QUARTERLY MARKET COMMENTARY: 2018-Q3

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It was an impressive 3rd quarter for U.S. Equities as the path to new highs continued into the 4th quarter. In tandem with the stock market run-up, yields on U.S. Treasuries also climbed to 7-year highs driven by another Fed rate increase and more positive news along the lines of employment and wage growth. As anticipated, the Federal Reserve raised rates for the third time this year with the possibility of a fourth, as they continue to monitor the ever-growing signs of inflation.

Even though U.S. Equity markets have come off recent highs, there is a lingering concern that we are in overbought territory again. However, given the current levels of the S&P 500, it is surprising that we are only trading at a forward P/E of approximately 16.8. This reasonable multiple is supported by our recent breakdown & analysis of the companies within the DJIA which resulted in a fair market value of approximately 26,200 for the index. Throughout 2018, we have observed company fundamentals playing catch-up, thus providing stronger support for higher equity valuations. In the presence of healthy fundamentals, we do note an increasing presence of negative earnings adjustments which we believe is attributed to rising costs/expenses. This may present a challenge to capital markets in the next 12 to 18 months.

On the trade front, we received good news regarding Canada's decision to join the U.S. and Mexico in the replacement of NAFTA. Based on available information, positive aspects for the U.S. have been identified within the newly coined "USMCA." However, we do not expect a significant impact on trade figures among the three countries. The post NAFTA agreement should not be gauged by the impact on trade reports, but by the position of relative strength that it provides to the U.S. in addressing trade issues with China.

All eyes have been focused on the near-term effects caused by the implementation of tariffs. Analysts have even attributed part of the exceptional 2nd quarter GDP figure of 4.2% to the anticipation of tariffs, pressuring other countries to make large purchases from the U.S. before tariffs kicked in. Some reports have reflected that up to 1.2% of the 4.2% was driven by additional orders. We can only get a better sense of this discussion when the 3rd quarter GDP is reported. Monitoring near-term impact is important, but we must realize the current trade war will probably have long-term implications as well.

One of our main concerns for the U.S. economy was the Fed acting too aggressively in raising rates based on inflationary indicators that we believe were being driven by non-demand factors such as a weaker U.S. dollar, higher oil prices and tariffs. We now believe the threat of such a drastic economic downturn caused by this scenario is not as great when positive signs in wage growth continue to emerge. Despite our confidence in market fundamentals, we realize that investor emotions can be driven by the bombardment of headlines and observed market fluctuations. We remain committed to looking beyond these short-term factors and continue to make investment decisions for the long-term based on fundamentals. As always, any questions regarding your portfolio should be directed to your consultant.

As a reminder, we have recently completed our transition to a new reporting platform, Black Diamond. If you should have any questions upon receiving and reviewing your 3Q 2018 Quarterly Performance Report from Black Diamond, please contact your consultant or our office. On a final note, we are extremely excited to announce the addition of Chris Grude to our Ellis Team! With over 31 years of experience within the financial services industry, Chris joins our firm as a Senior Financial Consultant.