# GBA Financial

**Monthly Newsletter**

**January 2019**

## COMMENTARY

2018 started off on fire with January with markets exploding to the upside and because of this, we anticipated a correction which we saw play out over the next few months. We remained bullish and looked for the S&P 500 to make new all-time highs around the 4th quarter and were looking spot on at the end of September but the failed breakout in October created significant technical damage resulting in a quick selloff. Support levels looked to be created in November but were broken during December. The market moved down very quickly and the result was the end of one of the longest bull markets we have experienced. A relief rally took place late in the year from oversold levels, but now investors are questioning what's next?

**2019 Outlook -** Our base case is for equities to comeback down and form a double bottom before moving higher. We suspect 2019 will be a bumpy ride and the first quarter will be very telling for the remaining part of the year. March could provide multiple catalysts for bulls and bears: deadline for U.S. and China trade talks, Federal Reserve meeting, and UK leaving the EU (Brexit). Weaker economic data could change our view relatively quickly, but as it stands now, the possibility of a recession seems unlikely. Our 2019 year end S&P 500 target is 2800 (+11.7%).

If our base case scenario seems too optimistic, we understand. The financial media likes to hammer out negative stories as a negative headline generates more "clicks" (revenue from clicks). With that said, we do recognize the market is in a precarious position. Passive indexes and algorithm trading has been fueling much of the recent selling and we may have yet another leg down before this shakeout is over. If corporate earnings falter, the Fed tightens too much, and/or trade wars intensify we could see the market selloff drastically.

Valuations look attractive for equities as the S&P 500 pulled back 20.2% (high on September 21st of 2,940.91 to the low on December 24th 2,351.10) from peak to trough. The third year of a presidential term is typically the strongest year out of the four year term and with multiple catalysts early in the year, we could see a market repeat similar to 2016. In 2016 the markets were able to find a bottom early in the year (as did oil) before moving higher and ultimately having a total return of 11.96% on the S&P 500 total return index (January 4, 2016 open of 2012.66 and December 31, 2016 close of 2238.83).

We have focused mostly on domestic equities as we believe the U.S. market is going to be the primary driver coming out of this bear market. When domestic equities started to diverge from international equities, we were looking for domestic equities to pull international equities up and not the other way around. Emerging Markets seem to have made a bottom and are showing early signs of out-performance versus domestic equities.

## ECONOMIC HIGHLIGHTS

| | |
|---|---|
| **S&P 500** | 2,506.85 |
| **DJIA** | 23,327.46 |
| **NASDAQ** | 6,635.28 |
| **OIL** | $45.41/barrel |
| **GOLD** | $1,281.30/ounce |
| **10-YEAR TREASURY YIELD** | 2.69% |
| **UNEMPLOYMENT** | 3.7% |
| **GDP** | 3.4% (Q3 3rd estimate) |
| **CONSUMER PRICE INDEX (CPI)** | +0.0% (12 month change: +2.2%) |
| **CORE CPI** | +0.2% (12 month change: +2.2%) |

**Bull Case (25%)** – A change in tone from the Fed (from Hawkish to Dovish), a trade agreement with China, and starting point for the year that is relatively low could make 2019 look really good when we get to the end of the year.

**Base Case (50%)** – More than likely the market needs more time while creating a bottom before moving higher. We think the first quarter will be choppy and could provide the final shakeout before we see a new uptrend start.

**Bear Case (25%)** – We do see a scenario where the Fed needs to tighten more and faster than what is currently estimated. That, plus the possibility of an ongoing trade war and slowing economy may keep a lid on the global market.

Although we stated the U.S. market is going to be the primary driver of the global recovery, we think emerging markets has the highest upside in 2019 with valuation levels even more attractive than the U.S.

What will the Fed do in 2019? First off, we think the Fed has done a superb job since the 2008 Financial Crisis propelling the economy out of the great recession. But this may be one of the tougher spots the Fed is in – raising rates too much will almost certainly bring the economy into a recession, but not raising rates at all may signal the economy is much weaker than most think. Current probabilities indicate the Fed Target rate to be unchanged by December 2019. It's hard to see the Fed not raising rates at all, but we've changed our initial prediction for 2019 and have come down from three rate hikes to one rate hike.

**MARKET TRACKER**

| Index | 3 Mo | 1 Yr | 3 Yr | 5 Yr |
|---|---|---|---|---|
| S & P 500 | -13.52 | -4.38 | 9.26 | 8.49 |
| MSCI EAFE | -12.54 | -13.79 | 2.87 | 0.53 |
| BARCAP AGG BOND | 1.64 | 0.01 | 2.06 | 2.52 |

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*The MSCI Emerging Markets Index Designed to measure equity market performance in global emerging markets. It is a float-adjusted market capitalization index.*

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*The Bloomberg Barclays Capital U.S. Aggregate Bond Index is a broad-based flagship benchmark that measures the investment grade, US dollar-denominated, fixed-rate taxable bond market. This unhedged index was created in 1986.*

*The MSCI EAFE Index was created by Morgan Stanley Capital International (MSCI) that serves as a benchmark of the performance in major international equity markets as represented by 21 major MSCI indexes from Europe, Australia and Southeast Asia.*