LEGACY

FINANCIAL STRATEGIES

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Note from the Chief Investment Officer

2019 OUTLOOK

- *Slower real economic growth of 2.5%(but still growth)*
- *Inflation grinds higher but not out of control - wage growth fairly contained despite low unemployment*
- *No recession expected near term as the consumer has money, is spending it, and drives 68% of GDP*
- *Challenging year for stocks as the corporate earnings outlook is less clear (post-tax cuts)*
- *Volatility will be high as traders (not investors) buy/sell on economic headlines and tweets*
- *Interest rates move modestly higher which limit both bond and stock returns*

International stocks will seemingly be challenged due to a variety of factors

ECONOMIC RECOVERY

We are currently undergoing the second longest economic recovery since World War II. If we make it to July 2019 without a recession, it will mark the longest economic recovery since WWII. However, it will be the weakest in terms of Real GDP growth.

PORTOLIO POSITIONING

1. *Favor short maturity bonds over longer maturity bonds*
2. *Overweight US stocks for Non-US*
3. *A position in natural resources to hedge higher inflation*
4. *Balance of stocks and bonds based on the client's risk budget*

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Chart 1 – 2018 Calendar Year

Asset Class	Index	2018 Return
Cash	Bloomberg Barclays 1-3 Month Treasury	1.8%
Bonds	Bloomberg Barclays US. Aggregate	0.0%
Large US Company stocks	S&P 500 Index	(-4.4%)
Small US Company stocks	Russell 2000 Index	(-11.0%)
Developed International Stocks	EAFE Index	(-13.4%)
Emerging Market stocks	MSCI EME Index	(-14.2%)
Asset Allocation	Diversified mix of asset classes	(-5.80%)

EXPANDED EXPLANATION:

2019 will likely be challenging for a couple of reasons. First, the year-over-year earnings comparisons will be more difficult because corporate profits expanded considerably this year due to growth (2/3) and corporate tax cuts (1/3). Second, higher rates is bad for both the bond and stock market. Existing bonds are worth less (prices fall, yields rise) because new bonds will pay a higher interest rate. Stocks don't like higher rates because it increases financing costs and makes future cash flows worth less (which is how analysts value future earnings). Throw in a tariff dispute and it creates uncertainty, which markets don't like.

HOWEVER, consensus earnings growth for the companies in the S&P 500 is anticipated to be 10% for full year 2019. Consumer spending drives 68% of GDP so the tax cuts may still have a carryover effect keeping the economy moving along. Through Friday, the forward (expected) P/E ratio for the S&P 500 was under 15, which is below the 25 year average. This is due to strong earnings growth coupled with 0% growth in the broad equity market prices

ALAN GREENSPAN:

As for Greenspan, he was not very specific in expressing his views and told us nothing we didn't know already. He is well known for his characterization of the equity market as "irrational exuberance" back in 1997. However, he was about 3 years early but his comment was substantiated with far more "proof" back then. Internet startups that were highly unprofitable and worth billions of dollars were far more prevalent and obvious as they are now.

Chris Proctor
Chief Investment Officer

Source data:

[1] *Charles Schwab, Bureau of Economic Analysis, FactSet.*
[2] *Barron's (March 4, 2019; April 8, 2019).*
[3] *Federal Reserve Board – Monetary Policy Report, February 22, 2019*
[4] *JP Morgan Guide to the Markets Q2-2019*
[5] *Goldman Sachs on CNBC 3/26/19*
[6] *Bloomberg Barclays Global Aggregate Bond Index 3-22-19*