4th Quarter 2018 Market Overview

Markets Throw a Tantrum

The fourth quarter was dismal for the markets. Immediately following a strong third quarter, they began to slide. By December, markets lapsed into a full-blown tantrum mode. In the 14 days leading up to Christmas, the Dow dropped 4,260 points and the S&P 500 fell 13%. From September to the low point on Christmas Eve, the S&P 500 fell 20%. It was a drop of dismal proportion.

We will be more successful investors over the long term if we understand the causes for market declines and effectively manage the volatility that comes from any stock market disruption. Essentially, the stock market needs to endure setbacks because it is during this time when revaluations occur and the market can begin rising again.

Between 2016 and early 2018, the market climbed an unprecedented 15 consecutive months with almost no volatility. Furthermore, the market had not even posted a negative calendar year since 2008. It is very unusual for stock prices to have such a long, steady, and uninterrupted advance. The path of the market was unsustainable entering 2018. It was ripe for disruption.

Throughout the year, markets were troubled by the Federal Reserve implementing a monetary tightening policy. There were four rate hikes in 2018 that made investors very uncomfortable.

Growing fears over the US trade war with China and the concurrent brash posture from the administration also stoked investor fears. These tariffs, along with President Trump's self-proclaimed "Tariff Man" caused a considerable drag on stocks throughout the year.

Meanwhile, cracks began to appear in a strong economy. Housing dried up in the spring. Auto sales peaked. Bank loan growth turned down. Early in the fall, Japan and Germany both reported contracting economies and China was slowing sharply. Oil prices fell from 80 to 40 in only two months. "**Global growth" shifted to "global slowdown."**

These factors worried investors, but when Fed Chair Powell greeted the fourth quarter with a statement proclaiming "the greatest economy in our history", investors revolted by selling. How could the Fed Chief ignore relevant and important data that was permeating our economy?

Even Treasury Secretary, Steve Mnuchin, remarked in December, "We continue to see strong economic growth in the U.S. economy with robust activity from consumers and business." Mnuchin and Powell's remarks were regarded as cavalier, ill informed, and out of touch with reality.

The markets hated this and buyers staged a strike. It was apparent "Central Command" did not have a grasp of the data in order to conduct proper policy. As a consequence, markets threw a tantrum.

Positive Factors

Despite the damage in 2018, the outlook for the market in 2019 is *exceedingly* better than at the outset of last year. Stocks began 2018 stocks after climbing in uninterrupted fashion. Bullish enthusiasm was rampant. Interest rates were threatening to move markedly higher. These considerations contributed to an inherently fragile investment environment. Markets sat on thin ice as we began 2018.

The conditions for 2019 begin in sharp contrast to last year.

First of all, *stock prices are down*. **The average stock in the S&P 500 finished 2018 down 30% from its high point.**

The second positive factor for investors is *interest rates*. While last year, rising rates plagued the market, this threat has faded. Fed rate hikes are now on hold. Mortgage rates have fallen to 4.5% from 5%. It is always favorable for stocks when interest rates are *not rising*.

Lower fuel prices provide considerable savings to consumers at the pump and this should help consumer spending.

These factors provide a positive platform for investing in the first quarter of 2019.

Peregrine Portfolio

In reaction to the deteriorating stock market in the fourth quarter, assets were re-allocated to safe investments in order to protect client account levels. These balances will be re-deployed prudently into equities as the market recovers.

2018 ended up as the worst year since 2008 for investors. All major asset classes posted negative returns. These included world markets, bonds, and commodities. The S&P 500 dropped 14% in the fourth quarter and finished down 6.3% for 2018.

Our Equity and Balanced Composites relinquished their 2018 gains and fell 10% for the quarter and down 4% for 2018.

We look forward to client accounts staging a strong rebound in this first quarter of 2019.

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