The fourth quarter opened with reasonably positive expectations based upon corporate earnings, consumer confidence, low unemployment and favorable leading indicators. A dramatic shift occurred during the quarter driving major stock indices down sharply; DJIA was down -11.3% for the quarter more than wiping out gains for the full year which was off -3.5%. The S&P 500 slid -13.5% for the quarter and -4.4% for the year while NASDAQ (think technology) was down a steep -17.3% for the quarter and -2.8% for the year. Contrasting with stock results, the Barclay’s Aggregate Bond index which was up+1.6% for the quarter and was flat for the year.

There were many factors contributing to the market decline. The indices had risen considerably in the first 9 months of 2018 concurrent with a rise in volatility. The Federal Reserve raised interest rates in December (probably not a good idea as inflation is low) and, in combination with trade war pressures plus slowing growth in China, the market dropped. One additional factor hurting the market is the gridlock in Washington. The current Government shut down and the inability to develop an immigration policy are examples of this stalemate. More immediate issues include uncertainty about how the imposition of tariffs will work out and how new trade policies with Mexico and Canada will impact companies and economic growth.

Except for Latin America, which was up +10.8% in the fourth quarter, international markets were down for the quarter and full year. China, for example, was down -11.6% for the quarter and down -19.6% for all of 2018. Other evolving issues include: the outcome of Brexit, significant political unrest in France and the general slowing of international economies. The growing assertiveness of China, continuing “talks” with North Korea, the impact of our sanctions on China and Iran are problem areas for those countries and the U.S. We would be remiss to overlook the continuing disaster called the Middle East! We hope that eventually the U.S. and Russia will help resolve this nightmare as well as the growing problems between Russia and the USA.

We have described some of the major economic issues facing the USA and major international areas. But the news isn’t all bad! Unemployment is still low and record numbers of Americans are employed. Wages are rising and inflation is low (the Fed may not increase interest rates as planned in 2019) and corporate earnings should be OK. Finally, the overall economy should continue to grow although at a slower rate.

Market results are detailed below.

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
|  | **QUARTER Ending 12/31/2018** | **12 MONTHS Ending** **12/31/2018** | **THREE YEARS Ending** **12/31/2018** | **FIVE YEARS Ending** **12/31/2018** |
| **DJIA** | -11.3% | -3.5% | 12.9% | 9.7% |
| **S & P 500** | -13.5% | -4.4% | 9.3% | 8.5% |
| **NASDAQ Composite** | -17.3% | -2.8% | 11.1% | 11.0% |
| **Barclay Agg. Bond** | 1.6% | -0.0% | 2.1% | 2.5% |
|  |  |  |  |  |
|  |  |  |  |  |
|  | **QUARTER Ending 12/31/2018** | **12 MONTHS Ending** **12/31/2018** | **THREE YEARS Ending** **12/31/2018** | **FIVE YEARS Ending** **12/31/2018** |
| *Mutual Funds* |  |  |  |  |
| Domestic |  |  |  |  |
|  *Large Cap* |  |  |  |  |
|  Growth | -15.4% | -2.1% | 9.0% | 8.2% |
|  Value | -12.5% | -8.5% | 6.9% | 5.4% |
|  *Small Cap* |  |  |  |  |
|  Growth | -20.9% | -5.8% | 8.5% | 5.1% |
|  Value | 1.0% | 8.4% | 13.8% | 8.4% |

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| International |  |  |  |  |
|  Europe | -13.3% | -15.3% | 1.5% | -0.5% |
|  Latin America | 10.8% | -5.7% | 20.7% | -1.5% |
|  Japan | -15.6% | 15.1% | 3.4% | 5.1% |
|  Pacific ex Japan | -8.3% | -14.6% | 6.8% | 3.4% |
|  China Region | -11.6% | -19.6% | 3.8% | 3.1% |
|  |  |  |  |  |
| Corporate Bond |  |  |  |  |
|  Long | 0.2% | -3.3% | 4.2% | 5.2% |
|  Intermediate | 0.9% | -0.5% | 2.2% | 2.3% |
|  Short | 0.5% | 1.0% | 1.7% | 1.3% |
| Government Bond |  |  |  |  |
|  Long  | -2.9% | -3.7% | 0.5% | 4.4% |
|  Intermediate | 2.0% | 0.5% | 1.1% | 1.8% |
|  Short | 1.1% | 1.1% | 0.8% | 0.7% |
| Municipal Bond |  |  |  |  |
|  Long  | 1.1% | 0.3% | 2.0% | 4.0% |
|  Intermediate | 1.2% | 0.8% | 1.7% | 3.1% |
|  Short | 0.7% | 1.2% | 0.9% | 1.0% |

**Market Outlook**

Expect volatility. A lot of domestic and international issues have to be worked through but the overall economy is in pretty good shape; corporate profits should be OK. The probability that the Fed won’t increase rates in 2019 is encouraging for the market. While we are not as bullish on the market as we were last quarter, we are not negative.

Unless you need more liquidity (ready cash – money market account) we suggest you continue with your current target allocation to stock. If you would like to discuss your allocation or feel uncomfortable about it, please let us know.

**MSM FINANCIAL STRATEGIES**

 **1/4/2019**

*@Copyright 2019 MSM Financial Strategies*