25 NORTH MARKET STREET, SUITE 223
JACKSONVILLE, FL 32202
904-674-3353

SALVUS
WEALTH MANAGEMENT

1040 BROAD STREET, SUITE 203
SHREWSBURY, NJ 07702
732-542-2629

January 14, 2019

Dear Clients and Friends,

"Smart is when you believe half of what you hear. Brilliant is when you know which half."
— *Robert Orben*

Despite some typical consternation and uncertainty, the markets were rolling along quite nicely during 2018 until the month of October began. It seems hard to remember right now, but the S&P 500 had a positive return of approximately 10.5% on September 30, 2018. October followed with generally negative stock market performance while November reversed course again with positive returns. Then we witnessed a bizarre December that contained both the largest one-day point gain in the history of the Dow Jones Industrial Average and the worst S&P 500 performance for the month of December since the Great Depression. At the close of the year, the S&P 500 declined 13.5% during the fourth quarter and finished the full year down 4.4%.

The carnage in the markets during 2018 was not limited to the United States and, in fact, was worse across the International markets. European and Asian markets averaged losses of over 14% while emerging markets declined nearly 15%. Long maturity, high-yield and emerging market bonds also experienced losses during the year. In other words, there were very few places to hide last year outside of short-term bonds and cash (two themes we will be mentioning later in this letter).

As usual, the markets and economy are a good news/bad news story depending upon which data points investors are evaluating. On the positive side, January began with a sensational employment and wages report as non-farm payrolls surged by 312,000, wages advanced by 3.2% and 419,000 new workers entered the labor force, all of which surprised the consensus opinions of most economists. Both the economy (as measured by GDP) and corporate profits are expected to continue steady growth in 2019, albeit at a slower pace than the previous year. Additionally, the Federal Reserve made clear that the pace of interest rate increases looks to slow this year after multiple increases in 2018. One other very important positive point is that the sharp drop in the markets at the end of last year has brought equity valuations back down to reasonable levels where the future probability of higher returns has increased.

Taking a look at negative signs that exist today, investors can point to a general slowdown in growth both in the United States and across the globe. Feeding into this concern, trade issues and tariffs are certainly contributing to the slowing growth along with the continuing saga of political infighting in D.C., across Europe and other parts of the world. A "long-in-the-tooth" bull market and rising deficits and debt are also weighing on the minds of investors as we begin the new year.

So there you have it – good news/bad new or is the glass half empty or half full? There is always a myriad of data points to consider when trying to assess the future direction of the economy and the markets and 2019 looks no different. As you read the quote at the top of the page by writer and comedian Robert Orben, it is very difficult to filter through all of the information that bombards us on a daily basis and determine what to really pay attention to and what to actually believe. This era of competing media narratives and potential fake news can make it a challenge to determine what is fact and what is opinion. Perhaps a remedy is to take in all current information with a grain of salt while staying focused on the long-term view which lessons the impact of short-term reactions.

One other point that we would like to make as we close the books on a volatile last couple of months in the markets, is a view that we have regarding how to best manage your portfolios through difficult markets. No doubt, you have heard us mention that a long-term time horizon is an investor's best friend and an antidote to short-term market volatility. It is entirely logical that short-term gyrations in the markets, no matter how sudden and deep, can be smoothed out over time. After a few years of positive portfolio growth, most investors can shrug off short-term market declines that occurred months or years earlier.

However, those investors who have short-term time horizons or are relying upon their portfolios for current income may not have the same luxury of time healing portfolio losses. Before we go any further with this thought, we should first point out that investors with a time horizon under three years are not really investors, but should be considered to be savers. In our view, investors can stomach markets swings and should have exposure to the equity markets, while savers cannot endure volatility and should have their funds entirely in cash or short-term fixed income instruments.

So how should investors who need regular income from their portfolio position themselves to better endure volatile markets? This is an age old question for advisors and one in which we have some thoughts. It is a given (not fake news) that equities provide the greatest long-term return to investors. Depending upon what time frame you look at, equities have returned 8% - 10% on average, while bonds closer to 5% and cash around 3%. We obviously believe that investors should keep as much of their long-term capital invested in equities as possible. However, we do not want to harm a client's portfolio by being forced to liquidate stocks during a market decline in order to provide income. This could result in unnecessary trading costs and trigger a taxable event.

Instead, consider an alternate portfolio management technique: We work with a client to determine their upcoming 12 months of cash/income needs. We then set aside a full years' worth of cash and keep it liquid and away from market volatility. These funds are then periodically transferred to the client's bank account to be used for their cash needs. During the course of the year, we opportunistically take some gains away from the equity portfolio to replace the cash that is being depleted. For clients who have enough capital available, we may look to set aside a full three years' worth of cash by keeping the funds in a combination of short-term bonds and money market accounts, now that yields have risen to around 2% - 3%.

We would compare and contrast our above strategy with that of another strategy that many try to utilize – market timing. Instead of staying invested and keeping enough cash on hand to cover upcoming expenses, many try to forecast volatility and move in and out of the market to avoid losses or generate needed cash. We have talked much in the past about how we avoid this thinking as we believe that it not only creates a lot of unnecessary costs from buying and selling and generating taxes, we also believe that it is also nearly impossible to consistently time the market correctly over long periods of time. We choose instead to maintain a long-term approach to investing while making certain to best accommodate our clients' short-term income needs.

We look forward to seeing many of you over the coming months so that we can review your portfolio and discuss your individual needs. Until then, we thank you for your continued support and wish for a happy, healthy and prosperous new year for us all.

Best regards,

Bob

Robert W. Joel, CFP
Chief Investment Officer
Salvus Wealth Management

Chuck

Charles T. Woolston, CPA
Chief Executive Officer
Salvus Wealth Management