Glen Eagle
Faith Family Firm®

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Investment Commentary

As we pack up holiday decorations and put away the champagne glasses from New Year's, we are often inclined to reminisce on the past year…and what a year it was. President Trump met with the North Korean leader Kim Jong Un, fires and hurricanes ravaged California and North Carolina, midterm elections led to a split congress, a Supreme Court Justice become the figure of fierce debate, an American actress married into the British Royal Family, and the US Olympic Team brought home 23 medals from the games in South Korea…just to name a few.

The financial markets also gave us plenty to observe in 2018. Heading into October, the S&P500 was up over 8%. Yet October kicked off one of the worst months since The Great Recession, leading the market to give up all of its previous gains to end the year with a loss of over 6.5%. To understand this recent volatility, let's look at what we see as the root causes of these extreme market moves and where that leaves investors going forward:

Factors Affecting the Market in 2018

- **Tariffs** – In part, the market volatility has correlated with the rise and fall of the emotional state of investors watching the China-US tariff "negotiation process," For example, in December we saw the stock market jump on presumed tariff truce talks between President Trump and President Xi Jinping at their meeting in Buenos Aires, but then subsequently fall by even more than it gained as it became clear after the meeting that the two leaders had failed to walk away with the same vision for tangible next steps.
- **International Markets** – Once again, the US stood out as the best house in a bad neighborhood. In part this was because institutional investors started to avoid emerging markets which will need to make payments on roughly $249 billion of US denominated debt in 2019. Over the past year, this burden on emerging markets has become even heavier as the US dollar has continued to rise, making it harder for these governments to pay back loans using their less-valuable local currencies. To further the plight of international markets, the pace at which investors withdrew capital increased as Italy elected a populist government, Venezuela continued falling into political chaos, and the Middle East power-dynamics became a little more unstable when it became evident that Saudi Arabia's Crown Prince could be connected to the murder of a journalist in Turkey.
- **China** – While it could be argued that China should be included in the above bullet point, we believe it warrants emphasis given that it now accounts for 18.7% of the world's GDP and remains the largest exporting country. Consequently, as news that China's economy has slowed down and is now growing at an annual rate of just 6.5% (compared to its breakneck growth rates in the early 2000's) investors became worried, leading the Chinese stock market to drop by 28%.[1] While the Chinese government has tried to spur further growth by encouraging banks to lend more, investors remain extremely cautious, particularly in light of the still-unresolved trade negotiations with the US.

- **Decrease in Liquidity** – In order to spur this country out of The Great Recession, the Federal Reserve lowered interest rates and pumped roughly $4 trillion into the economy beginning in 2008. These actions were two of the main catalysts for the bull market that we have been experiencing for over 9 years. In particular, lowering interest rates both reduced the risk of borrowing, allowing businesses and individuals alike to pursue investments that otherwise would have been too costly, and encouraged people to invest in the stock market, where they were likely to earn a much higher return than in their bank accounts. As the Federal Reserve has been slowly unwinding this policy by raising interest rates and reducing the money they are putting into the economy, investors have become concerned that this will lead to an economic slowdown inducing some to fear the worst and start selling their investments.

Looking Forward to 2019

- **Focus on Value** – As a whole, we believe that 2019 will be a positive year for the stock market. Our view is driven by current valuations and the strength of the underlying US economy. The significant stock market drop in the fourth quarter has made the valuation of many companies much more appealing. For example, the S&P500 Forward PE (a ratio that indicates how expensive the index is) has dropped by -11.62% since one year ago despite the fact that corporate earnings increased in 2018 and are expected to grow further in 2019.[2] As a result, we believe that many companies have seen their stock price dragged down despite still having strong fundamentals and good growth prospects.
- **Take Advantage of Income Generating Investments** – While we believe market fundamentals point toward a rise in the market over this next year, we also like to remind investors that we are in our ninth year of this bull market which will not last forever. Now is a great time to further diversify your portfolio and ensure you are taking the appropriate amount of risk given your financial goals. One way of conservatively diversifying some of your portfolio is by investing in fixed income vehicles such as preferred equities, convertible bonds, and treasuries. Short-term treasuries, in particular, have become more attractive as they offer yields of up to 2.5% with almost no risk as long as they are held to maturity.
- **Know Your Timeline** – Not all investors are the same and it is important during times of market volatility to reassess your timeline. For example, an investor that is planning to retire in one year may want to consider reallocating a portion of their portfolio to be more conservative and income-oriented. Contrastingly, an investor with a longer time horizon can afford to continue allocating money into equities since studies show that buy-and-hold strategies often outperform, assuming you can maintain your composure during the ups and downs of the market.

As a final note, we often find that the start of the new year is a good time to remind our clients to fully fund their retirement accounts for 2018 since the deadline to do so is April 15, 2019. The maximum you can contribute to your IRA or Roth IRA is $5,500 unless you are above age 50, in which case this amount rises to $6,500. By contributing each year, you can take advantage of one of the most tax-advantageous ways to grow your wealth.

As always, if you have any questions please do not hesitate to reach out.

Wishing you a wonderful and prosperous 2019,

The Glen Eagle Investment Team

- https://www.statista.com/statistics/270439/chinas-share-of-global-gross-domestic-product-gdp/
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