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First Quarter 2019

Up, But Not Out

Our fourth quarter newsletter from 2018 was titled "Down, But Not Out," insinuating that while we experienced a significant pullback to end 2018, the markets weren't particularly ready to throw in the towel and the first quarter of 2019 proved exactly that. After suffering the worst December since 1931 and the worst annual returns since 2008, the markets rebounded significantly in Q1 as the S&P 500 experienced its best quarter since 2009 returning 13.07%. Much of the worry around slower earnings growth which had arisen at the end of 2018 was quickly forgotten once Q4 results came trickling in. More than 70% of S&P 500 companies reported earnings that beat estimates and over 60% reported stronger than expected revenues. Even the negative news to come out of earnings season didn't affect stocks as investors would have expected. Companies experienced their best stock price reactions to negative earnings surprises in nine years, suggesting most of the bad news had been priced in at the end of last year.

Tech stocks fared even better as the trade outlook improved, lifting the NASDAQ 16.49% year-to-date. The Dow Jones was on a similar path to start the year but trailed the other two major market indexes after Boeing's stock price took a 17% hit following the news of its 737 Max 8 aircrafts being grounded due to a software glitch which was linked to two separate incidences in less than six months. With over a 10% weight in the index, Boeing is the largest component of the Dow Jones Industrial Average and was the primary detractor that caused the index to lag the S&P by nearly 2%, returning 11.15% for the quarter.

Looking internationally, foreign markets also had a strong start to 2019, but as has been the case frequently over the past few years, again underperformed U.S. markets. Economic readings from Europe showed the EU economy was clearly losing momentum. However, despite that disconcerting European economic data, foreign developed markets slightly outperformed emerging markets on a net basis. The lack of an official trade deal between the U.S. and China by quarter end, along with a stronger U.S. dollar, negatively impacted emerging markets. Foreign developed markets were aided by the European Central Bank announcing in March it would re-start a stimulus program to help the EU economy.

In the fixed income markets the Barclays US Bond Aggregate Index returned just over 3% in Q1 as the 10-year treasury rate fell by nearly 30 basis points (0.30%). Given the Fed's language regarding interest rates and their de facto commitment to put the current rate hike cycle on pause, longer-term bonds outperformed relative to short-term bonds as investors paid heed to the Fed's cautionary language regarding global economic growth.

Going back to our fourth quarter newsletter, we pointed out three primary reasons for the pullback in late 2018; the fear of a peak in earnings growth, trade tensions, and an overly-aggressive Fed. Even though all three of those fears have been somewhat subdued, none of them have been fully resolved.

While many feared we were headed for an earnings recession, the S&P 500 eked out a positive quarter as earnings rose 3% in Q4, albeit at a much slower rate than in the three quarters prior. Although trade negotiations between China and the U.S. have shown progress – primarily displayed in the extension of the March 1 deadline between the two countries – we can only speculate on where negotiations are truly headed with China and whether or not the two parties will come to an agreement that will result in lower tariffs. In November of last year, after Fed chair Jerome Powell walked back his comments from October about being "a long way from neutral," interest rates have

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come back down to 2017 levels. This back and forth puts the Fed in a precarious situation. They can't necessarily raise rates from here as they've already expressed concerns regarding global economic growth and risk sending stocks lower or worse, sending the economy into a recession. At the same time cutting rates in the near-term could send a negative psychological message to the markets and create the mindset of an impending recession. Ultimately the Fed does need to raise rates eventually in order to have the ability to properly stimulate the economy if and when the expansion does end. But as they've made clear over the last several months, those rate hikes shouldn't be expected to come in 2019.

ANNOUNCEMENT — Please join us in welcoming our newest addition to the FAS team, Pat Amey, CFP®!

Pat joined the team in January 2019 and will be working with new and existing FAS clients. Pat has worked as a financial planner for ten years. He earned his BA from the University of Kansas, MBA from Rockhurst University and obtained his CERTIFIED FINANCIAL PLANNER™ certification in 2013.

All three of these topics are interconnected through one major concern in the markets today – slowing of the global economy. The slowdown in China has driven much of the overall slowdown around the globe. While many see China as the manufacturing powerhouse of the world, it is easy to overlook the fact that China is also a major importer of materials from countries such as Germany, Japan, Taiwan and Korea. All of those countries have experienced a significant slowdown in manufacturing in recent months and could experience further declines if the U.S. and China cannot come to a mutual agreement on trade. As stated above, this fear of slowing global growth has been a major cause of concern for the Fed during the latest tightening cycle and has been the catalyst for putting the Fed on pause. Additionally, nearly 30% of S&P 500 companies' revenues are driven by foreign countries so the U.S. is not necessarily shielded from a global slowdown.

2019 Performance Figures

	1st Qtr.	2019
DJIA (Dow)	11.15%	11.15%
S&P 500	13.07%	13.07%
NASDAQ COMP	16.49%	16.49%
MSCI EAFE	9.04%	9.04%
Russell 2000 Small Cap	14.13%	14.13%
Barclays US Aggregate Bond Index	3.04%	3.04%
MSCI World All Cap	11.88%	11.88%

Markets have made a significant comeback since ending 2018 on a negative note. Stock valuations were relatively cheap by historical standards at the end of last year as the S&P traded at 14.1 times forward earnings and the recent rally has brought valuations back down (or rather up) to earth to just above its 25-year average. This upcoming earnings season will be important as corporate earnings results and commentary will need to reinforce and confirm the optimistic economic and corporate views currently reflected in the stock market.

We start this second quarter of 2019 thankful for the strong start to the year, but also mindful that now is not a time to become complacent – because risks to investors' portfolios remain. The markets may be up, but the global economy is not out of the woods just yet as we face several headwinds moving forward. Regardless, we are committed to helping you navigate this challenging investment environment. Even if volatility returns, history has shown that a long-term approach combined with a well-designed and well-executed investment strategy can overcome periods of heightened volatility, market corrections, and even bear markets. It is critical for you to stay invested, remain patient, and stick to a plan. This current economic expansion and bull market is over 10 years old. There is a saying that bull markets don't die of old age. While that is certainly true, it is prudent to be aware of this global slowdown and the negative impact it could have on stocks.