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QUARTERLY MARKETREVIEW

WINTER 2019

In this issue:

- Market Volatility in 2018
- Driving Forces Behind Market Moves
- Fundamental Data Points in Review
- Moving Forward

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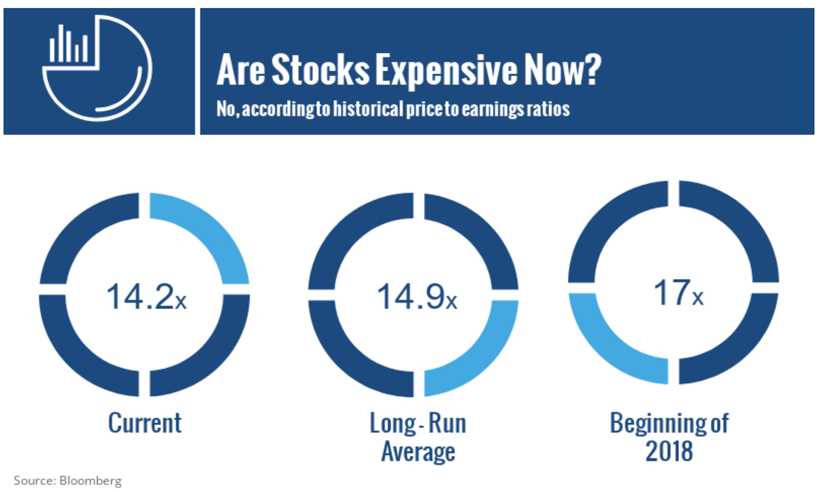
The markets did their best Ebenezer Scrooge impression in response to the traditional holiday well-wishes that accompany the month of December; Bah Humbug!!! December has historically been the strongest month of the year. Don't cast your well-wishes here as 2018 was the worst December for markets since 1931, and overall the worst year for markets in a decade. Bah Humbug indeed.

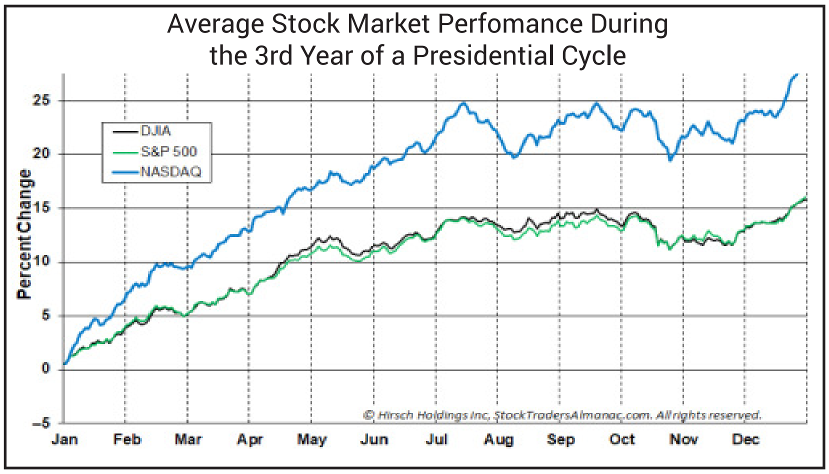
We will take this as our first chance to put things in to perspective beyond what happened during the last month, trading day, or 20 seconds. We know focusing on the long-term is out of vogue in our modern world of tweets, insta-analysis, and I want it now, now, now neurosis. However, those focused on the long-term instead of reacting emotionally to short-term issues will continue to be rewarded for their good-stewardship.



In 1931, the unemployment rate was nearly 25% and the global economy was in such shambles that despots the likes of Hitler were on the brink of gaining power. In 2018, the unemployment rate is at a 50-year low, and the global economy continues to expand. Regarding 2018 being the worst for markets in 10-years, that is unfortunately true. However, we've closed the books on the year and the US stock indexes are down approximately 5%. In 2008, the same indexes were down nearly 40%! The point of this reflection is not to have some Ebenezer Scrooge type epiphany, but rather to emphasize a tried and true market fact. A well-diversified portfolio based upon its unique risk tolerance and time horizon continues to be the only prudent form of investment management. Responding emotionally to market events has a nearly 100% track-record of failure. We do not like those odds. We do not like the weak returns of 2018 either – but catastrophe, calamity, and cataclysm (we've used up all the bad words we know that start with "C") was not in the cards for those that kept calm and carried on.

Twice during the year markets experienced a correction of over 10%. On Christmas eve the markets closed within a wink of officially hitting bear market status – defined as a 20% or greater pullback from recent market highs – before rebounding through the end of the year. Thus, the longest bull market in our great nation's history marches on. To be honest, we would have liked to see this dubious threshold breached just so we could stop hearing the echoing calls of "how much longer can this bull market last?". That's essentially the same question as someone asking us how much longer we have to live. We don't know; hopefully a long, long time. We don't think we're going to die tomorrow, but we can't be sure. On that somewhat macabre note, why don't we all make a new year's resolution to take our vitamins, wear our seatbelts, and go see the doctor. The only three guaranteed pieces of good advice in this entire note.

Back to the markets, the volatility of 2018 seemed awe-inspiring at times. Amazingly, the markets saw the largest one-day point drop (February) and point gain (December) ever! Over a thousand point move for the first time, both up and down, for the Dow Jones Index. Interesting times we live in indeed. Again though, putting things in perspective, we live in a world of percentages and absolute point swings can be distorted by the force of big numbers. For example, on that darkest of days in February when the Dow Jones was down over a thousand points, that represented approximately a 4% decline. For those of us that can remember Black Monday in 1987, the total point drop was half that amount but it represented a 27% decline! The volatility of 2018 seemed severe, but it really was a return to the normal. Recent years have borne witness to some eerily calm markets. 2017 was actually the least volatile year for the markets since 1964. That was the year the Beatles played Ed Sullivan and calls from a pay phone cost 10 cents. Who would have thought at the time the Beatles had more staying power than pay phones?



So, 2018 was not that terrible or abnormal after all, but it still did not feel good. So what happened? In our opinion, geo-political noise was the driving force behind the wild swings of 2018. Tensions with China over trade, allegations of election improprieties, the British exiting the European Union, and government shutdowns were only a few of the neck-snapping headlines. Fortunately, geopolitical noise has historically had very little staying power. While most of the political headlines have been negative we will throw another one in. We are entering the third year of a Presidential cycle and historically the third year of a Presidential term has been the strongest for markets. We believe this political data is just as useless as the other geo-political headlines out there in effectively navigating markets, but we thought it would be nice to at least add some positivity to the otherwise universal chorus of negativity.

Eventually the fundamentals will prevail over the noise and those fundamentals are still signaling no immediate economic abyss ahead. For example, the market for jobs continues to be quite strong. For the first-time in history, there are 7 million unfilled jobs in the American marketplace. Actually, the amazing part is that juxtaposed against these 7 million openings, there are currently only 6 million Americans looking for employment. This lack of qualified job candidates can create its own set of problems, but not the kind that lead to economic calamity. In addition, total GDP growth continues to expand between 2.5%-3.5% annually and overall stock valuations - as graphed – are below long-term averages. Specifically, since 1990, the average price to earnings ratio for stocks has been 14.9 while the current ratio sits at 14.2. The point is that the stock market is no longer expensive from a historical standpoint, as it was when we entered 2018. Beyond more attractive values, one of the few other beneficial elements of volatile markets is the fact that euphoria and irrational enthusiasm are dismembered. We would actually be far more concerned over the future direction of markets if we had witnessed another lurch higher in 2018, as we've experienced over the last few years. Markets never have and never will die of old age. Markets collapse when people think the good times will never end – think housing in 2008, the infancy of the internet-age in 2000, or any other crisis throughout the history of markets. When cavemen figured out fire – which generated some irrational excitement it is safe to assume – they probably got burned in multiple capacities. Our internal investment committee, as always, is analyzing markets and the economy exhaustively to uncover potential excesses forming. We just don't see any bubbles ballooning out there that could swamp the economy at the moment.

Unfortunately, the worst kind of pain comes from being blind-sided (when something occurs that so-called "experts" like ourselves believe isn't possible). The Titanic was considered unsinkable until it hit that iceberg. Our goal and responsibility is to never be blind-sided. That's why our strategies are designed to be "all-weather" in nature (appropriate on a risk-adjusted basis for each individual mandate regardless of whether market skies are sunny or stormy). Things are rarely as good or as bad as they seem. Over-pessimism now would be just as ill-advised as much of the irrational optimism coming in to 2018 we cautioned against. After markets spiked higher in 2017 we locked in those gains. This rebalance positioned our strategies well to take advantage of the volatility that presented itself in late January and early February of 2018. As markets rebounded in to the summer we again avoided the temptation to be greedy and reduced risk accordingly. With the onset of the most current bout of market turbulence, we again added exposure on a risk-appropriate basis to assets we believe to be attractively valued for future gains. Fundamentals instead of fear or greed – the twin evils of all decision-making – will continue to drive all our investment decisions made on your behalf. Just like old Mr. Bah Humbug himself, we cannot control what the ghost of markets futures brings to us, but we can control how we respond.

As always, thank you for your continued trust, confidence, and support in our investment process, long-term strategy and constant vigilance. Have a safe and prosperous new year.