SELECTOR® Money Management
2016 Third Quarter Review

The Third Quarter Was The Best Quarter Of The Year For Domestic Equities

The bulk of the positive action was a follow-through from the rebound after the 'Brexit vote' correction. The result was a very positive July followed by a quietly positive August. That momentum was enough to take most domestic equity indexes to relatively muted all-time highs. The only correction of the quarter took place in September, of course, but it was limited to just a few days. The S&P 500 Index pulled back a mere 3.37%, followed by another quiet rebound. September has the reputation of being the most difficult month of the year, but the S&P 500 Index closed out the month with a decline of only 2 points, or -0.09%. Through the first three quarters, the S&P 500 Index finished with a gain of +7.84%. The big winners of the third quarter were small cap and mid cap equities. The S&P SmallCap 600 Index gained +7.20% in the third quarter while the S&P MidCap 400 Index rose +4.14%. For the year these two indexes are now up +13.88% and 12.40%, respectively.

Sector Rotation Was Very Evident In The Third Quarter

The biggest story of the third quarter for domestic equities was the major shift in leadership amoung the major equity sectors. Through the first six month, defensive sectors were at the front of the pack with the utilities and the real estate sectors establishing commanding leads. In the third quarter these two sectors actually registered net declines, while still holding positive numbers YTD. The Dow Jones U.S. Utilities Index was the worst performing sector index of the third quarter, down -5.87%. The Dow Jones U.S. Real Estate Index fell -1.15% in the quarter. The best performing sector of the third quarter was technology, with the Dow Jones U.S. Technology Index up +13.58%. Another standout sector was biotechnology, and the NASDAQ Biotechnology Index gained +12.50% in the quarter. This is a major shift in emphasis from defensive sectors to aggressive sectors. Coupled with the substantial gains in small cap and mid cap equities during the domestic equity market leadership is significantly broader and stronger.

On The International Front, Emerging Equities Continued Their Strong Performance

Both Asian and Latin emerging markets enjoyed very strong third quarters, contributing to the MSCI Emerging Markets Index gains of +9.03% for the quarter and +16.02% YTD. European equities markets also posted gains for the third quarter following the Brexit vote surprise. With Germany once again in the lead, the S&P Europe rose +5.23% in the quarter and crossing over into positive territory YTD with a gain of +0.04%. While developed international equity markets are still trailing their domestic cousins across the board, their technical conditions have improved dramatically. Interestingly, the strongest international sectors, both developed and emerging, are the financials.

Domestic High Yield Bonds Have Been Big Beneficiaries Of The Small/Mid Cap Equity Surge

The largest gains in domestic bond markets during the third quarter were seen in high yield bonds, as reflected by the Markit IBoxx USD Liquid High Yield Index rise of +5.09% in the quarter. This index is also the top-performer YTD with a gain of +13.76%. International and emerging market high yield bonds also enjoyed a very strong quarter. This is a general reflection of the 'risk-on' rotation that took place in equities during the third quarter. Every bond market index that we monitor is positive on the year, including investment grade, treasury, TIPs, and municipals.

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