SASSER

INVESTMENT MANAGEMENT, INC

Disciplined Value Investing

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## Q1 2019 Commentary: Eyes on the horizon

For an extended period of time the stock market exhibited an extraordinary period of calm. Volatility was very low, and the stock market went for historic periods without a major correction. In the last year that has changed, and the oscillations of the market have become more extreme. Last Summer we had the best quarterly return in five years. That was followed by the worst quarterly performance since 2011. In the first quarter, immersed in a government shutdown and a slowing global economy, the stock market advanced by the greatest amount since 1998. The S&P 500 advanced by 13.7% for the quarter and has continued to march higher in April. As of this writing, the stock market is within a single percentage point of the all-time high set in September of last year. Although prospects for stocks are generally positive, we should be prepared for market fluctuations similar to what we have experienced in the last year.

The stock and bond market recoveries from 4th quarter woes were triggered, almost entirely, by the Federal Reserve's announcement that interest rate increases were on hold. The Fed was reacting to signs that both the US and global economies were slowing. The bond market response to the Fed abandoning planned interest rate increases was for the yield on the 10-year US Treasury to plummet and bond prices to push higher. Higher prices propelled the Bloomberg Barclays US Aggregate Bond index 2.9% higher in the quarter.

Tax cuts fueled a torrid rate of earnings growth for the S&P 500 in 2018. However, expectations for early 2019 turned much lower reflecting the anticipated slowdown in the economy. First quarter earnings estimates are 3% lower than a year ago, which will be the first year-over-year earnings decline since the second quarter of 2016. The prospect of flat earnings, a slowing global economy, political and trade turmoil and the Fed's position to keep raising rates pushed investors to the sidelines. It must be remembered that financial markets are always reflecting what investors, in aggregate, are expecting in the future and projecting what is to come. Last Fall, they did not like what was on the horizon. In the first quarter, that changed.

With the Fed on hold, expectations for growth have taken a turn for the better. There is a concerted global effort to spur economic growth. Chinese monetary policy has been very accommodative and interest rates in Europe are falling and have even gone negative in Germany. These actions bode well for later in the year and the stock market is overlooking the current rough patch with expectations that earnings growth will resume in the 2nd half of the year.

Beyond the Fed standing down on further interest rate increases, additional developments have spurred investors to buy stocks. Foremost among them are the diminishing prospect of a continuing or expanded trade war with China. It seems that the best situation for the stock market with regards to the trade war would be for negotiation to linger on. Every time a white house official proclaims there has been progress in the trade talks, the stock market responds favorably. As soon as there is an agreement, expect its impact on the market to fade. In the meantime, the bond market has done the job for the Fed. Lower interest rates have raised optimism for the rest of 2019. The economy continues to be strong. Despite the move higher, the stock market is not near an extreme valuation and we continue to be positive about portfolios going forward.