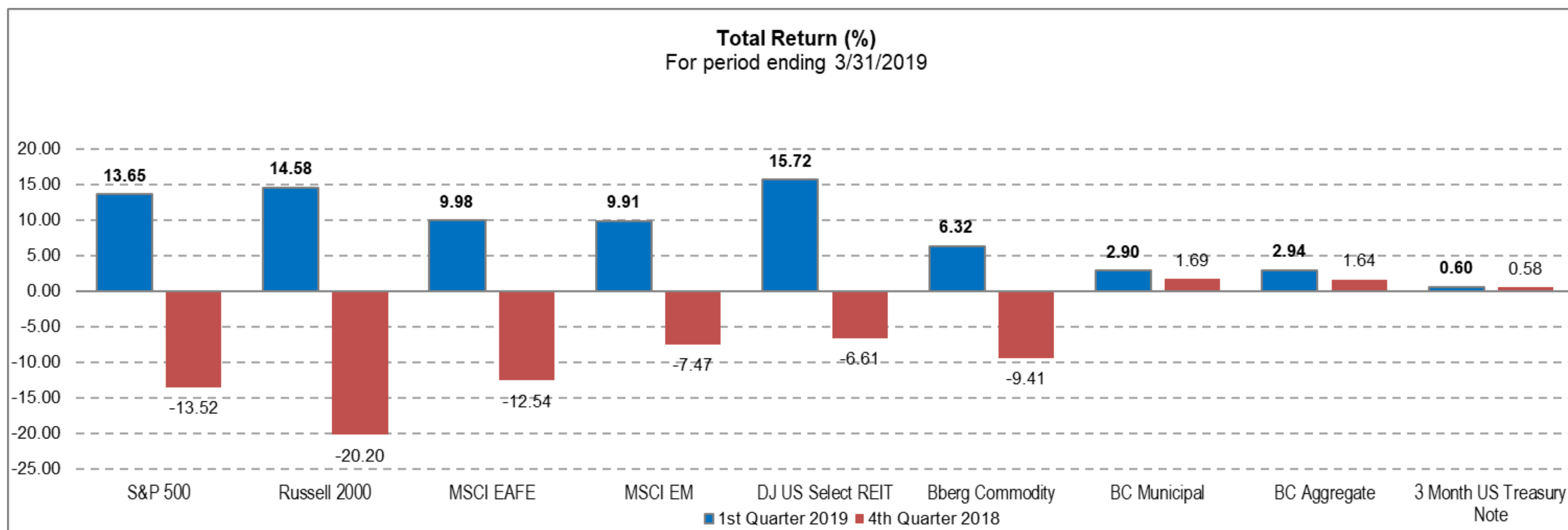
Portfolio Review

Prepared by Schneider Downs Wealth Management Advisors, L.P.
March 31, 2019

SCHNEIDER DOWNS
Wealth Management



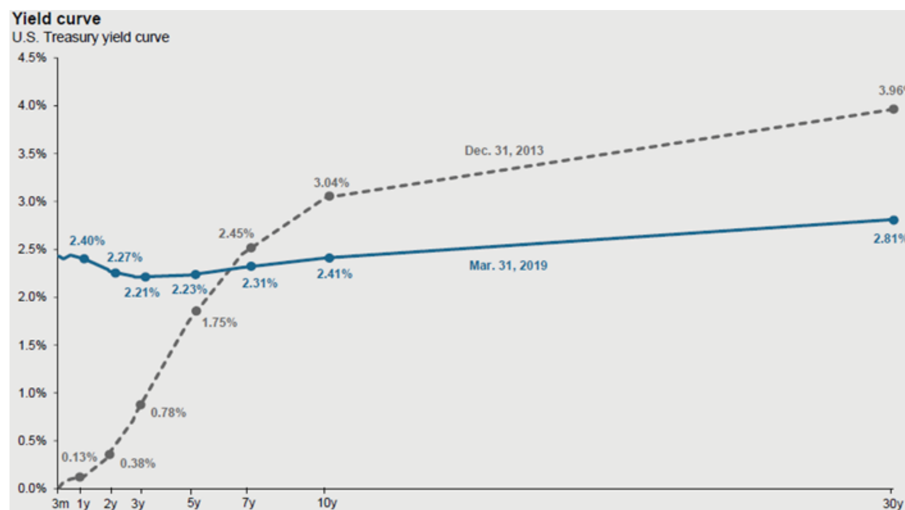
As our team reflects on the significant decline in risk-based assets in the fourth quarter of 2018 (denoted in the red bars above), keeping clients invested despite the negative news cycle and sharp rise in volatility was of paramount importance. This singular focus was due to the fact that markets can swing upward quickly, often with little to no notice, making "timing" of markets nearly impossible. The first quarter of 2019 brought investors the aforementioned "swing upward," shrugging off a negative story on Apple on the second trading day of the year[1] and propelling risk-based assets to one of the best first quarters on record[2]. Stocks rallied sharply off their December bottoms in January and continued their climb in February before moderating the last two weeks of March. For investors that were looking for a better entry point in the first quarter, they did not find one; and that is why we advised clients to stay the course, because often times the next rally is right around the corner. As the Oracle of Omaha, Warren Buffet, often says "be greedy when others are fearful, and be fearful when others are greedy."[3] Investors were rightfully shook up after the violent decline in the 4th quarter, but if they had packed up their bags for greener pastures (entry points), they would have missed out on the best first quarter in a decade.

The backdrop heading into 2019 for U.S. equities was a deluge of negative news articles. The negative prognostications seemed to have some legs to them when Apple announced some issues with their business in China, and that it would miss sales estimates assigned to the company on the second day of trading in 2019[4]. Apple declined almost 10%, causing US markets to decline in excess of 2%. However, the headwind would soon be forgotten as Jerome Powell, Chairman of the U.S. Federal Reserve, indicated that the Fed would be "patient" and "data dependent" on future interest rate increases, effectively ending the Fed's monetary tightening program[5]. As the pressure of future increases in interest rates (and thus higher funding costs and lower margins for businesses) was taken off the table, investors regained their "risk on" orientation. U.S. large cap equities were up 13.65% in the first quarter and U.S. small cap equities fared well too, returning 14.58%.

---

[1]https://www.cnn.com/2019/01/03/investing/stock-market-today-apple-dow-jones/index.html
[2]http://fortune.com/2019/03/29/us-stocks-tech-best-quarter-decade/
[3]http://www.berkshirehathaway.com/letters/2004ltr.pdf
[4]https://www.cnn.com/2019/01/03/investing/stock-market-today-apple-dow-jones/index.html
[5]ttps://www.c-span.org/video/?457240-1/federal-reserve-leave-interest-rates-unchanged-amid-economic-crosscurrents

International equities had a difficult 2018, but they ended the year outperforming their U.S. counterparts in the fourth quarter (on a relative basis). The strongest headwind for international equities has been the strength of the U.S. Dollar (with a close second being the parade of internal strife and emanating from Europe - from BREXIT, the lack of cohesion amongst the European Monetary Union, and political uprisings in Germany and France to name a few). As a result of these headwinds, international equities as a whole are trading at a significant discount to their U.S. peers[6], while offering a dividend yield that is 68% greater than its U.S. counterparts[7]. The rising tide of global risk appetite lifted international equities higher with International Developed and Emerging Market Equities advancing approximately 10% in the first quarter. Emerging Market equities completed a strong six-month run on a relative and absolute basis, as they were the top performing broad equity asset class on a trailing six month basis. Yet with all things international, Emerging Market equities face questions as a proxy for global growth and often times are the unfortunate recipient of downward pressure in a risk off environment. Emerging Market equities offer perhaps the most pure exposure to global growth at low valuations, but they also face the most uncertainty with threats from an increasing U.S. dollar.



While equity markets have been rapidly appreciating in 2019, the bond market has been flashing a bright caution sign. The U.S. yield curve inverted in late March[8], with the three-month U.S. Treasury bill yielding more than the ten-year U.S. Treasury note. While yield curve inversions are not a perfect predictor of recessions, the broader yield curve gives a view into a subset of investors' expectation of growth. The flatness of the overall yield curve (3-month to 30-year yields) suggests that the bond market is not expecting much in the way of economic growth in the U.S. over the coming years. Given this as a backdrop, our core fixed income allocation provided solid returns during the 1st quarter.

As advisors and investors, we largely find portfolios back to where they were at the beginning of the 4th quarter in 2018 as equity markets have broadly retraced the losses incurred in the last 90 days of the year. The fixed income market, while providing safe haven, offers low yields and conflicting messages from that of the equity market. At the risk of sounding repetitive, when assessing the full backdrop of the markets, the investment community finds itself at another crossroads. Markets have spun up quickly, and there remains a strong possibility that equity markets will not advance much past their current levels. However, with further monetary tightening seemingly off the table globally, risk-based assets could conceivably run a bit further. Given the uncertainty, thoughtful rebalancing and an accurate measure of risk tolerance (and corresponding asset allocation), remain the prudent course for long-term investors.

The SDWMA team thanks you again for another year of trust in shepherding your assets through these tumultuous times, and we look forward to meeting with you to discuss first quarter results. If you have any questions or concerns, please reach out to your SDMWA representative.

[6] https://am.jpmorgan.com/us/en/asset-management/gim/adv/insights/guide-to-the-markets/viewer
[7] https://am.jpmorgan.com/us/en/asset-management/gim/adv/insights/guide-to-the-markets/viewer
[8] https://www.businessinsider.com/yield-curve-inversion-one-of-four-horsemen-predicting-us-recession-2019-3

Material discussed is meant for general illustration and/or informational purposes only and it is not to be construed as investment, tax or legal advice.
The information has been gathered from sources believed to be reliable, however, complete accuracy cannot be guaranteed. The indexes shown are for illustrative purposes only and are not indicative of past or future results of any specific investment. Indexes are unmanaged and investors cannot invest into them directly and with any investment vehicle, past performance is not a guarantee of future results.