Unitarian Universalist Common Endowment Fund

Monthly Market Commentary for May 2015

		Last Month	YTD	Last Year	Last 3 Years	Last 5 Years
Domestic Stocks	S&P 500	1.3%	3.2	11.8	19.7	16.5
	S&P Mid Cap 400	1.8	5.6	12.3	19.9	16.6
	Russell 2000	2.36	4.0	11.3	19.5	15.0
Domestic Bonds	Barclays Aggregate	-0.2%	1.0	3.0	2.2	3.9
	High Yield Bonds	0.3%	4.1	2.0	8.1	9.2
	91-Day T-Bills	0.0%	0.0	0.0	0.1	0.1
Non-US Stocks	MSCI EAFE (Net)	-0.5%	8.6	-0.5	15.6	10.0
	MSCI Emerg Mkts (Net)	-4.0%	5.7	0.0	6.0	4.1
Global Bonds	Citi World Gov't	-2.3%	-3.8	-8.0	-2.3	1.5

US equities bounced around in May with trading marked by low volume and changing sentiment as investors grappled with the potential impact of mixed economic data on the Federal Reserve's timing of a rate increase. Smaller-cap issues fared better than their large-cap counterparts due, in part, to a sustained strong dollar prompting trade headwinds for some larger companies. To this end, the Russell 2000 returned 2.3% while the S&P 500 gained 1.3%. International developed and emerging market equities gave back some of April's gains. That said, they remain two of 2015's best performing asset classes with the MSCI EAFE Index up 8.6% and the MSCI EM returning 5.7% year to date. Emerging market equities were hit especially hard in May—losing 4.0%—as investors grew wary of higher valuations and weak economic data coupled with extreme equity market fluctuations in China.

Fixed income markets were affected by a sharp rise in German Bund yields as encouraging economic data gave investors pause on the prospect of an albeit small but earlier-than-expected recovery; the yield on the 10-year Bund rose to 0.72% mid-month from 0.37% at the beginning of May. Undeterred, the European Central Bank indicated it would stay the course with its quantitative easing program, even announcing it would frontload bond purchases in the summer. As a result, developed yields across Europe began to re-compress by month end. Part of the reversal may also be attributed to concerns over negotiations over Greek debt, which triggered a modest flight to quality in the second half of the month, moderating a rise in US yields as the 10-year Treasury ended May at 2.12%, up basis points. These oscillations fueled losses across most fixed income indices with the Barclays Aggregate declining 0.2% and the Citigroup WGBI losing 2.3%. Emerging market bonds fared similarly as broad indices were dragged down by countries such as Brazil and South Africa where balance of payments issues still loom as the prospect of a US rate hike draws closer.

Looking forward, we expect markets to remain heavily influenced by the pervasive policy decisions of central banks, particularly in the US and Europe. In the US, speculative trading patterns appear to have emerged, ebbing and flowing with each new piece of economic data. The resulting effect has been a slow appreciation of equity prices, but also a sustained increase in volatility along the Treasury curve. We believe the potential for a rate hike, paired with a steep Treasury curve and generally low yields, is a relatively unattractive environment for holders of traditional US fixed income assets or core bonds. As such, we recommend investors embrace an unconstrained approach to US fixed income, which can be accessed through a tactically-oriented absolute-return or multi-sector strategy. Recognizing that eschewing duration altogether may leave investors unhedged to a number of unfavorable economic scenarios, we believe investors should consider a 'barbell' approach with a small allocation to long-duration Treasuries or a blended government/credit strategy. In Europe, we continue to view the ECB's accommodative action as favorable to potential earnings growth. As a result, we recommend investors consider an equal or overweight allocation to international developed stocks relative to US equities. Despite the recent strengthening of the US dollar, we believe holding foreign developed currencies carries additional risk over the long term with no discernable return premium. Thus, we also recommend implementing such an allocation with a partial currency hedge.

[Commentary courtesy of New England Pension Consultants (NEPC). UUCEF has a consultancy agreement with NEPC to assist in the oversight of investment managers and provide other advisory services to the UUCEF Investment Committee. NEPC® is an independent, full service investment consulting firm, providing asset allocation, manager search, performance evaluation and investment policy services to middle and upper market institutional investment programs.]