FIRST QUARTER CLIENT LETTER


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As we entered 2019, most investors were cautious. We had just finished a challenging year. Stocks and bonds gyrated throughout the year, buffeted by macroeconomic events. In the final weeks of 2018, stocks fell sharply—giving up earlier gains—and teetered near a 20% loss from those previous highs, ending 2018 down 4.4%.

In 2019, those risks lingered. Interest rate fears continued to rise, casting doubt on whether economic growth could continue. The simmering trade dispute with China threatened to boil over into a prolonged trade war, and domestic political wrangling continued with the usual attacks and counterattacks.

Early in the first quarter some of those risks began to fade, at least temporarily. Talk of trade retaliation and tariffs gave way to more negotiations. Jerome Powell, Chair of the Federal Reserve, signaled that interest rates had risen enough, and no further rate increases were expected in 2019.

As the perceived level of risk dropped, markets rose. By the end of the quarter, the S&P 500 had recovered the losses of 2018 and then some. Bonds also rose with the prospect of continued low rates. The Barclays Aggregate Bond Index erased earlier losses.

Apparently, the dramatic moves were brought on by reactions to risk. The media often refers to down periods as "risk off" and rising markets as "risk on." Our view of risk is a bit different. Risk isn't always bad. We all encounter risks in investing and in our daily lives. Some level of risk is largely unavoidable. We build portfolios in anticipation of risk, not in response to it. As Columbia professor and famed investor Benjamin Graham once said, "Successful investing is about managing risk, not avoiding it." This is best accomplished with a timeframe that is measured in decades not days.

Domestic Equities: The first quarter market movements again show that predicting short-term market movements is a near futile exercise. Just when rising interest rates and trade issues were certain to derail the 10-year run in equities, they didn't. The S&P 500 bolted to a 13.7% gain. This was the best quarterly gain in almost 10 years. Smaller U.S. stocks, which are sometimes considered less exposed to trade issues, did even better. The Russell 2500 index shot up 15.8%.

International Equities: Foreign stocks struggled with issues of their own. European economies have been slower to recover than in the U.S. In addition, Europe has struggled with Britain's halting negotiations for an exit from the European Union. Despite these issues, international equities also marched higher in the first quarter. The Developed Market Index increased 10% for the quarter. Emerging markets, despite the tariff issues, rose 9.9%.

Fixed-Income: The economy has obviously recovered strongly over the years since the Great Recession. Clearly, the massive stimulus provided by its unnaturally low interest rate policy had to be reversed. The trick would be to gradually raise rates. This is important because many areas of the economy like housing and consumer consumption are related to the level of rates.

When the Fed announced that instead of several interest rate increases in 2019, there likely would be none, bond investors breathed a sigh of relief and prices rose. The Barclays Aggregate, a measure of the total bond market, increased 2.9% for the quarter. This is quite a jump for the usually muted movement of bonds.

It is gratifying to see hard earned capital recover and grow. We sometimes get the question, "Are we out of the woods yet?" The answer is unfortunately, no. As stewards of capital, we understand we must protect hard-earned capital as well as grow it. The key is to balance these objectives, never letting one dominate the other—always seeking gains but aware of risks even when they are not yet evident. Our commitment to you is that we will be there during whatever the future brings.

% Return as of 03/31/2019

Equity Indexes	**1st Q**	**1 Yr**	**3 Yr**
S&P 500	13.7	9.5	13.5
Russell 2500	15.8	4.5	12.6
MSCI EAFE	10.0	-3.7	7.3
Emerging Market	9.9	-7.4	10.7
Wilshire REIT	16.0	19.3	5.5
Bond Indexes			
TIPS	3.2	2.7	1.7
Aggregate	2.9	4.5	2.0
Government	2.1	4.2	1.1

Mortgages	2.2	4.4	1.8
Investment Corporate	5.1	4.9	3.6
Long Corporate	8.0	4.4	5.3
Corporate High-Yield	7.3	5.9	8.6
Municipals	2.9	5.4	2.7
Cash Equivalents			
3-Month T-Bill	0.6	2.2	1.2
Consumer Price Index	0.1	1.5	2.2

Thank you for your confidence in us. Please let us know if you need anything or just want to talk. We are here to help.

Source of data – Barclays Aggregate, Morningstar, Wall Street Journal, Bloomberg, Reuters, Dow Jones Newswires, American Funds, MSCI, S&P Index, The Federal Reserve. The performance of an unmanaged index is not indicative of the performance of any particular investment. It is not possible to invest directly in any index. Past performance is no guarantee of future results. This material represents an assessment of the market environment at a specific point in time and is not intended to be a forecast of future events, or a guarantee of future results. Three-year performance data is annualized. Bonds have fixed principal value and yield if held to maturity and the issuer does not enter into default. Bonds have inflation, credit, and interest rate risk. Treasury Inflation Protected Securities (TIPS) have principal values that grow with inflation if held to maturity. High-yield bonds (lower rated or junk bonds) experience higher volatility and increased credit risk when compared to other fixed-income investments. REITs are subject to real estate risks associated with operating and leasing properties. Additional risks include changes in economic conditions, interest rates, property values, and supply and demand, as well as possible environmental liabilities, zoning issues and natural disasters. Stocks can have fluctuating principal and returns based on changing market conditions. The prices of small company stocks generally are more volatile than those of large company stocks. International investing involves special risks not found in domestic investing, including political and social differences and currency fluctuations due to economic decisions. Investing in emerging markets can be riskier than investing in well-established foreign markets.

The MSCI EAFE Index is designed to represent the performance of large and mid-cap securities across 21 developed markets, including countries in Europe, Australasia and the Far East, excluding the U.S. and Canada. The Russell 2500 Index measures the performance of the 2,500 smallest companies (19% of total capitalization) in the Russell 3000 index. The S&P 500 index measures the performance of 500 stocks generally considered representative of the overall market. The Wilshire REIT Index is designed to offer a market-based index that is more reflective of real estate held by pension funds.

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