the “hard” data has been less impressive. This skepticism was confirmed with the first quarter GDP estimate released by the Commerce Department. Real GDP grew at an anemic 0.7%, coming in at the bottom end of expectations from economist and market surveys. Further doubt in the bond market was driven by the absence of significant legislative accomplishment by the Trump administration and a Republican-controlled Congress. The Treasury yield curve flattened during the month, as yields on longer dated bonds fell more than yields on shorter maturity bonds, a sign of concern from bond investors.

Broad commodities slumped during the month, driven lower by the energy component of the market. US crude inventory levels, which declined slightly during April, have otherwise been on an uptrend in recent months, as oil prices have hovered around the $50 per barrel level, incentivizing US companies to restart drilling. The market has largely discounted the production cuts implemented by the Organization of Petroleum Exporting Countries (“OPEC”), so much so that OPEC has been rumored to extend its cuts to ensure the global market continues to work toward equilibrium. Gasoline inventories in the US rose during the month, adding downward pressure on prices for that fuel. Metals markets likewise largely declined, with several industrial metals leading the way down. Copper, zinc, nickel and lead all experienced declines of at least 3% during the month, as signs emerged that Chinese demand for these metals had subsided somewhat recently and supply from Chinese producers had inched up. Gold rose by over 1% for the month, holding on to gains from the uncertainty of the French election. Most agricultural commodities fell, with oversupply remaining the primary driver of the declines.

Should you have any questions about this update or your portfolio, please do not hesitate to contact your Portfolio Manager or Trust Officer.
Unless otherwise noted, performance and return data sourced from Bloomberg, LP as of April 28, 2017.

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This is only an opinion and not a prediction or promise of events to come.

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