Q1

FIRST REPUBLIC
PRIVATE WEALTH MANAGEMENT

QUARTERLY UPDATE

First Quarter / 2019

HIGHLIGHTS

- **Optimism that the U.S. and China are getting closer to a trade agreement helped U.S. equities finish their best first quarter in nearly a decade**
- **The Fed adopted a dovish tilt signaling no further interest hikes in 2019 after its preferred inflation gauge dipped below 2%**
- **Despite ongoing geopolitical challenges, international equities rallied, buoyed by hopes that a trade compromise deal is near**

OVERVIEW

Financial markets were off to a strong start during the first quarter of 2019, as reports of substantial progress made during the latest round of trade talks between the U.S. and China lifted investor sentiment. Despite the trade spat still ongoing, the bellicose tensions that ignited a tit-for-tat tariff war last year eased, following several rounds of negotiations.

Meanwhile, economic indicators showed that the U.S. economy continued to grow during the first months of 2019, albeit at a slower pace. As a response to a string of softer economic data and tepid inflation readings, the Federal Reserve (the Fed) signaled that they were unlikely to raise interest rates for the remainder of this year. The Fed's pause to further monetary tightening gave markets a respite, overshadowing concerns of dampening global growth stemming from Europe and China. The Fed's dovish outlook also pressured U.S. Treasury yields sharply lower, sending the 10-year Treasury yield below the shorter-dated 3-month Treasury bill yield.

When long-term bond yields reach levels below short-term bills, a so-called "yield curve inversion" occurs. Given that an inverted yield curve has historically served as a formidable recession predictor, investors grew concerned about a looming economic downturn, moving into safer assets like corporate and government bonds. However, the Fed's "patient" outlook also boosted optimism that the 10-year bull market in U.S. equities could still have room to continue, helping domestic indices recoup nearly all of the losses suffered late last year. International equities rallied in tandem, as clouds around trade cleared and tensions abated.

U.S. EQUITIES: A SLOWIN' BUT GROWIN' ECONOMY AND A "PATIENT" FED BOOST SENTIMENT

Despite the encouraging trade news, U.S. equities remained sensitive to mixed economic data. While the probability of a recession in the near-term remains low, investors have had to grapple with volatility in the financial markets, a partial government shutdown, and a downshift in hiring signals from February's jobs report. Consumer spending — a key engine of U.S. economic growth — barely increased in January, rising just 0.1% after plunging 0.6% in December.

In turn, the personal consumption expenditures (PCE) price index — the Fed's preferred inflation gauge — fell 0.1% in January, knocking down the yearly rate from 1.8% to 1.4%, and remained well below the Fed's target level of 2%. As a result, low levels of expected inflation drove consumer sentiment higher in March, while lower mortgage rates helped new home sales rebound in February.

The final gross domestic product (GDP) reading showed that the U.S. economy expanded at a firm 2.2% during the fourth quarter, highlighting the transition from a "great" to "good" environment. Further slowing (but still positive) earnings growth, accommodative financial conditions, and improvements in trade talks presented a positive backdrop during the first quarter. As a result, the S&P 500 marked its best first quarter since 1998, advancing 13.6%. Meanwhile, the NASDAQ Composite gained 16.8%.

DEVELOPED MARKETS: TRADE OPTIMISM AND A DOVISH ECB DROVE A RECOVERY

In Europe, Brexit and other political uncertainties soured investor risk appetite, sending investors into corporate and government bonds. Additional evidence of slumping global demand — particularly from China — weighed on Europe's export-driven businesses, raising worries that the trade dispute could further aggravate economic conditions. In Germany, IHS Markit's manufacturing survey showed that German output fell to 44.7 from 47.6 (with a score below 50 indicating a fall in business activity) in February for a third consecutive month, marking the lowest level in over six-and-a-half years.

In response to slowing growth and signs of feeble inflationary pressures, the European Central Bank (ECB) announced new stimulus measures in an attempt to boost the bloc's economy. The ECB stated that it would roll out loan programs in an attempt to promote business and consumer bank loans at lower rates, while also postponing any interest rate hikes until 2020 at the earliest. As a result, investors flocked into government bonds sending Germany's 10-year government bond yield into negative territory for the first time since 2016.

Despite all headwinds, investors looked past the weaker economic data and focused on reports that a near-term trade deal between Washington and Beijing is closer on the horizon. Further, reports of the UK and the European Union agreeing on a short extension to Brexit reduced the risk of a disorderly departure, sending equities higher. As a result, the MSCI EAFE index rose by 10% during the first quarter.

EMERGING MARKETS: EQUITIES RISE FOLLOWING REBOUND IN CHINESE MANUFACTURING

In response to the signs of decelerating economic growth witnessed in 2018, the People's Bank of China stepped up its efforts to boost lending to businesses while lowering financing costs. In addition, Premier Li Keqiang announced that the Chinese government would reduce taxes and fees while loosening financial conditions and monetary policy. While slowing global demand and the tariff dispute dragged emerging markets sharply lower last year, investors witnessed a rebound in Chinese equities early in 2019. Both an accommodative stance from the central bank and de-escalatory measures from the U.S. and China sparked "risk-on" sentiment from investors.

On a positive note, China's manufacturing PMI index surprisingly rose in March, as factory activity showed a decent recovery. While worries of a global slowdown persisted due to weakness in other emerging market countries, the upbeat manufacturing data from China offered investors a sign that activity in the world's second largest economy may be beginning to pick up. As a result, Chinese equities marked their third consecutive month of gains, while the MSCI Emerging Markets index closed the quarter 9.9% higher.

THE YIELD CURVE: CAUTIONARY SIGNS FROM THE FIXED INCOME MARKETS

So far this year, longer-term Treasury yields have trended lower, as investors have favored safer assets in response to signs of decelerating global growth. In turn, the Fed's four interest rate hikes in 2018 drove short-term rates higher, flattening — and at certain points inverting — the yield curve. As a result, investors' anxieties rose as an inverted yield curve has historically preceded every recession since the 1960s. Further, the inversion also triggered sell orders on computer algorithms which are preset by traders to 'trade out' of a position once certain levels are reached. These algorithms have been responsible for exacerbating market sell-offs as the orders are executed automatically once preset trigger levels are hit. It is worth noting that while the inverted yield curve is not an infallible recession harbinger, it is an important sign worth monitoring closely due to its historical accuracy, particularly if it persists and widens. However, after inverting in March, the U.S. Treasury yield curve widened slightly towards the end of the month, as the yield on the 10-year U.S. Treasury note temporarily rose above the yield on the 3-month Treasury bill, returning the curve to a "normal" shape.

CONCLUSION

While volatility and sharp market movements last year took investors by surprise, the subsequent rebound seen during the first quarter of 2019 highlights the value and importance of having a balanced, long-term approach to investing. The CBOE Volatility Index, a so-called "fear gauge", dropped 46% in the first quarter of 2019 to a level closer to its historical average, as the cloudy outlook seen during late 2018 has somewhat cleared. As we continue navigating choppy waters in the late stage of the economic cycle, we expect some additional bumps down the road, as the outcome of Brexit is still uncertain, and the U.S. — China trade dispute is still outstanding despite the progress made. However, current employment and labor conditions in the U.S. remain at historically robust levels and do not indicate a recession in the near-term.

FINANCIAL MARKET RETURNS

U.S. Equity	Q1 2019	1 Year	3 Year (Annualized)	5 Year (Annualized)	10 Year (Annualized)
DJ Industrial Average	11.8%	10.1%	16.4%	12.2%	16.0%
NASDAQ Composite Index	16.8%	10.6%	18.0%	14.3%	18.9%
S&P 500 TR Index	13.6%	9.5%	13.5%	10.9%	15.9%
Russell 1000 Index	14.0%	9.3%	13.5%	10.6%	16.0%
Russell 1000 Growth Index	16.1%	12.7%	16.5%	13.5%	17.5%
Russell 1000 Value Index	11.9%	5.7%	10.5%	7.7%	14.5%
Russell Mid Cap Index	16.5%	6.5%	11.8%	8.8%	16.9%
Russell Mid Cap Growth Index	19.6%	11.5%	15.1%	10.9%	17.6%
Russell Mid Cap Value Index	14.4%	2.9%	9.5%	7.2%	16.4%
Russell 2000 Index	14.6%	2.0%	12.9%	7.1%	15.4%
Russell 2000 Growth Index	17.1%	3.9%	14.9%	8.4%	16.5%
Russell 2000 Value Index	11.9%	0.2%	10.9%	5.6%	14.1%

International Equity	Q1 2019	1 Year	3 Year (Annualized)	5 Year (Annualized)	10 Year (Annualized)
MSCI EAFE Index ($USD, net)	10.0%	-3.7%	7.3%	2.3%	9.0%
MSCI AC World Index ($USD, net)	12.2%	2.6%	10.7%	6.5%	12.0%
MSCI AC World Ex US Index ($USD, net)	10.3%	-4.2%	8.1%	2.6%	8.8%
MSCI Emerging Markets Index ($USD, net)	9.9%	-7.4%	10.7%	3.7%	8.9%
MSCI BRIC Index ($USD, net)	14.0%	-3.4%	15.7%	6.3%	8.5%

Fixed Income	Q1 2019	1 Year	3 Year (Annualized)	5 Year (Annualized)	10 Year (Annualized)
Bloomberg Barclays US Treasury 1-3 Year Index	1.0%	2.7%	1.0%	1.0%	1.0%
Bloomberg Barclays US Treasury 5-10 Year Index	2.4%	5.3%	1.0%	2.7%	3.1%
Bloomberg Barclays US Long Treasury Index	4.7%	6.2%	1.5%	5.4%	5.1%
Bloomberg Barclays US Treasury US TIPS Index	3.2%	2.7%	1.7%	1.9%	3.4%
Bloomberg Barclays US Govt/Credit Intermediate Index	2.3%	4.2%	1.7%	2.1%	3.1%
ICE BofAML Municipals 1-10 Year A-AAA Index	2.0%	4.3%	1.7%	2.1%	2.9%
Bloomberg Barclays US Corporate High Yield Index	7.3%	5.9%	8.6%	4.7%	11.3%
ICE BofAML Preferred Stock Fixed Rate Index	8.7%	5.0%	5.0%	6.3%	11.5%
JPMorgan GBI EM Global Diversified Index	2.9%	-7.6%	3.3%	-0.8%	4.4%

Source: Bloomberg, Morgan Stanley Capital International, Russell®, Standard and Poor's and Barclays.

INDEX DEFINITIONS

U.S. EQUITY

Dow Jones Industrial Average: is a price-weighted average of 30 actively traded blue-chip U.S. stocks

NASDAQ Composite Index: is a market capitalization index of approximately 3,000 common equities listed on the NASDAQ exchange

S&P 500 TR Index: is a type of equity index that tracks both the capital gains of the equities in the S&P 500 and assumes any cash distributions (dividends) are reinvested back into the index

Russell 1000 Index®: measures the performance of the 1,000 largest companies in the Russell 3000

Russell 1000 Growth Index®: measures the performance of those Russell 1000 companies with higher price-to-book ratios and higher forecasted growth values

Russell 1000 Value Index®: measures the performance of those Russell 1000 companies with lower price-to-book ratios and lower forecasted growth values

Russell Mid Cap Index®: measures the performance of the 800 smallest companies in the Russell 1000 index

Russell Mid Cap Growth Index®: measures the performance of those Russell Midcap companies with higher price-to-book ratios and higher forecasted growth values. The stocks are also members of the Russell 1000 Growth index

Russell Mid Cap Value Index®: measures the performance of those Russell Midcap companies with lower price-to-book and lower forecasted growth values. The stocks are also members of the Russell 1000 Value index

Russell 2000 Index®: measures the performance of the 2,000 smallest companies in the Russell 3000 index

Russell 2000 Growth Index®: measures the performance of those Russell 2000 companies with higher price-to-book ratios and higher forecasted growth values

Russell 2000 Value Index®: measures the performance of those Russell 2000 companies with lower price-to-book ratios and lower forecasted growth values

INTERNATIONAL EQUITY

MSCI EAFE Index: is a free float-adjusted market capitalization index that is designed to measure the equity market performance of developed markets, excluding the US & Canada

MSCI AC World Index: is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of developed and emerging markets

MSCI AC World Ex US Index: captures large and midcap representation across 22 of 23 developed marketing countries (excluding the US) and 23 Emerging Markets countries

MSCI Emerging Markets Index: is a free float-adjusted market capitalization index that is designed to measure equity market performance in the global emerging markets

MSCI BRIC Index: is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance across the following 4 emerging market country indexes: Brazil, Russia, India and China

FIXED INCOME

Bloomberg Barclays US Treasury 1–3 Year Index: measures the performance of U.S. Treasury securities that have a remaining maturity of at least one year and less than three years

Bloomberg Barclays US Treasury 5–10 Year Index: measures the performance of U.S. Treasury securities that have a remaining maturing of at least five years and less than 10 years

Bloomberg Barclays US Long Treasury Index: includes all publicly issued, U.S. Treasury securities that have a remaining maturity of 10 or more years, are rated investment grade, and have $250 million or more of outstanding face value

Bloomberg Barclays US Treasury US TIPS Index: the index includes all publicly issued U.S. Treasury inflation-protected securities that have at least one year remaining to maturity, are rated investment grade, and have $250 million or more of outstanding face value

Bloomberg Barclays US Govt/Credit Intermediate Index: the index measures the performance of the USD-denominated U.S. Treasuries, government-related and investment grade U.S. corporate securities that have a remaining maturity of greater than one year and less than ten years

Bloomberg Barclays US Corporate High Yield Index: measures the USD-denominated, high-yield, fixed-rate corporate bond market. Securities are classified as high yield if the middle rating of Moody's, Fitch and S&P is Ba1/BB+/BB+ or below. Bonds from issues with an emerging markets country of risk, based on Barclay's EM country definition, are excluded

ICE BofAML Municipals 1-10 Year A-AAA Index: is a subset of the BofAML U.S. Municipal Securities Index and includes all securities with a remaining term to final maturity less than 10 years and rated AAA through A3, inclusive.

ICE BofAML Preferred Stock Fixed Rate Index: this index is designed to replicate the total return of a diversified group of investment-grade preferred securities

JPMorgan GBI EM Global Diversified Index: is an investable benchmark that includes only those countries that are directly accessible by most of the international investor base. This index exclude countries with explicit capital controls, but does not factor in regulatory / tax hurdles in assessing eligibility

DISCLOSURE

First Republic Private Wealth Management encompasses First Republic Investment Management, Inc. ("FRIM"), an SEC-registered investment advisor, First Republic Securities Company, LLC ("FRSC"), Member FINRA/SIPC, First Republic Trust Company ("FRTC") and First Republic Trust Company of Delaware LLC ("FRTC-DE"). FRIM, FRSC, and FRTC-DE are wholly owned subsidiaries of First Republic Bank. FRTC is a division of First Republic Bank. Investment advisory services are provided through FRIM. Securities brokerage services are provided through FRSC. Trust and fiduciary services are provided through FRTC and FRTC-DE.

This document is for information purposes only and is not intended as an offer or solicitation, or as the basis for any contract to purchase or sell any security, or other instrument, or to enter into or arrange any type of transaction as a consequence of any information contained herein.

All analyses and projections depicted herein are for illustration only, and are not intended to be representations of performance or expected results. The results achieved by individual clients will vary and will depend on a number of factors including prevailing dividend yields, market liquidity, interest rate levels, market volatilities, and the client's expressed return and risk parameters at the time the service is initiated and during the term. Past performance is not a guarantee of future results. Investors should seek financial advice regarding the appropriateness of investing in any securities, other investment or investment strategies discussed or recommended in this report and should understand that statements regarding future prospects may not be realized.

Investors cannot invest directly in an index. The indexes referred to do not reflect management fees and transaction costs that are associated with some investments. Although information in this document has been obtained from sources believed to be reliable, we do not guarantee its accuracy, completeness or fairness, and it should not be relied upon as such. This document may not be reproduced or circulated without our written authority.

Investment and Advisory Products and Services are Not FDIC Insured, Not Bank Guaranteed and May Lose Value.