Market & Investment Update

June 3, 2019

May proved to be an ugly month for stocks with the S&P 500 losing 6.4%, wiping out nearly half of the gains made thus far in 2019. Following the recent weakness, the S&P 500 is still up 10.7% year-to-date through May 31. However, the cumulative total return of the S&P 500 Index since the beginning of 2018 has only been 5.9%, with most of the return coming from dividends. Foreign developed and emerging market stocks have fared worse, facing meaningful losses as a result of a stronger US dollar, political issues (e.g., Brexit), escalating trade tensions, and slowing global growth. Bond investors have experienced only modest positive returns during this period given the low interest rate environment. Despite some positive returns earlier in 2019, when looking at the last year and half, overall returns have been relatively anemic.

Year-to-Date Returns (as of May 31, 2019)

Category	Representative Index	May 2019	YTD 2019	2018
US Large Cap Equity	S&P 500	-6.4%	10.7%	-4.4%
US Small Cap Equity	Russell 2000	-7.8%	9.3%	-11.0%
Foreign Developed Equity	MSCI EAFE	-4.8%	7.6%	-13.8%
Emerging Market Equity	MSCI Emerging Markets	-7.3%	4.1%	-14.6%
Real Estate	Dow Jones US Real Estate	0.0%	17.0%	-4.0%
US High Yield Fixed Income	ICE BofAML High Yield	-1.3%	7.5%	-2.3%
US Fixed Income	Barclays Aggregate Bond	1.8%	4.8%	0.0%
Cash Equivalents	ICE BofAML 3 Mo Deposit	0.2%	1.2%	2.1%

After almost a year-and-a-half of mostly sideways markets, a logical question might be: "Why haven't returns been higher?"

Last update, we noted that in our view, investors remain broadly focused on three primary factors:

1) Trade negotiations / tensions

> **Update:** after months of incrementally positive messaging from both with China and the U.S., it appeared we were on pace to have a historic trade deal finalized by the end of May. This progression took a serious stumble when President Trump surprised markets mid-May by accusing the Chinese of backing out of a deal and marching forward with tariffs. China responded with more forceful rhetoric by encouraging their people to stay strong during what could be an extended trade war, and externally blaming the U.S. for negotiating in bad faith and implying that China may cease export of critical rare

earth materials. Adding to this uncertainty, on May 30 Trump surprised markets with a tweet announcing 5% tariffs on imports from Mexico starting on June 10 as a result of border related concerns. We still believe that ultimately a deal with China will be reached and that the U.S. will work within the recently negotiated USMCA agreement in trade with Mexico. That said, given the increased uncertainty, we will not be surprised to see bouts of increased market volatility while these trade issues remain outstanding.

2) The actions and future rate direction of the Federal Reserve

Update: The Fed remains on hold. Despite stronger than expected first quarter GDP growth in the U.S., there has been no indication that the Federal Reserve has any appetite to increase rates in the near term. If anything, given the global trade uncertainty and increased tensions recently, markets are anticipating that the next move the Fed makes would be to cut rates, not raise again. We view the significant decline in long-term interest rates thus far in 2019 as supportive for many interest rate sensitive segments of the economy such as housing, automotive, and construction.

3) The health of corporate earnings and economic growth

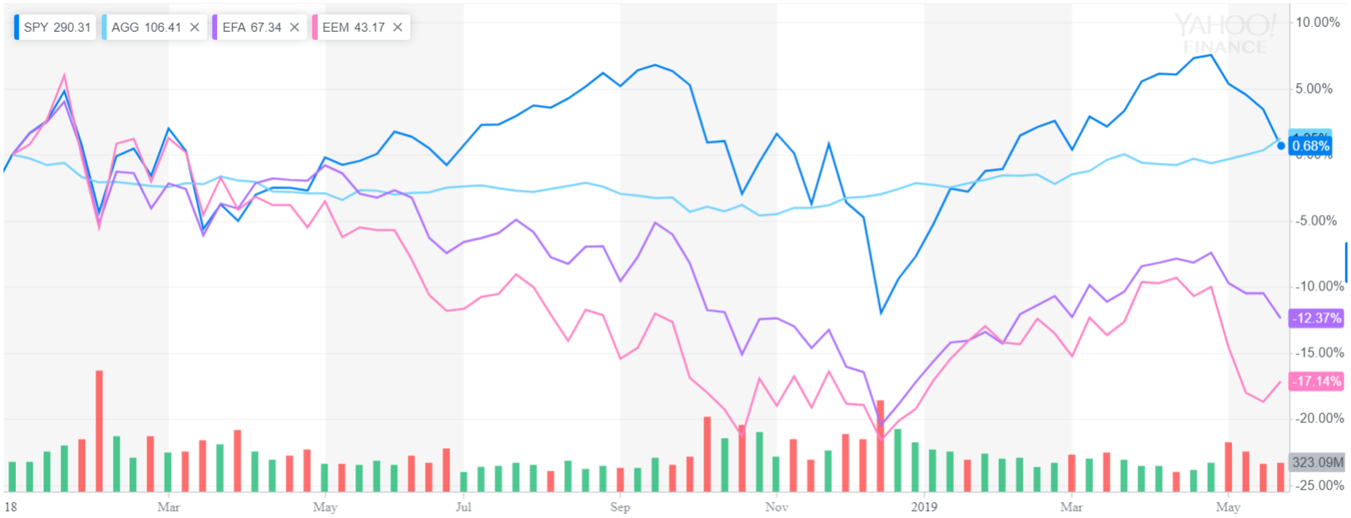
Update: as companies reported first quarter earnings in April and into May, the results were generally positive and not indicative of a looming recession. While we believe that most U.S. corporations are healthy and profitable, the longer uncertainty around trade issues persist, the greater the risk that companies will pull back on spending and investing which could dampen economic growth. Economically, the U.S. still appears to be healthy, although some parts of the world, particularly the Eurozone and China are seeing continued declines in growth rates.

To explain the sideways market over the last 17 months, we should also add corporate tax cuts to the equation. As of January 1, 2018, the US corporate tax rate was reduced from as high as 35 percent to a flat 21 percent. This led to very strong year-over-year earnings growth in 2018 and helped to justify higher prices paid by investors for earnings. By the first quarter of 2019, corporate tax cuts are now behind us (no longer contributing to earnings growth), leaving escalating trade tensions are the primary culprit of decreased investor enthusiasm.

What does all this mean for markets and portfolios going forward?

The bond market is clearly showing that investors are nervous about a future recession, and are rotating into bonds to lock-in higher yields today in anticipation of potential Fed rate cuts in the future. One of the more visible side effects of this uncertainty has been the collapse of 10-Year U.S. Treasury bond yields, which have declined from 3.2% in November 2018 to 2.1% at the end of May. As noted above, we feel that the US economy remains stable, but there is also risk that investors may not be sufficiently compensated given the uncertainties of potentially slowing global growth and escalating trade wars.

Although there are signs of slowing in parts of the U.S. economy and globally, the U.S. economy is still growing at a healthy pace. If there was a resolution on trade and a favorable end to Brexit, we would expect markets to rebound. We are long-term investors and focus on the value and quality of our portfolios.



Price returns for key ETFs from December 31, 2017 through May 31, 2019. SPY is the iShares S&P 500 Index ETF, AGG is the iShares Bloomberg Barclays Aggregate Bond ETF, EFA is the iShares MSCI EAFE ETF, and EEM is the iShares MSCI Emerging Markets ETF.

Prices (as of May 31, 2019)

Representative Index	Current	Year-End 2018
S&P 500	2,752	2,507
Dow Jones Industrial Avg.	24,815	23,327
NASDAQ	7,453	6,635
Crude Oil	$53.36	$46.49
Gold	$1,310	$1,291
2 Year Treasury	1.95%	2.48%
10 Year Treasury	2.14%	2.69%
30 Year Treasury	2.6%	3.02%

Source: Morningstar, Bloomberg, US Treasury (total returns shown gross of fees)

Past performance may not be representative of future results. All investments are subject to loss. Forecasts regarding the market or economy are subject to a wide range of possible outcomes. The views presented in this market update may prove to be inaccurate for a variety of factors. These views are as of June 3, 2019 and are subject to change based on changes in fundamental economic or market-related data. Please contact your Financial Advisor in order to complete an updated risk assessment to ensure that your investment allocation is appropriate.