FLAGSTONE

FINANCIAL ADVISORS, INC.

MARKET REVIEW
THIRD QUARTER 2019

What Happened:

After a very strong first half of 2019, the market lost some steam in the third quarter. Investors became more fearful, largely because the news turned more negative. We were bombarded with headlines on impeachment inquiries, the China trade war and recession. Making matters worse, the fourth quarter stumbled out of the gate on news that manufacturing was slowing in the U.S. Investors struggled to make sense of it all. However, as our clients know, what matters to the news media is not necessarily the same as what matters to the market. Market gains are driven primarily by corporate earnings. Let's look more closely at what lies ahead on the earnings front.

Corporate earnings for the third quarter will be released beginning in early October. Consensus earnings estimates for the third quarter are expected to decline by 3.8%, then grow by 3.0% in the fourth quarter. For the full year 2020, earnings are expected to grow by 10.3%. Keep in mind that the market is forward-looking which means that future advances will be based on future expectations of growth, which are strong. That bodes well for the fourth quarter and beyond.

On the economic side, U.S. GDP growth of 2.4% is expected for this year and 2.3% for 2020. Worldwide, the numbers look even better with expected GDP growth of 3.1% for 2019 and 3.4% for 2020. These numbers would suggest that economic growth is steady and that fears of a near-term recession are probably overblown.

Investors tend to devote most of their attention to the stock market. If you are in that camp, you may have missed a remarkably good run for bonds which gained 8.5% in the first nine months of 2019. This stellar bond performance, which was largely unexpected, was directly attributable to rising bond prices brought about by falling interest rates.

9/30/2019 YTD Performance:

S&P 500 Index (large stocks)	20.6%
Russell 2000 Index (small stocks)	14.2%
MSCI EAFE Index (international stocks)	12.8%
Barclays U.S. Aggregate Bond Index (bonds)	8.5%

Prognosis:

It didn't work out in 2018, but the 4th quarter is historically the best quarter for the market. Considering the strength of earnings projections, there may be more upside potential for this bull market. What's more, most economic indicators are positive, including record-low unemployment, low inflation and low interest rates. On the negative side of the ledger, we see no end to the political discord in Washington, D.C. or the ongoing trade war with China. But as we pointed out earlier, these troublesome matters will take a back seat to the positive effects of earnings growth. Enjoy the fall colors!

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