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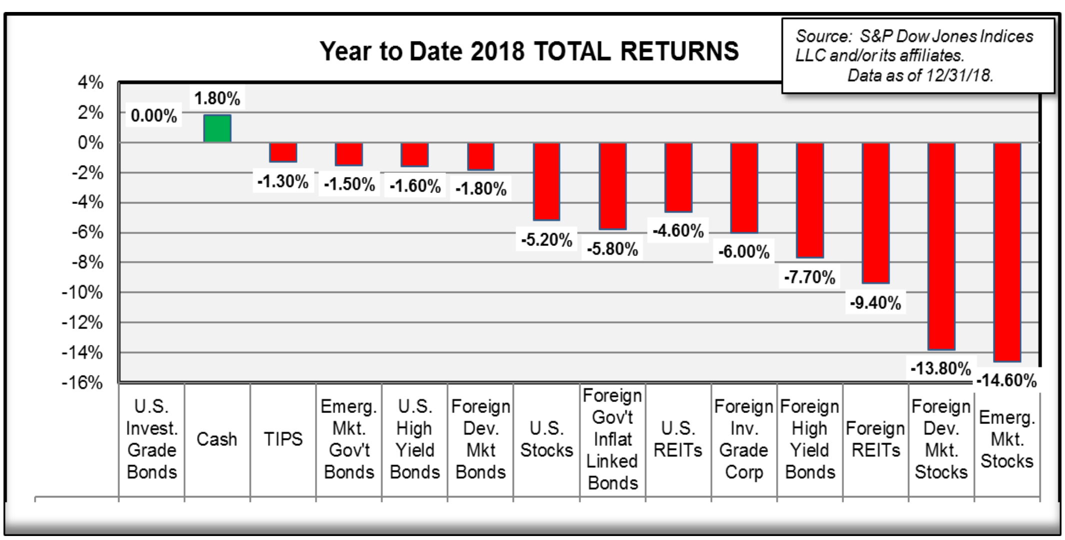
2018—The Year Nothing Worked (for the Investors)

I nearly wrote a brief summary on the market conditions some weeks ago, but some amount of constraint and professional intuition had me wait until a couple of days ago – close to the year-end yet soon enough on the heels of the market correction which has seen the index of largest American companies (S&P500) correct -15% since the start of the quarter through Dec. 27th (with Emerging Markets index following suit at -9% and the index of 21 developed countries excluding Canada and U.S.A. rounding of the correction at -14%). In tandem, oil prices plummeted from their lofty $73 a barrel to the current $46 a barrel for the West Texas Crude in the same period. On record, one of the worst quarters the markets produced in a long while.

What is the most meaningful commentary on the causes and rationale for it?

I often talk to my father about my work and he has, on a somewhat persistent basis offered an idea there are forces which dictate large market swings that he, like all other individual investors cannot be protected from. While I do not subscribe to his "dark forces" theory (and for the purpose of full disclosure given that he is not a US citizen ((and/or permanent resident here)) I do not advise him on his investments), I do believe that the current market conditions have been in part influenced by a much larger role momentum/algorithmic investors have had on the market. In the past, the markets were moved by individual and institutional investors (for whom ownership in a particular company stock was extremely valuable) while today these investor classes have been dwarfed by passive and momentum (algorithmic) investors for whom that is not the objective. It would appear that the market is moved by the latter and not the former. If so, why such volatility when the fundamentals remain so solid?



IRA and Pension Limits 2019

IRA Contribution $6,000
Age 50 and over $7,000

SIMPLE elective deferral
Under age 50 $13,000
Age 50 and over
$16,000

401K, 403B, 457
Elective Deferral
$19,000
Age 50 and over
$25,000

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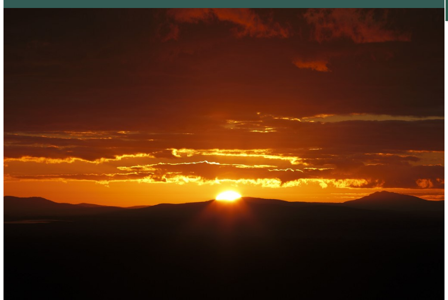

Speaking of fundamentals, job growth remains steady (albeit the U.S. economy is producing some 200,000 jobs monthly while only producing 100,000 people through population growth); retail sales for the current holiday season are at +5.1% best in 6 years (with online sales at +19.1% gain best ever); unemployment figures are at their lowest since late 1960's (3.7%) and the operating earnings so far have been up 27% on a year over year basis. So why the volatility and why the underperformance? Is it the steady drumbeat of trade war escalation? Is it the Fed action trying to contain the overheated economy? Is it a slow momentum expiration of last year's tax cuts? Is it the government shutdown? Or is it that the markets have been doubting all of it and producing the volatility and pricing that forecasts a slowdown leading to a recession next year? Quite possible.

What is then in store for the investing public in 2019? Given that we have not seen the fundamentals shift – patience first. Also, a change in focus from domestic equities to gradual and bigger emphasis on seeking returns in both developed and emerging markets (both of which have been underperforming yet have lower valuations than the U.S. market) – will reward the investors if they are patient and unafraid. Last but not least, cash will be more prominent given the rate increases have given us 2.5-3% CD rates.

If you are currently invested in a diversified portfolio and it has performed near or below benchmark, look to make moderate adjustments that reflect the above. As always, remember your time horizon and have your portfolio reflect that risk.

Nenad (Ned) Tufekcic

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