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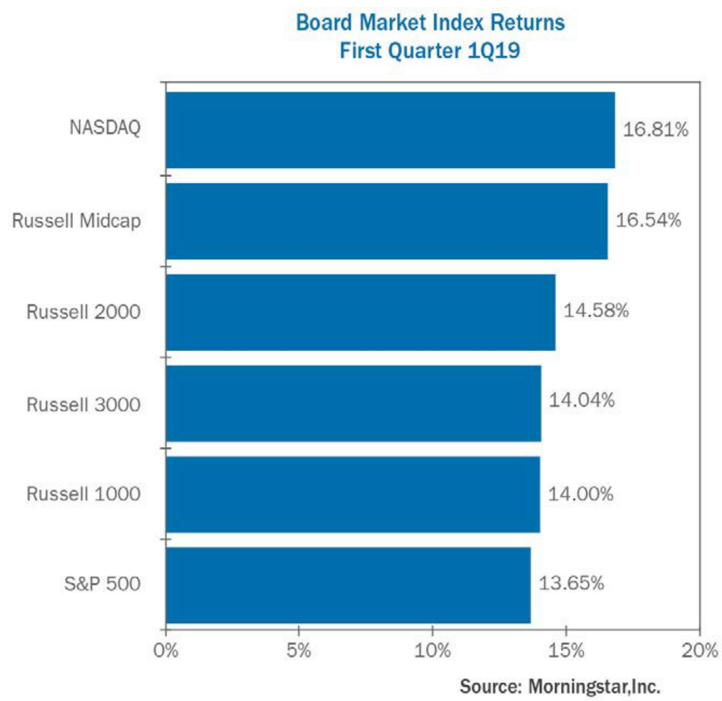
Market Commentary
Q1 2019

Talk about turning on a dime! As we mentioned in our last report, December of 2018 was the worst December for the market since the depression. In quick turnaround, this past quarter the market had its best performing quarter since 2009. Basically, all areas of the stock as well as the bond markets were up.

The Economy



The US economy's growth moderated somewhat in the first quarter. The Bureau of Economic Analysis reported its second estimate of fourth quarter 2018 gross domestic product (GDP) of 2.2%, lower than the prior estimate of 2.6%, and also lower than the third quarter's 3.4% reading. The employment situation slowed in the latest month, but continued to deliver gains, with an average of approximately 186,000 jobs added each month. The unemployment declined to 3.8% from the prior month's level of 4.0%. The Federal Open Market Committee (FOMC) maintained its existing interest rate policy by keeping the federal funds rate target at a range of 2.25% to 2.50%. Economists do not expect there to be any additional interest rate increases in 2019 as economic growth has eased.

The global economic environment has softened somewhat, with some economists saying the global expansion is now past its peak for this cycle. The reasons for the slowing are attributed to the cooling in world trade, capacity constraints and a tightening in monetary conditions. The European Central Bank has again loosened monetary policy in an effort to catalyze the slowing Eurozone economy, and the Brexit outcome will also impact the region's outlook. China's policymakers are attempting to transition the economy to one that can deliver more sustainable growth.

At the same time, growth is cooling, and trade talks with the US could complicate matters.

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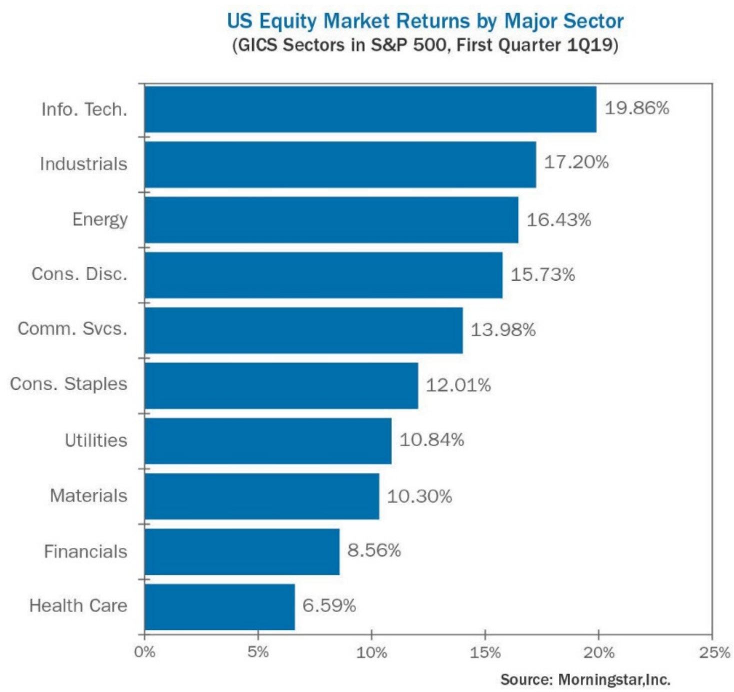
Highlights

GROSS DOMESTIC PRODUCT (GDP)



The Bureau of Economic Analysis released the second estimate of the fourth quarter 2018 real GDP, a seasonally adjusted annualized rate of 2.2%, down fairly materially from the third quarter's 3.4% annualized growth, and lower than the 2.6% prior estimate. The economy slowed from the second and third quarters of 2018 when the benefits of the deficit-financed tax cuts were in full force. Consumer spending was the primary driver of the growth, followed by fixed investment. Corporate profits fell by 0.4% (not annualized) during the quarter, while real disposable income rose by 4.3%. Economists and analysts are not in agreement as to whether the slowdown is the start of something more serious – perhaps leading to a recession – or merely temporary. On the positive side, the government shutdown that occurred during the latter stages of the quarter is over, and over the past few years GDP growth has been somewhat seasonal, with slowing in the fourth and first quarters and acceleration in the second and third. In addition, economists believe that the economy's significant momentum will enable it to avert a recession in the foreseeable future.

HOUSING

The housing segment rebounded sharply after consolidating for most of the past year due to rising mortgage rates. Existing-home sales for February (the latest monthly data available) grew at an annualized rate of 5.5 million units, almost 12% higher than the results from January, but down about 2% from year-ago levels. The inventory of existing homes was at about four months of supply, up somewhat from the prior year. Existing-home prices in February increased 3.6% from February 2018. In the new-home segment, the NAHB Housing Market Index, a measure of homebuilding activity, ended the quarter at 62, the same as February's level, but much lower than the levels experienced earlier in 2018. The outlook for housing remains positive, as wages continue to increase, and mortgage rates have declined from recent levels.

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EMPLOYMENT

The employment situation slowed dramatically in February, exhibiting signs of weakness following a long period of generally robust gains. Employers added only 20,000 jobs during the month, well below the consensus expectations of 180,000 new jobs, and far below the prior month's gain of 311,000. Analysts point to seasonality as being one of the key reasons for the slowdown in payroll growth. The three-month moving average also fell as a result of the meager gains in February, coming in at 186,000. The unemployment rate in February declined to 3.8%, and economists are generally of the opinion that it will end the year even lower. Average hourly earnings increased by a 3.4% from the year-ago level.

FEDERAL RESERVE POLICY

The FOMC ended its recent March meeting by announcing that there would be no change in the federal funds rate target range to 2.25% to 2.50%. The decision to stand pat was widely expected, and was seemingly a commitment by the committee to take a more sustained pause. Many economists believe that rate increases for this cycle are now over as the FOMC does not want to derail the expansion. Analysts do not expect any rate increases for the remainder of 2019.

Interest Rates

Fixed income securities' prices and yields were impacted by concerns about slowing global economic growth during the quarter. The FOMC has acknowledged the slowdown and in a desire not to drive the US economy into a recession has backed off of further rate increases. This pause has resulted in a rally in bond prices, and a drop in yields. Some economists have pointed out that now that the FOMC has hit the pause button in its rate-hike program this cycle, it will be difficult to raise rates this year if the economy begins to heat up due to the repercussions such an unanticipated move would have on the financial markets. In a change from the previous quarter, most analysts, and the FOMC itself, expect there will not be any more rate increases in 2019.

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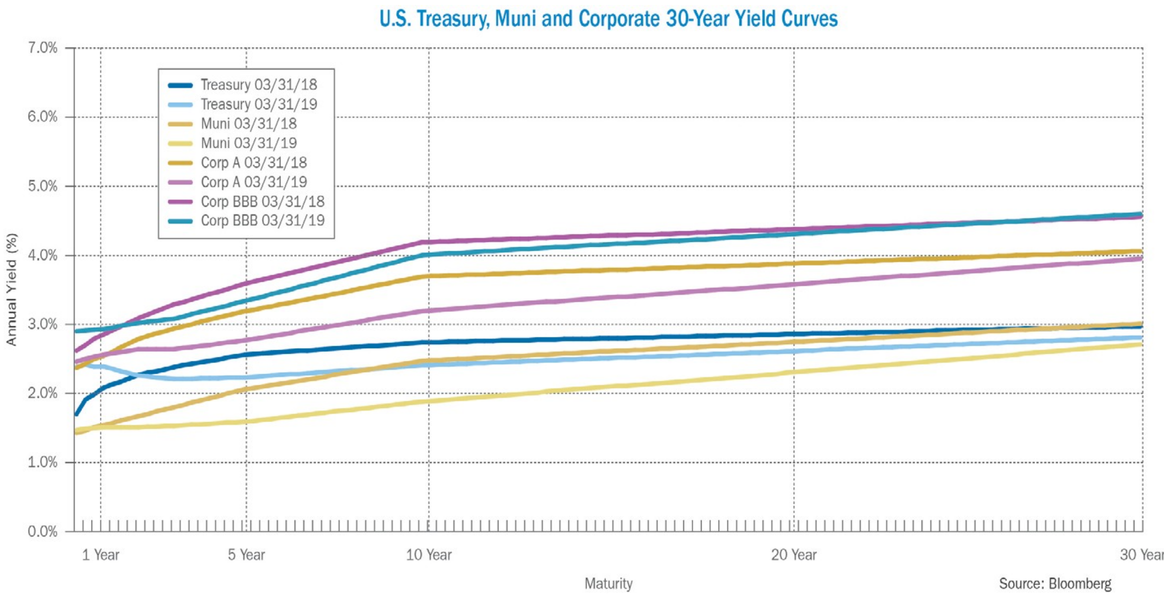

As has been the trend in recent quarters, the Treasury yield curve flattened again during the first quarter, with yields on short-term maturities staying relatively stable and those on intermediate-term maturities falling. By the end of the quarter, the yield on the benchmark 10-year US Treasury note was lower, ending the quarter at 2.41%, compared to 2.69% on December 31.

As mentioned above, interest rates in the quarter headed steadily lower as a result of concerns about the slowing pace of global growth. In addition, investors were also attempting to digest the potential Brexit outcomes and scenarios of trade talks between the U.S. and China, as well as the Federal Reserve's ongoing balance sheet unwinding.

Total returns on fixed income securities were positive across the various market segments. The Bloomberg Barclays Treasury 5-7 Yr. Index jumped by +2.2% for the quarter. The Bloomberg Barclays U.S. Corporate 5-10 Yr. Index surged +5.4% during the three months. High yield securities, which often follow the performance of equities, climbed, delivering a positive return of +7.3%. Municipals fared well, as the Bloomberg Barclays Municipal Bond Index rallied by +2.9% during the quarter. Prices of non-US fixed income securities were also higher in the quarter, as the Bloomberg Barclays Global Aggregate ex-U.S. Index advanced +1.5%. Emerging markets bonds made a robust recovery, with the JPM EMBI Global Index gaining +6.6%.

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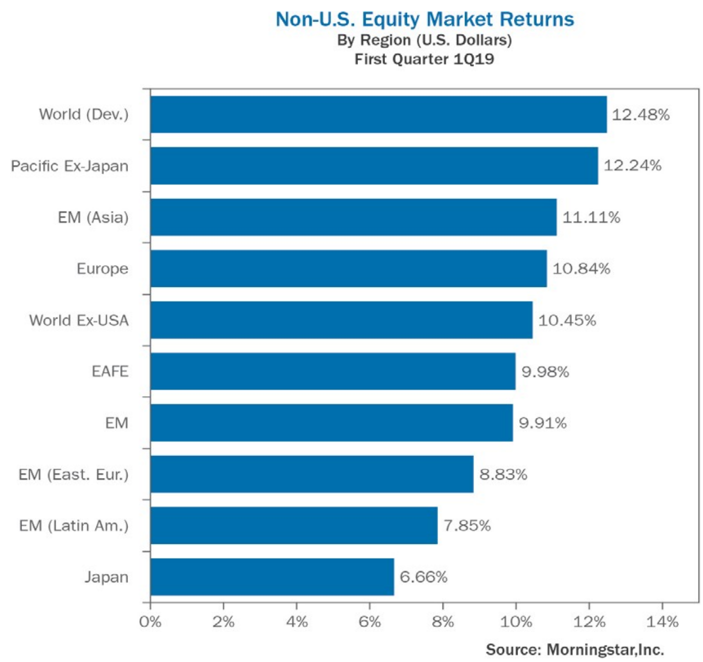
Equity Markets

Equity markets did an about-face during the quarter, generating the largest quarterly advance since the third quarter of 2009. Stocks' first quarter performance almost completely recouped the losses of the prior quarter. Whereas the losses in the fourth quarter of 2018 were prompted by fears that the FOMC was being unnecessarily aggressive in raising rates, the gains of the first quarter can largely be attributed to the FOMC's curtailing of its rate-increase program. Investors were heartened by the decision, which appears was made in time to avert a significant economic slowdown or recession. During the quarter several broad-based indexes rose more than 15%. Within this landscape, the S&P 500 Index finished the quarter with a robust gain of +13.7%.



Each of the ten primary economic sectors produced performance results that were strongly positive during the quarter. Information Technology, Industrials and Energy were the strongest performers on a relative basis, generating returns of +19.9%, +17.2%, and +16.4%, respectively. The Health Care, Financials and Materials sectors were the poorest relative performers, posting returns of +6.6%, +8.6%, and +10.3%, respectively. The Russell 1000 Index of large capitalization stocks generated a +14.0% total return. Within the large cap segment, growth stocks sharply outperformed value stocks. Small cap stocks, as represented by the Russell 2000 Index, slightly outperformed large caps, and finished the quarter with a total return of +14.6%. Small cap value underperformed small cap growth. The NASDAQ Composite, dominated by information technology stocks, finished the quarter with a gain of +16.8%. The Dow Jones Industrial Average of 30 large industrial companies advanced +11.8%.

Real Estate Investment Trusts (REITs) also posted solid gains during the quarter, with the DJ US Select REIT Index surging +15.7%. Commodities were also lower, with the Bloomberg Commodity Index gaining +6.3% for the quarter.

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International stocks delivered generally positive results that fell somewhat short of the gains in US equities. Economic growth continues to lag that of the US, and the Eurozone is also trying to determine how the UK's departure from the European Community ("Brexit") will come to pass. The MSCI ACWI Ex-USA Index, which measures performance of world markets outside the US, advanced by+10.3%. The MSCI EAFE Index of developed markets stocks rose by +10.0%. Regional performance was also generally strong for the quarter.

China was the strongest performer on a relative basis, with a return of +17.7%. Latin America was the poorest relative performer, gaining +7.9%. Emerging markets performance was positive, as the MSCI Emerging Markets Index was higher by +9.9%.

Looking Forward

The US economy's expansion continues on, and will likely become the longest on record this summer. The rate of growth likely won't be able to keep pace with that of the middle quarters of 2018, and the recent deceleration in job growth indicates that future economic gains will be more muted. Importantly, however, the expansion is on track to continue, driven largely by the FOMC's recognition of slowing conditions and resulting decision to curtail its rate-increase program. Mortgage rates have declined, undergirding the housing market, and stock prices have rebounded very sharply. Economists point to government spending also being a positive contributor to growth going forward. Inflation and wage growth have experienced an uptick, and economists believe that further acceleration could mean the expansion is nearing an end as the FOMC will need to act to avoid overheating. Analysts are encouraged that there may be a positive resolution to the trade war with China relatively soon, if for no other reason than President Trump wants to avoid a stock market correction similar to the one that occurred in the fourth quarter when trade talks with China were not going so well. It appears an uncomplicated resolution to Brexit will not occur, and Brexit is now likely to be pushed off for at least several months. Most analysts are of the opinion that whatever the outcome, Brexit does not impose serious problems for the world economy.

After the significant drop in the market at the end of last year, investors were breathing a huge sigh of relief this past quarter. However, the market performance over the past 6 months underscores the extreme volatility potential in the market. As quickly as the market can go up it can also go down and vice versa.

With the recovery from the December drop, we feel it is a great time for all clients to review their upcoming cash needs and to let us of any changes that we are not aware of. Additionally, please be sure to let us know

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if you have any concerns about your portfolio and allocation of if you feel your allocation is no longer appropriate for your situation or tolerance for risk.

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