MARKET OVERVIEW

First Quarter 2019

OPAL WEALTH ADVISORS

Global Economic Review

Jerome Powell's January 4th speech in Atlanta was a pivotal point for financial markets. The U.S. Federal Reserve's shift away from its tightening monetary stance turned the tide for global markets that had plunged into bear market territory in December. While most economic indicators remained tepid during the first quarter, China's policy stimulus resulted in signs of stabilization and progress.

- Economists have been raising their estimates for first quarter U.S. GDP to 2.0%–2.5% after the trade deficit unexpectedly narrowed in February. European GDP has been falling from the low 2's to the low 1's and China's GDP is at 6.4% (7% used to be considered a recession). U.S.-China trade negotiations are increasingly looking outcome oriented, not time oriented which is both a positive (results) and a negative (lingering uncertainty).
- The 3-month/10-year yield curve briefly inverted in March triggering concerns that a recession could be on the horizon. While it is true that every recession since 1962 has been preceded by a yield curve inversion, not every inversion has been followed by a recession. Currently the yield curve is not inverted with the 3-month yield at 2.44% and the 10-year yield at 2.59%.
- The Fed kept rates steady at 2.375%, projected no more rate hikes in 2019, reduced their 2019 growth forecast to 2.1%, and announced a tapering of the balance sheet normalization program with a conclusion by September—much sooner than anticipated. The pace of Chairman Powell's pivot from a hawk last October to an outright dove in March has been remarkable. Fed funds futures markets have taken it further, now pricing in over 50% odds of a rate cut in 2019.
- Most recent headline and core PCE inflation readings of 1.4% and 1.8%, respectively, raised no eyebrows and probably supports the dovish tone from the Fed.
- British Prime Minister May's Brexit withdrawal proposals have failed in Parliament three times as did eight votes on alternative proposals including remaining in the European Union, holding a second referendum on Brexit, and revoking Article 50. The European Union is soon to decide on a second extension which may push things out to June 30th or later.
- U.S. unemployment rates continue to hover around historic lows (3.8%). Wage growth moved slightly higher to 3.2%.
- The most recent consumer confidence reading of 124.1 was far short of expectations thanks to deteriorating views of the economy and wage growth while consumer sentiment jumped to a 6-month high of 98.4 reflecting favorable current conditions and forward expectations.

Market Review

Over the last six months, the S&P 500 swung from its worst quarter in in over seven years to its best quarter in almost ten years. In fact, December was the worst final month of the year since the Great Depression. By comparison, January and February performance was the strongest start to a year we have seen in 32 years. Volatility, as measured by the CBOE Volatility Index, spiked on Christmas Eve hitting 36.07, well above its 5-year average of 14.95. The S&P was up 13.7% in the first quarter with Technology (+19.9%), Industrials (+17.2%), and Energy (+16.4%) jumping to the front of the pack after dropping the most during the fourth quarter. Healthcare (+6.6%) was the laggard during the first quarter after being the best performing sector during the second half of 2018. Growth stocks outperformed value stocks as evidenced by the S&P 500 Growth

Index (+15.0%) vs. the S&P 500 Value Index (+10.8%). There was a slight positive bias towards smaller companies with the Russell 2000 posting a 14.6% return. International equities also had strong results for the quarter with both the EAFE Index and MSCI Emerging Markets Index gaining 10.0%. The United Kingdom (+11.9%) and France (+10.8%) led developed markets while China (+17.7%) and Russia (+12.2%) led emerging markets. Although fears over the U.S.-China trade war seem to have abated, worries about Brexit and the U.S. closing its border to Mexico have investors fretting about global supply chains as we enter the second quarter.

Like the equity markets, the risk-off trade in fixed income markets during the fourth quarter was largely erased during the first few months of 2019. The Fed's dramatic shift to a dovish tone mitigated fears that a recession is imminent, and investors piled into bonds during the first quarter. The yield curve has been flattening for some time and briefly inverted on March 22nd through March 29th, its first inversion since 2007. Every recession since 1962 has been preceded by a yield curve inversion, but not every inversion has been followed by a recession. Sometimes, an inversion is a signal that markets are anticipating a cut in interest rates. U.S fixed income posted positive returns across the maturity spectrum during the first quarter with the Bloomberg Barclays Aggregate Bond Index gaining 2.9%. Returns were also positive across the quality spectrum with high-yield bonds posting the strongest results as evidenced by the Bloomberg Barclays High Yield Bond Index up 7.3%. Municipal bonds kept in step with taxable bonds with the Bloomberg Barclays Municipal Bond Index up 2.9%. Internationally, more than half the debt of developed economies yields below 1%, as measured by the Bloomberg Barclays Global Developed Sovereign Index. In many cases, investors have to go out five years or more on the yield curve to achieve a positive yield. It appears that global bond investors are betting on further central bank stimulus in the face of softening economic data. The FTSE World Gov't Bond Index ex U.S. was up 1.7% in the first quarter.

Commodity prices climbed 6.3% in the quarter, boosted by a 15.9% gain in the energy sector and a 12.9% gain in industrial metals. WTI Crude Oil prices spiked sharply higher during the first quarter ($45.15 at 12/31 to $60.19 at 3/31) as the global demand outlook improved while supply remained constrained (Venezuela, Saudi, Iran). Agriculture was impacted by the U.S.-China trade war and lost 3.2%.

Outlook

We are maintaining a cautiously constructive view looking forward and recommending that clients remain modestly overweight risk assets relative to their long-term strategic asset allocation targets. Despite the spike in volatility at the end of last year, we are reassured by strong corporate fundamentals and solid economic data, particularly in the U.S. Earlier concerns that a hawkish Fed may raise rates too aggressively and trigger a recession have dissipated. We are closely watching as China's policy stimulus gains traction and potentially sends positive ripples through emerging markets and Europe, as this may present an opportunity later in the year.

OPAL
WEALTH ADVISORS

Opal Wealth Advisors / 2 Jericho Plaza / Suite 208 / Jericho, NY 11753 / t. 516.388.7980 / f. 516.388.7968 / **opalwealthadvisors.com**