

FEBRUARY 2019 RECAP

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The rebound in equity markets continued in February as the S&P 500 increased by +3.2% and is now up +11.5% year-to-date – the best start to a calendar year since 1991. The market has now gained back nearly all of December’s losses. Recall that 2018 included a near bear market (peak-to-trough decline of -19.8%), the first calendar year loss since 2008, and the worst December monthly return since 1931. The strong start to 2019 is not because all the issues facing the market in late-2018 have quickly evaporated. Rather, we believe that last year’s selloff was another example of how markets can be extremely volatile and sometimes irrational in the short-term. In February, the news flow on the market’s current most important topics, the economy, US/China trade war, and Fed policy was generally positive (see below for details).

Our equity market outlook remains balanced as we do not believe this is the time for excessive risk taking or extreme caution. We will publish a full market outlook along with our Q1 2019 recap next month. We would move to a more optimistic stance if the US and China agree to a trade deal where all tariffs are rescinded, the Fed remains accommodative, and/or global economic growth starts to accelerate. We would turn more cautious if trade talks breakdown, the Fed turns hawkish, and/or economic data begins to deteriorate. We acknowledge that markets and risks can change quickly, and we will continue to monitor new developments.

Index	February	YTD	1-Year	3-Year	5-Year
S&P 500	3.21%	11.48%	4.68%	14.89%	10.63%
Dow Jones Industrial Average	4.03%	11.62%	5.95%	18.65%	12.34%
Nasdaq Composite	3.44%	13.52%	3.57%	17.85%	11.78%
S&P 400	4.24%	15.14%	4.14%	14.28%	8.46%
Russell 2000	5.20%	17.03%	5.58%	16.46%	7.34%

International Equity Markets					
Index	February	YTD	1-Year	3-Year	5-Year
MSCI EAFE	2.56%	9.32%	-5.57%	9.81%	2.54%
MSCI Europe	3.37%	10.21%	-4.85%	9.19%	1.29%
MSCI Japan	-0.03%	6.07%	-9.98%	9.78%	5.55%
MSCI Emerging Markets	0.23%	9.02%	-9.54%	15.40%	4.50%

Fixed Income					
Index	February	YTD	1-Year	3-Year	5-Year
Barclays US Aggregate Bond Index	-0.06%	1.00%	3.17%	1.73%	2.31%
Barclays US Credit Index	0.22%	2.38%	2.72%	3.57%	3.12%
Barclays High Yield Index	1.66%	6.26%	4.31%	9.96%	4.52%
Barclays Municipal Bond Index	0.54%	1.30%	4.13%	2.29%	3.43%

Commodities					
Index	February	YTD	1-Year	3-Year	5-Year
Oil	10.06%	26.01%	-7.17%	74.56%	-44.22%
Gold	0.80%	2.70%	-0.21%	7.62%	-0.65%
Silver	0.83%	2.26%	-3.80%	4.25%	-25.65%
Copper	9.77%	12.25%	-5.07%	39.28%	-8.91%

SOURCE: BLOOMBERG

International markets produced positive results as Developed International (MSCI EAFE) markets increased by +2.6% while Emerging Markets (MSCI EM) gained +0.2%. Within Fixed Income markets, bonds declined slightly as the Barclays US Aggregate Bond Index decreased by -0.1%.

We’d like to highlight three key events of February 2019:

Q4 2018 GDP – Growing but Slowing

The United States economy ended 2018 at a solid pace as Q4 GDP came in at a +2.6% seasonally adjusted annual rate. The report was better than the expected +2.2% consensus estimate. Consumer spending, which accounts for about two-thirds of the economy, increased by +2.8% and was driven by health care, financial services, and insurance spending. The current economic expansion is set to become the longest on record in mid-2019.

Economists expected economic growth to moderate in late 2018 and through 2019 due to weaker global growth and the fading effects of fiscal stimulus. GDP growth in the second and third quarters of 2018 came in at +4.2% and +3.4% respectively. The current Bloomberg consensus estimate for 2019 GDP growth is at +2.5% Y/Y, which would be a deceleration from 2018’s +2.9% Y/Y level.

The first GDP estimate for Q4 2018 was originally scheduled to be released on January 30th, but it was delayed by a month due to the government shutdown. The Commerce Department estimated that the government shutdown lowered Q4 growth by about -0.1%. The agency also cautioned that the full effects of the shutdown cannot be fully quantified.

Obligatory Trade Update

The US and China moved closer to reaching a trade agreement throughout February as extensive negotiations yielded positive results. A US delegation traveled to China in the middle of the month while talks resumed in the Washington the following week. The latest round of trade negotiations went well enough that talks were extended for an additional two days. In a positive sign that the two sides are moving closer to a deal, President Trump agreed not to implement the previously scheduled tariff rate increase of 10% to 25% on \$200 billion worth of Chinese goods.

Reports indicate that a deal could be finalized at a meeting between President Trump and President Xi as early as mid-to-late March. The two sides are working toward a comprehensive deal that addresses currency, agriculture, non-tariff barriers, technology transfer, and intellectual property. If a deal is signed, what happens to the current tariffs remains a major question. Tariffs could remain in place for a period until there is verifiable evidence that both sides are following the terms of the agreement or they could be rescinded immediately. The trade war will remain a major stock market risk and a drag on the global economy until an agreement is signed and all tariffs are eliminated.

FOMC Minutes

The Federal Open Market Committee (FOMC) minutes from the January meeting shed some light on the Fed’s new “patient” and “flexible” approach. Recall that in January the Fed pivoted from their December of 2018 approach by stating they would now be patient with future interest rate increases and flexible with their balance sheet runoff program. The January minutes stated that patience would allow the Fed more time to assess the US economy, inflation, ongoing trade war, and the economic slowdown in Europe and China. Most investors expect the Fed to pause interest rate increases until at least the second half of the year.

The big news from the FOMC minutes was that the Fed will announce a plan to end their balance sheet runoff in late-2019. Fed Chair Powell recently stated that “we’re going to be in a position to stop the runoff later this year and my guess is we’ll be announcing something fairly soon.” The minutes indicated that the Fed was somewhat puzzled that investors partially blamed the balance sheet runoff for the stock market decline in December 2018. The Fed noted that the balance sheet reduction plan was communicated well in advance and had been proceeding smoothly for more than a year. A formalized plan to end the balance sheet runoff could be announced at the March 20th FOMC meeting.

CLIENT QUESTION

Are market risks elevated compared to historical periods?

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“In the 20th century, the United States endured two world wars, the Great Depression, a dozen or so recessions and financial panics, oil shocks, a flu epidemic, and the resignation of a disgraced president. Yet the Dow rose from 66 to 11,497.” – Warren Buffett

An old investment adage is that the stock market climbs a “wall of worry.” This simply means that the market has risen over time despite a constant barrage of potential risks that could cause a correction or decline. The market always has risks to overcome and there is never an “all-clear” signal. The following chart shows the top market risk each year going back to 1968. We fully acknowledge that some of the risks should have been taken very seriously and some did cause negative returns for a period. However, despite all these “reasons to sell”, the stock market produced a total return of +11,744% from 1968 to 2018. The market also generated positive returns in 40 of the 51 years. Over that time period, a hypothetical \$10,000 investment would have grown to about \$1,177,000. Equity markets have historically provided excess returns over the risk-free interest rate (3-month US Treasury Bill) over long time periods. The risk-free interest rate is defined as the return of an investment with no risk of financial loss. Since 1960, the excess return of the S&P 500 over the risk-free interest rate has averaged about +6% each year. As investors, taking the risk that the market could go down and experiencing the volatility is the price we pay for that excess return.

The 24-hour news cycle and advent of social media might make it seem as though risks are more prevalent today, but they have always existed. Historically, you might not find out about economic data or company specific news until you read about it in the newspaper the next day. Now everything happens in real-time- with a never-ending flow of pundits and articles ready to pontificate about what happened and how **it may** impact the markets. We caution our clients to not overreact to one data-point, piece of news, or what a so-called market authority might be predicting.

Our point with highlighting historical risks is not to say that investors should blindly put money into the market and pretend that risks don’t exist, but rather to point out that there are always risks and there is also a lot of noise. Each quarter we publish our own set of potential risks along with our **market outlook**. Our role at Winthrop Wealth Management is to help our clients identify and manage risk and navigate through the noise by providing a detailed financial plan combined with a structured, consistent, and repeatable investment process.

We consistently encourage our clients to maintain a long-term viewpoint while remaining focused on their overall goals and objectives. At Winthrop Wealth Management, financial planning works in concert with investment management. The Financial Plan, which helps clients define cash flow needs and future objectives, drives the investment management strategy. The investment management process is designed to provide well-diversified portfolios constructed with a methodology based on prudent risk management, asset allocation, and security selection. As always, please contact us if you have any updates to your personal or financial circumstances.

Reasons to Sell Stocks								
Year	Market Risk	Return	Year	Market Risk	Return	Year	Market Risk	Return
1968	USS Pueblo Seized	11.04%	1985	Economic Growth Slows	31.72%	2002	Recession	-22.10%
1969	Money Tightens - Markets Fall	-8.40%	1986	Dow Nears 2,000	18.67%	2003	War in Iraq	28.66%
1970	Vietnam War Spread	3.94%	1987	Record-Setting Market Decline	5.25%	2004	Rising Interest Rates	10.88%
1971	Wage Price Freeze	14.30%	1988	Election Year	16.61%	2005	Hurricane Katrina	4.91%
1972	Largest U.S. Trade Deficit Ever	19.00%	1989	October “Mini Crash”	31.67%	2006	Real Estate Peaks	15.78%
1973	Energy Crisis	-14.69%	1990	Persian Gulf Crisis	-3.18%	2007	Subprime Lending	5.57%
1974	Steepest Market Drop in Four Decades	-26.47%	1991	Berlin Wall Falls	30.40%	2008	Great Recession Begins	-37.00%
1975	Clouded Economic Prospects	37.23%	1992	Global Recession	7.62%	2009	Double Digit Unemployment Numbers	26.45%
1976	Economic Recovery Slows	23.93%	1993	Health Care Reform	10.07%	2010	European Sovereign Debt Crisis	15.06%
1977	Market Slumps	-7.16%	1994	Fed Raises Interest Rates Six Times	1.31%	2011	U.S. Credit Downgrade	2.11%
1978	Interest Rates Rise	6.57%	1995	Dow Tops 5,000	37.54%	2012	Afghanistan War	15.99%
1979	Oil Prices Skyrocket	18.61%	1996	Dow Tops 6,400	22.91%	2013	Fed Taper Tantrum	32.37%
1980	Interest Rates at All-Time High	32.50%	1997	Hong Kong Reverts to China	33.32%	2014	Oil Prices Plunge 50%	13.68%
1981	Steep Recession Begins	-4.92%	1998	Long Term Capital Mgmt Collapse	28.55%	2015	China Economic Slowdown	1.37%
1982	Worst Recession in 40 Years	21.55%	1999	Y2K	21.04%	2016	Global Economic Slowdown	11.95%
1983	Market Hits New Highs	22.56%	2000	Tech Bubble Burst	-9.10%	2017	High Valuation	21.82%
1984	Record Federal Deficits	6.27%	2001	9/11 Terrorist Attacks	-11.89%	2018	US/China Trade War - Fed Policy Mistake	-4.39%
1968 to 2018:								
Total Return: 11,774%.		Hypothetical Growth of \$10,000: \$1,177,000.		Total Annualized Return: +9.8%				

This is a hypothetical example and is not representative of any specific situation. Your results will vary. The hypothetical rates of return used do not reflect the deduction of fees and charges inherent to investing. SOURCE: BLOOMBERG

DISCLOSURES:

The economic forecasts set forth in this material may not develop as predicted and there can be no guarantee that strategies promoted will be successful. Content in this material is for general information only and not intended to provide specific advice or recommendations for any individual.

International investing involves special risks such as currency fluctuation and political instability and may not be suitable for all investors. These risks are often heightened for investments in emerging markets.

The fast price swings in commodities and currencies will result in significant volatility in an investor's holdings.

All indexes mentioned are unmanaged indexes which cannot be invested into directly. Unmanaged index returns do not reflect fees, expenses, or sales charges. Index performance is not indicative of the performance of any investment. Past performance is no guarantee of future results.

The Standard & Poor's 500 Index is a capitalization weighted index of 500 stocks designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries.

The S&P Midcap 400 Stock Index is an unmanaged index generally representative of the market for the stocks of mid-sized US companies.

The Russell 2000 Index is an unmanaged index generally representative of the 2,000 smallest companies in the Russell 3000 index, which represents approximately 10% of the total market capitalization of the Russell 3000 Index.

The 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.

The Bloomberg Barclays U.S. Aggregate Bond Index is an index of the U.S. investment-grade fixed-rate bond market, including both government and corporate bonds.

The Barclays Capital U.S. Credit Bond Index measures the performance of investment grade corporate debt and agency bonds that are dollar denominated and have a remaining maturity of greater than one year.

The Barclays Capital Municipal Bond Index is a broad market performance benchmark for the tax-exempt bond market, the bonds included in this index must have a minimum credit rating of at least Baa.

The Barclays Capital US Corporate High Yield Bond index is an index representative of the universe of fixed-rate, non-investment grade debt

The 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. The MSCI EAFE Index consists of the following developed country indices: Australia, Austria, Belgium, Denmark, Finland, France, Germany, Hong Kong, Ireland, Israel, Italy, Japan, the Netherlands, New Zealand, Norway, Portugal, Singapore, Spain, Sweden, Switzerland and the UK.

The MSCI Europe Index captures large and mid cap representation across 15 Developed Markets (DM) countries in Europe*. With 445 constituents, the index covers approximately 85% of the free float-adjusted market capitalization across the European Developed Markets equity universe.

The MSCI Japan Index is designed to measure the performance of the large and mid cap segments of the Japanese market. With 322 constituents, the index covers approximately 85% of the free float-adjusted market capitalization in Japan.

The MSCI EM (Emerging Markets) Index is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of the emerging market countries of the Americas, Europe, the Middle East, Africa and Asia. The MSCI EM Index consists of the following emerging market country indices: Brazil, Chile, Colombia, Mexico, Peru, Czech Republic, Egypt, Greece, Hungary, Poland, Qatar, Russia, South Africa, Turkey, United Arab Emirates, China, India, Indonesia, Korea, Malaysia, Philippines, Taiwan, and Thailand.

The Dow Jones Industrial Average is comprised of 30 stocks that are major factors in their industries and widely held by individuals and institutional investors.

The NASDAQ Composite Index measures all NASDAQ domestic and non-U.S. based common stocks listed on The NASDAQ Stock Market. The market value, the last sale price multiplied by total shares outstanding, is calculated throughout the trading day, and is related to the total value of the Index.

Investing involves risk including loss of principal. There is no guarantee that a diversified portfolio will enhance overall returns or outperform a non-diversified portfolio. Diversification does not protect against market risk.

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