the financial planner

GOLDMAN LANCASTER, INC.
REGISTERED INVESTMENT ADVISOR

Winter 2019

The Markets

It has been long said that all things must come to an end. And so it was for the S&P 500 stock index's nine year winning streak. Stock markets around the world suffered a severe correction in the 4th quarter, causing the index to end the year with a negative total return for the first time since 2008 (at -4.4%). The positive run from 2009-2017 thus ends in a tie with 1991-1999 for the longest positive streak in the history of the index. That it would finish the year negative was far from a foregone conclusion just three months before…at the close on September 20, the S&P 500 was sitting at an all-time high, and up 11% on the year. Over the next 3 months, it would give back all of those gains and more, with a peak-to-trough decline of over 20%. And December was exceedingly ugly. On Christmas Eve, the S&P was down 14.8% in December alone, on track for the worst December, ever. A post-Christmas bounce softened the blow somewhat, but the damage was done. By New Year's Eve, the S&P 500 sat at -9% for the month, marking the largest monthly index decline since February 2009, and the worst December since 1931.

Why did stocks drop? Take your pick: rising interest rates, global economic slowdown, worsening trade war, weakness in housing and auto sales, mid-term election results, etc. For what it's worth, we think that the market's behavior in January goes a long way toward identifying the most powerful driver of recent market volatility.

Just a week after the market's peak on September 20th, the Federal Reserve, continued on a clearly articulated and dedicated path of action, and voted to raise short-term interest rates by ¼ point. In early October, Jay Powell reiterated the hawkish view; openly stating that in his opinion, the Fed was still a "far ways away" from a "neutral rate", and that it would likely have to go beyond neutral in order to assure that inflation would not awaken from its slumber and wreak havoc on the citizenry. Judging by October's sharp decline across virtually all risk-assets, market participants didn't like the message, and

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What's New?

Tax time! For those expecting LPL 1099 forms, the first wave will be sent out by February 15th. LPL will hold off sending final 1099's for accounts which hold positions for which LPL considers it likely that the investment sponsor may send corrected data to them after this date. Subsequent mailings will go out March 1st and 15th. Check with us if you want a better idea of when to expect yours.

Interest Rate Update

From Barron's 2/5/2019	Now	1 Yr Ago
Prime Rate	5.50%	4.50%
3-Month T-Bill Rate	2.42%	1.53%
5 Year CD - National Avg.	2.04%	1.55%
Fannie Mae 30 Yr. Fixed Conventional Mortgage	4.46%	4.22%

Financial Markets Scoreboard

Index Returns *(Through 12/31/2018)*	***4th Quarter***	***2018***
Dow Jones Industrials	*-11.31%*	*-3.48%*
Standard & Poors 500	*-13.52%*	*-4.38%*
M.S. EAFE (Developed Markets Foreign Stocks)	*-12.50%*	*-13.36%*
M.S. EM Free (Emerging Markets Stocks)	*-7.40%*	*-14.25%*
Barclay's Capital U.S. Aggregate Bond	*+1.64%*	*+0.01%*
Barclay's Capital US Corporate High Yield Bond	*-4.53%*	*-2.08%*

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THE PERSPECTIVE PAGE
INTRA-YEAR DECLINES

In 2017 the stock market could have been described as "calm, cool and collected." In 2018, a better descriptor might be "wild and crazy."

In point of fact, many investors were spoiled by the unusual calm of markets in 2017...steady gains with very few interruptions, and with those that did occur proving to be very mild by historical standards.

2018, with two distinct and violent downdrafts, saw volatility return to levels seen more frequently in recent history. On the one hand, we can say that after a long period of unusual calm, the storm appears more violent. On the other hand, the volatility investors endured in the 4th quarter registers closer to the high end of the range seen over the last 40 years, than it does to the low end of that range.

Consider the graph below as case in point. The graph shows the total gain or loss registered by the S&P 500 index each calendar year, from 1980 to 2018, measured by the grey bars. The red dots, meanwhile, measure the largest peak to trough decline seen by the index during each calendar year.

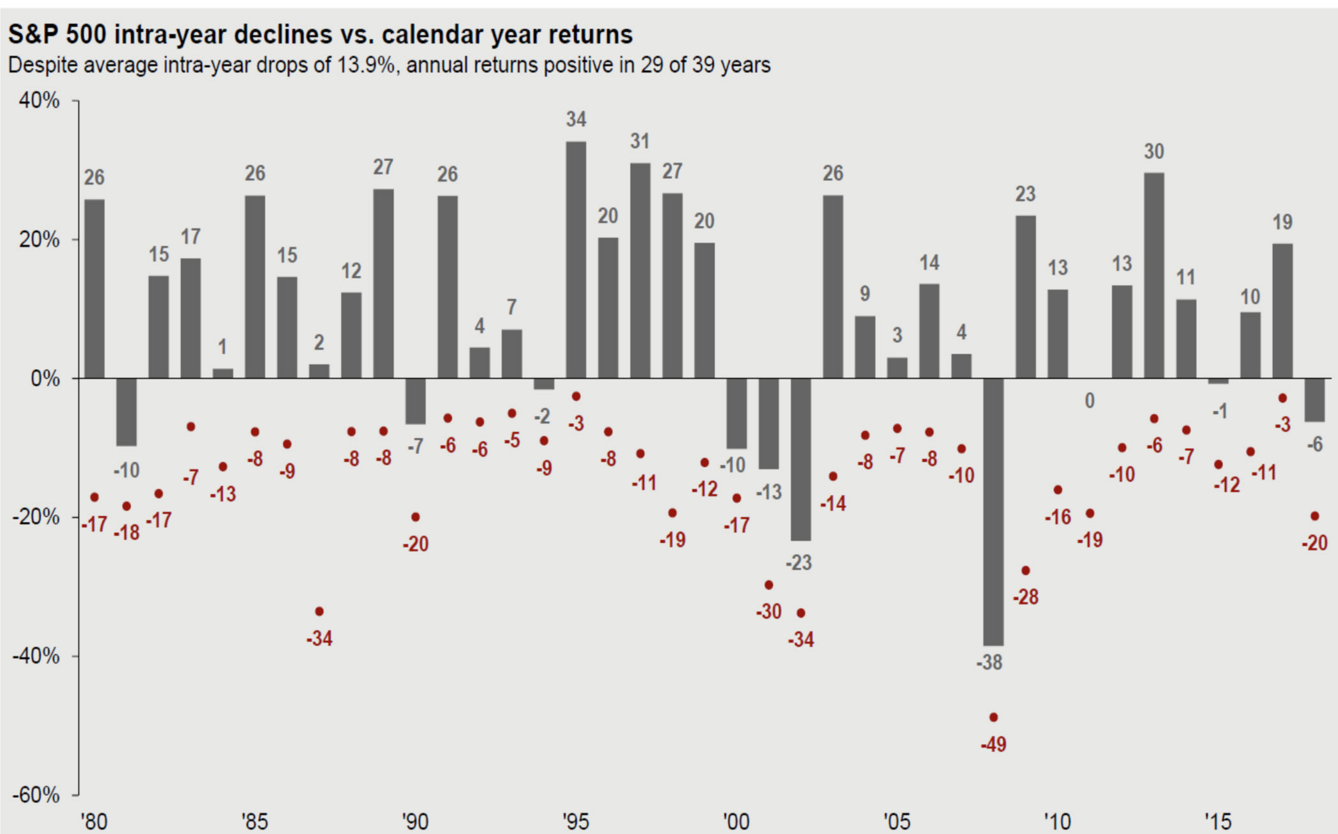
The takeaways are that:

Declines are very common and most often prove to be transitory in nature.

It is rare to go through an entire calendar year without a peak-to-trough decline of high single digits or greater.

The index has had far more positive years than negative years over the time period examined.

2018 was the worst year for the index since 2008.



Source: FactSet, Standard & Poor's, J.P. Morgan Asset Management.
Returns are based on price index only and do not include dividends. Intra-year drops refers to the largest market drops from a peak to a trough during the year. For illustrative purposes only. Returns shown are calendar year returns from 1980 to 2018, over which time period the average annual return was 8.4%.
Guide to the Markets – U.S. Data are as of December 31, 2018.

J.P.Morgan Asset Management

***Markets** (Continued from page 1)*

nor did the Commander-in-Chief, who began a Twitter assault on the Fed Chair. Meanwhile, as the market indices topped out and began to wane, in October we saw the 10-Year US Treasury Bond yield make an upward assault on 3.25%, only to reverse course and fall all the way to 2.75% by Christmas, as a slew of economic reports came in below forecasts, the price of oil collapsed from $75 to $43, and a souring outlook for corporate earnings took hold. The Fed met again on December 18-19, and because the move was telegraphed, and maybe also because Fed officials felt it critical to maintain their air of independence, they raised rates by another ¼ point, although this time, they did modestly scale back plans for additional rate increases in 2019. Still, pessimism prevailed as the calendar turned, and the market dropped by over 2% on January 3rd, as Apple warned that it had suddenly become much harder to sell their phones in China.

Then, on January 4th, Chairman Powell spoke on a panel in Atlanta, and he stated that the Fed was hitting the pause button and was no longer married to the idea of more rate increases in 2019. Further, he said the Fed would continue to watch developments and respond as necessary; not just economic developments, but market developments too. This was a significant shift from a man who had on many previous occasions stated that the Fed shouldn't be overly concerned about stock prices. Well, that day was a huge up day for stocks, and was followed by mostly up days since, such that the S&P 500 turned in its best January since 1987; this even though January did not bring with it marked improvements in economic reports, trade relations or corporate earnings. It seems that the only thing that changed was the tone of the Fed. How's that for cause and effect?

We have for some time questioned whether the US (and for that matter the global) economy will have the ability to handle "normal" interest rates. This is because there is so much more debt on the books now, across governments, corporations and individuals, compared to the size of the economies in which all exist. It's one thing to carry massive debt at interest rates close to zero, but another altogether when rates rise significantly. And so over the back half of 2018 we were not too surprised to see weaker home and auto sales as higher rates set in, pushing up the price of mortgage debt and car loans. Granted, we're talking higher, not high, at least by the standards those of us north of age 50 have experienced in our lifetimes!

Consider that we have just completed a decade where the Federal funds rate averaged 0.4% and the 10-year T-note yield averaged 2.5%, the lowest such measures for any 10-year period since the WWII era. Yet, real GDP growth averaged just 1.8% per year through this period. That is all the most accommodative interest rate structure in modern history could manage to deliver in terms of economic growth. The closest we ever came to this type of interest rate environment was the 1954-64 period — and in that ten-year phase, real GDP growth averaged 4.0%. So what's the difference, say, outside of aging demographics? In one word - debt. There's far too much of it. In that 1954-64 era, the level of household, business and government debt relative to GDP averaged 140%. This time around, that all-in debt ratio has been 330%. This is the pervasive constraint on the economy and why it is that even moderate increases in interest rates are so hard to digest.

We really don't know for sure, but the question which we expect to see answered in 2019 is, did the Fed go too far? The fall in longer term interest rates over the last couple months could provide a significant palliative effect to the economy, and a drop in pressure on trade issues would also likely help both the earnings outlook for corporate America and economies abroad.

We're also watching the Fed's decisions regarding the trillions in bonds it still holds on its balance sheet, the product of a years-long bond buying campaign called "quantitative easing." A slow unwind is well under way, referred to in some circles as "quantitative tightening" - and the exact effect can't be known. But for those of us who thought the build-up lifted prices, it would be illogical to assume that the wind-down can't have the opposite effect. We think "dovish" comments from Chairman Powell on this topic have also been important triggers in bringing January buyers back to Wall Street. "QT" will continue in 2019, unless and until the economy or market head south, and will occur against a backdrop of massive debt issuance by the Federal government, which, regardless of party, seems to have zero regard for fiscal restraint. By its own estimates it is expected to run a budget deficit of nearly $1 trillion in the coming fiscal year, even in the face of an expanding economy. We continue to favor a guarded approach.

Mike's Corner

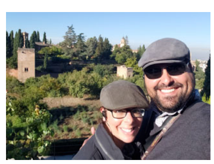
As you may know, Laurel and I were married in April 2018 in an intimate ceremony in Santa Barbara wine country. We waited a few months to take a honeymoon, and in October we headed to Spain, where, over the course of three weeks, we saw much of the country. We chose to drive most of the trip so we could take in as much of the country as possible and discover smaller cities off the beaten path. Recounting every spectacular detail of the places we stayed, things we saw and food we ate would fill a book, so I won't do that here. I will, however, tell you about some of our favorite spots and those we know we want to revisit someday.

We started and ended our trip in Barcelona, a magical city full of surreal architecture and local pride, not to mention world-class cultural experiences and food. Highlights of our time there included a flamenco guitar performance at the breathtaking Palau de la Musica Catalan, and mouthwatering meals at two of our favorite restaurants in all of Spain – Cal Pep and El Passadis del Pep.

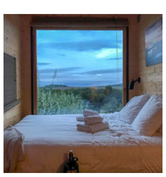
After Barcelona, we headed to Valladolid, a city just northwest of Madrid and about 30 minutes from the small town of La Seca, where my paternal grandfather was born. My parents and siblings actually joined us for this part of our trip, which was incredible. Prior to leaving the United States, we contacted some distant cousins in Valladolid, who not only offered to show us around but even arranged a family reunion of sorts. Twenty-one family members from all over Spain joined us for lunch and a tour of the church where my grandfather was baptized. Though I had never been to Spain before, let alone La Seca, it was like coming home, and I will never forget how special that felt.

Laurel and I then headed north while my parents and siblings headed south. We stopped to taste some wine (of course) in one of our new favorite wine regions, Ribera del Duero, where some of the country's most spectacular red wines are made. We then explored the Basque coast from San Sebastian all the way to Bilbao. We ate more than our share of delicious pintxos (small plates), marveled at the rugged beauty of the northern coast, and walked aimlessly around beautiful Bilbao, hopping from one pintxo bar to the next all night before heading back to our honeymoon suite overlooking the spectacular Guggenheim Museum. To be sure, Basque Country is definitely on our list of places we'll return someday.

After Basque country it was time to head south. We started in Seville, where we explored the ancient Moorish Alcazar and took a peaceful horseback ride through olive orchards before exploring the Sherry Triangle, the Pueblos Blancos in the Andalucian mountains, Ernest Hemmingway and Orson Welles' old stomping grounds of Ronda, and the beautiful seaside town of Malaga. We continued north along the coast before jogging inland to Granada, one of our other favorite cities, where we enjoyed dinner and a flamenco show in a cave built into the hillside and took a fantastic guided tour of the ancient Alhambra – an absolute must-see.



After two and a half weeks of being on the go, our final stop was a relaxing couple of days in the Penedes wine region just outside of Barcelona. We rented a "tiny house" that was situated in the middle of an ancient vineyard owned by a fantastic cava winery called ArtCava. We drank cava to our hearts' content and woke every day to an unobstructed view of the Montserrat mountains in the distance. It was nothing short of the perfect way to end our trip.



In short, we packed a lot into three short weeks but know that there is so much we didn't have time to see. I guess we'll just have to go back!

THANK YOU!

...to the following clients and colleagues for showing your confidence in me by referring your friends, family members, associates and clients to me during the last three months…

Charlie Scott,
Cecilia Larios,
&
Kevin Alcaino

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