DURAND
CAPITAL PARTNERS

Quarterly Review & Outlook

1Q Review

The first quarter of 2019 produced strong returns for the U.S. equity market. The S&P 500 index was up 13.6% on a total return basis. This was almost the exact mirror image of the final quarter of 2018, when the index was down 13.5% on a total return basis. (Though this quarter's positive numbers were almost, on an absolute basis, exactly the same as the previous quarter's negative ones, that's not enough to make up for those losses: After a 20% drop, a security or benchmark requires a 25% return to get back to its starting point.). This is why mitigating losses is so crucial.

Stocks that are classified as growth outperformed their value and core counterparts once again. Stocks classified as mid-cap growth returned more than 21% for the quarter, while the weakest segment of the style box, large-cap value, produced returns of 10.3%.

Performance trends could also be observed among different market sectors. While all 11 market sectors produced positive returns for the quarter, the strongest performers were technology stocks (up 19.6%), industrials (up 17.7%), and communication services (up 16.7%). The healthcare sector had the weakest relative performance for the quarter yet was still up 7.9% on a total return basis.

DCP US All-Cap Review

Against this backdrop we would expect the US All-Cap portfolio to be in participate mode, and that is exactly what we saw. The strategy surged 11.98% for the quarter, slightly lagging the 13.65% gain for the S&P 500.

The underperformance was driven by our roughly 10% weighting to cash, as well as our underweight to Real Estate and Energy which turned in the some of the performance sector wise of the quarter. Positive contributions were made through our overweight to the Technology Sector, which turned in the best performance of the quarter.

DCP International All-Cap Review

Our International portfolio once again outperformed the broader MSCI EAFE with a 11.49% return vs. 10.13% for the benchmark. The outperformance was driven primarily by our overweight to the Industrial and Energy Sectors. The strategy was hurt by an underweight to the Technology sector.

2019 Outlook

As we continue to march ahead into year 10 of this historic run from the lows seen in 2009, I thought it might be helpful to go through several of the market sectors and give our thoughts for these areas over the coming quarters:

Energy

With oil prices once again above our midcycle price of $55 per barrel, we see less value in oil-related stocks than we did at the beginning of the year. To be sure, we still see value in the energy space, but less so than at the beginning of the year. For oil globally, we expect the tug of war between OPEC and U.S. shale producers to continue. Amid the drop in crude prices that started in 2018, OPEC and its partners have rededicated to constraining supply after a brief period of turning the spigots back on in mid-2018. Additionally, low supply from Iran, because of sanctions, and Venezuela, because of political unrest, has further tightened global markets. Amid the backdrop of cuts from OPEC, U.S. shale producers have dialed back somewhat as well due to falling oil prices, but rig counts in the major U.S. shale basins have not declined dramatically, and many U.S. producers say they expect continued growth in 2019. We think the most recent round of OPEC cuts only nudges the door open for shale producers to increase production and keep taking share from OPEC and its partners.

Financials

Currently, we see the most value in the banking industry. The median bank that we cover has approximately 15% upside to its intrinsic value estimate, and we believe that European and Asia-Pacific banks are trading at more attractive valuations than North and South American banks. Compared with the previous quarter, we no longer see favorable risk- adjusted returns for asset managers. There's 10% upside to the median price/intrinsic value estimate of our asset management coverage after our coverage appreciated 11% in the previous three months. Expectations for rising interest rates have dramatically moderated. CME Group's FedWatch tool suggests around a 70% probability that the target U.S. federal-funds rate won't change in 2019 and a 30% probability that there will be a rate cut. This compares with an over 50% probability of a target rate higher than its current range of 2.25% to 2.5% as recently as November 2018.

Consumer Discretionary

We see opportunities for long-term investors to own structurally advantaged companies that have been held back because of cyclical pressures. For instance, companies with competitive advantages exposed to e-commerce or the Chinese consumer remain well-positioned for long-term growth. In the U.S., we expect e-commerce growth to remain robust in the years ahead, with online retail growing at a double-digit clip through 2022 versus less than 4% for the brick-and-mortar channel. Also, economic downturns have historically offered e-commerce marketplaces opportunities to lock in new buyers and sellers, which then engage in other higher-margin products and services as conditions stabilize. As for China, although we expect GDP growth to slow to 3.8% in real terms on average over the next five years from 6.8% during the previous five years, we believe that its mix is shifting to consumption, as we project household consumption growth to average 6.2% during the next five years, which supports operators exposed to its consumer. Further, the Chinese consumer remains relatively healthy, backed by wage growth, access to consumer credit, and potential government stimulus.

Hopefully, these sector overviews helped to provide additional insight into our thinking and processes, especially as it relates to where we are looking at opportunities currently. The team and I at Durand Capital truly appreciate your loyalty and trust. As always, if you have any questions in regard to anything above, or just questions about the strategy in general, please do not hesitate to get in contact.

Sincerely,

Jim Tassoni
President/CIO
Durand Capital Partners