The stock market attempted to stabilize during March following the sharp February sell-off, but volatility remained high. Technology led stocks to rebound early in March as the NASDAQ-100 reached a new all-time high. The markets then turned sharply negative in the last half of the month with most major stock market averages testing their February lows. Interest rates stabilized during March and the 10-year U.S. Treasury Note ended March below 2.80%.

The portfolio entered March with moderate exposure to the stock market in both the large-cap and technology sectors. We eliminated the technology allocation during the month, then increased our allocation to large-cap stocks at the end of the month as the market tested the February lows and our models strengthened.

If the market were to successfully test the February lows, along with increased investor pessimism, stable interest rates and improved momentum, we would likely further increase market exposure. However, if sentiment were to swing back to more optimistic, interest rates were to rise and momentum were to deteriorate, we would likely take a more defensive posture.

Our assessment of the four pillars of our investment process is as follows:

1. **Valuation:** Valuation remains elevated. The median price/earnings (P/E) ratio on the S&P 500 Index reached 26.8 in January 2018—its highest level in almost 15 years. The February market sell-off improved equity valuations modestly and the median P/E ratio declined to 24.8.

2. **Monetary factors and credit conditions:** The 10-year U.S. Treasury Note rose toward the 3.00% level in February—its highest level since spring 2014—which caused our rate of change models to become negative. However, as interest rates declined in March, the 10-year U.S. Treasury Note stabilized and ended the month below 2.80%. A stabilization of interest rates at current levels would be a positive development for equities and would improve our rate of change indicators.

3. **Sentiment:** Investor sentiment got far more bullish—negative from a contrary point of view—in January, but quickly reversed in February. In March, as market performance dropped toward the February lows, investor sentiment reached its most bearish level in over a year, which is positive from a contrary point of view. This shift was a positive development and factored into our decision to increase market exposure in late March.

4. **Momentum:** The February market sell-off and subsequent March test of those lows created an oversold condition. The percentage of stocks above their 10- and 30-week moving averages declined sharply in March. We took advantage of this oversold situation by increasing exposure to large-cap stocks. Historically, one of the signs of a more important top has been a divergence between the major market averages and the broad list of stocks. If fewer and fewer stocks are able to climb above their 10- and 30-week moving averages as the major indices rallied, it would be a negative development in our models.

Disclosure next page