SPRING 2019

Unlike the defending World Series Champions, the stock market is off to a roaring start in 2019. While the Red Sox have stumbled early in 2019, after a glorious finish to their 2018 season, most major stock indices across the globe are off to a great start after a rather inglorious finish in 2018. It is a long season in baseball and a longer year for the markets but the early results for stocks are a stark contrast to the finish of the investment "season" last year.

The S&P 500 produced a total return of 13.6% in the first quarter of 2019. This rally came on the heels of last years' dismal 4th quarter negative returns of (13.5%), one of the worst quarterly returns in recent memory. This reversal of fortune was enjoyed in overseas' markets as well with the MSCI EAFE (foreign developed) Index up 10.1% for the first quarter, versus a decline in final quarter of 2018 of (12.5%). The MSCI Emerging markets index rose 9.6% in the first quarter versus last years' fourth quarter decline of (7.8%).

In 2018 the S&P 500 had a negative total return of (4.4%) after the decline in the fourth quarter. The recovery in the first quarter of 2019 has boosted returns for the index for the past 12 months to 9.5%. The positive performance in both the foreign developed and emerging markets in the first quarter, while encouraging, was not enough to completely offset last year however, as both the MSCI developed and MSCI emerging indices have negative trailing 12 month returns of (3.2%) and (9.6%) respectively.

The negative return on the S&P 500 last year of (4.4%) actually overstated the performance of many stocks and industry sectors within the S&P 500 with the average stock in the index being down (9.0%). So far in 2019, according to Argus Research, 9 of the 11 sectors of the S&P 500 are up over 10%. Argus also points out that the advance this year in the S&P 500 has been more orderly than the rout in late 2018 with a daily rate of change of 0.61% in 2019 versus 1.1% in the fourth quarter of 2018.

While the stock market enjoyed broad upward participation in the first quarter of 2019, growth stocks, as measured by the Russell 1000 Growth Index, led the way versus value stocks once again. The Russell 1000 Growth Index rose 16.1% in the quarter while the Russell 1000 Value Index posted a respectable 11.9% gain. The Russell Growth Index is heavily weighted towards technology with over 25% of the index in Apple, Alphabet, Amazon, Microsoft and Facebook. The Russell 1000 Value Index largest holdings include J.P. Morgan, ExxonMobil, Berkshire Hathaway, Johnson & Johnson and Bank of America. While the contrast between "new economy" and "old economy" in the indices is readily apparent, we believe a diversified portfolio across both groups is the best long term strategy.

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As reassuring as the recovery in stocks has been the advance came on the heels of a quarter where everything seemed to be falling apart. Many of the issues impacting the market late last year remain unresolved but there has been progress on some fronts. A resolution of the trade war with China appears to be getting closer and the Federal Reserve has adopted a far more cautious stance regarding further interest rate increases.

One consequence of the Fed's new restraint has been a decline in bond yields, particularly in longer term bonds. This decline in long yields has led to an inversion in the yield curve, short term rates above long term rates, which may be a precursor to a recession. An inverted yield curve does not always precede a recession but it is a concern for many economists. In addition to concerns about the yield curve, there are worries about the pace of the U.S. economic recovery slowing and corporate earnings rising only modestly this year versus substantial gains last year. Many are concerned that we are in the very late innings of our recovery and that after 9-10 years we are due for a slowdown. Foreign economies continue to sputter and some fear a recession is inevitable.

We understand and appreciate these concerns and we may indeed see a recession in the near future. However, not every recession is like 2008-2009 or 2000-2001. In our long experience we have lived through a few recessions that we didn't know we were in until after they had ended. This isn't to make light of an economic slowdown, only to state that as long term investors we have to focus on stock valuation rather than economic forecasts. While the advance in stocks in the first quarter has pushed stock prices higher, we think reasonable valuations may be found in many individual stocks.

We hope the early success of the stock market will continue but we know a lot can happen over the long season. Hopefully the Red Sox will soon begin an uptrend of their own. We wish you the best as we greet our long awaited spring.

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