THE ECONOMIC MONTH IN REVIEW AND OUTLOOK – JANUARY

We'd like to begin by thanking Dr. Dan Seiver for being a member of our robust Investment Committee for just over ten years. Our tenured Investment Committee collectively represents nearly 150 years of economic and financial services experience and includes Dr. Seiver's Yale Ph. D. educational background and nearly 40 years of real-life experience. Successful Investment Management requires a team of experts and the combined knowledge provides the groundwork for the portfolios we create to help our clients navigate a map to success in their future financial lives. Now, onto the markets!

US Markets and Economy:

What a difference a month makes! The stock market extended its post-Christmas rally all through January. A nearly straight-line advance took the Dow Jones Industrials up by over 3000 points from its December low under 22,000, and the S+P 500 and NASDAQ Indexes also rallied sharply for the month. A bear market (defined as a 20% drop from the peak) was thus narrowly averted for the broad-based S+P 500.

While we have often said that long-term investors must endure these sharp short-term swings (and there will be more) in order to reap exceptional long-term profits, it is still worth asking: What changed?

Our first candidate is, as usual, the Fed. Even before their mid-month meeting, which left short-term interest rates unchanged, FOMC members (and Jerome Powell) let it be known that the Fed could indeed be done raising short-term rates. This is catnip for Wall Street's bulls, who love low interest rates. Low rates can make stocks look like the best game in town. Even more bullishly, the Fed let it be known that its program of $50 billion in monthly sales of its $4 trillion hoard of long-term securities could be stopped at any time. The Fed had been determined, as part of its move toward monetary policy neutrality, to bring these massive holdings, built up during the Great Recession and its aftermath, back to a more normal level of (perhaps) $2 trillion. Although this program had been in place for more than a year, without any obvious effect on long-term interest rates, Wall Street had decided in the fall that it was a chief culprit behind the late-year

decline. Although economists can disagree over whether Wall Street is right about this, all can agree that Wall Street would celebrate if the chief culprit were indeed sent packing.

But there was even more good news on the monetary front: the fears of "yield curve inversion" (short rates above long rates) had subsided by the end of January, as the yield curve itself had mostly undone its partial inversion. A full inversion has often signaled a forthcoming recession, but to paraphrase Yogi Berra, "it ain't inverted until it's inverted." And as of this writing, it ain't.

The economy itself delivered more good news as inflation stayed low, even as wage growth picked up, and businesses added over 300,000 net new jobs in December, to extend one of the longest streaks of growth in history. The first earnings reports for the fourth quarter of 2018 were also generally positive, as the effects of the corporate tax cuts were still feeding the bottom line.

Other news added to the bullish euphoria: the trade war with China seemed to be put on hold, with reports on progress toward a major trade deal, and Washington got back to work as the federal government shutdown ended, at least temporarily.

But we must add a cautionary note, since it is rare that stocks either rise or fall in a straight line for long. Wall Street traders would be likely to "take profits" at any sign that even one piece of the above bullish scenario was at risk. Of course these were the same short-term traders who drove stocks down last quarter. They generate the short-term volatility that long-term investors must endure.

In summary, the bulls have made a strong January statement that, to again paraphrase Yogi Berra, "the bull market ain't over until it's over." Looks like it ain't over yet.

World Markets and Economy:

European stocks rallied during the month, but the gains were only a fraction of Wall Street's. The blue-chip EUROSTOXX 50 Index rose 5% for the month, a good month except by comparison with Wall Street's surge. The specter of Brexit loomed ever closer, and the possibility that Britain will crash out of the EU at the end of March without any deal is still unnerving traders and policy makers. No one knows what will happen, including British PM Theresa May, but a disorderly Brexit will hurt both Britain and the EU. The situation is even more murky because it is not even clear that the British still want to leave. A second referendum is a possibility, and a vote to stay would muddy the waters beyond recognition. To make things worse, growth seems to be slowing again in Europe, and Italy is back in recession. (Italian stocks actually had a good month (up 7.5%), which is a useful reminder that short-term movements in stocks can be well-nigh inexplicable.) European stock traders will have to rely on the ECB to keep money easy enough to offset political developments.

In Asia, Japanese stocks also had a muted rally in January, rising about 3%. The market was held back by reports from the BOJ that inflation was weakening (Japan actually needs more inflation), and that the economy could be hurt by increasing world protectionism, and weakening demand from countries like China, where growth is still decelerating. To make matters worse, a Japanese patrol plane made an "intimidating" pass over a South Korean warship. While South Korea is an important trade partner for Japan, resentment against Japan's occupation of South Korea still exists, nearly 75 years after the end of World War II.

OUTLOOK:

US stocks remain in a bull market, and long-term investors with intestinal fortitude were again rewarded by holding on during the 2018 selloff. Trouble in Europe and Asia could create ripples in the US market, but stocks still provide the best long-term returns.