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Q4 2018
MARKET & ECONOMIC REVIEW

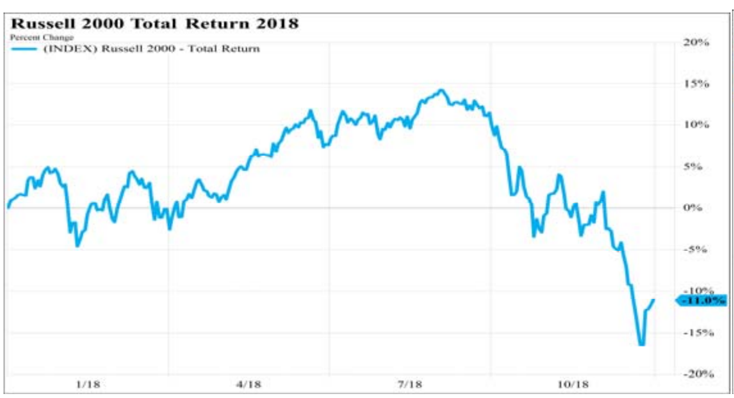
MAJOR EQUITY MARKET INDICES

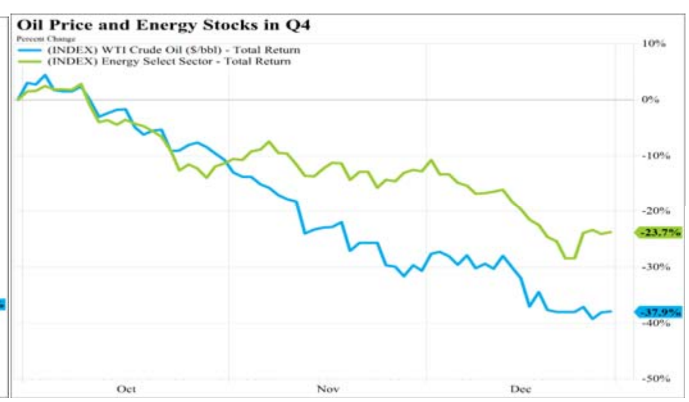
INDEX	DESCRIPTION	9/30/18	LOW CLOSE	HIGH CLOSE	12/31/18	QTD RETURN*
S&P 500	A market-capitalization weighted index of 500 large U.S companies.	2,913.98	2 ,351.10	2,925.51	2,506.85	-14.0%
DJIA	Dow Jones Industrial Average or "The Dow"; A price-weighted average of 30 major U.S. companies.	26,458.31	21,792.20	26,828.39	23,327.46	-11.8%
Nasdaq Composite Index	A market-capitalization weighted index comprised of over 3,000 companies, mostly in the technology and biotech industries.	8,046.35	6,192.92	8,046.35	6,635.28	-17.5%
Russell 2000	A market-capitalization weighted index tracking U.S. small-cap stocks.	1,696.57	1,266.93	1,696.57	1,348.56	-20.5%
NIKKEI 225	A price-weighted index comprised of Japan's top 225 most established companies.	24,120.04	19,155.74	24,720.62	20,014.77	-17.0%
MSCI Emerging Markets	An index comprised of 23 MSCI indices from emerging economies including Brazil, China, India, Mexico, Russia, South Africa, and the UAE.	1,047.91	934.80	1,047.91	965.67	-7.9%
Stoxx Europe 600	An index comprised of 600 companies based in one of 18 EU countries including Austria, Belgium, Denmark, France, Germany, Ireland, Spain, and the United Kingdom.	383.18	329.58	383.94	337.65	-11.9%

*** Excludes effects of dividends** **Sources: FactSet**

EQUITY MARKETS COMMENTARY

- Major U.S. stock indices all suffered significant losses during the fourth quarter of 2018, with the NASDAQ Composite down 17.5%, the small cap Russell 2000 small-cap stock index down 20.5%, the S&P 500 down 14.0%, and the Dow Jones Industrial Average down 11.8%.
- Small-cap stocks entered bear market territory in Q4, down 20.5%. As seen on the chart below, the Russell 2000 small-cap index was also down 11.0% on a total return basis for the year, its worst performance since 2008 and its fourth worst year ever since its creation in 1987.
- Most S&P 500 sectors were negative for Q4. The Energy sector was the worst performing, as oil prices fell 38% in the quarter (as seen below), but the Industrials and Technology sectors were not far behind. The defensive Utilities sector was the only positive sector in Q4, up 0.5%.
- The MSCI Emerging Markets Index was only down 7.9% in Q4, much less than most developed markets indexes, but lagged most of those same indexes for the whole of 2018. These markets suffered from concerns about fallout from global trading wars, especially since mainland China and Hong Kong combined comprise a significant part of the index.
- European stocks as represented by the STOXX Europe 600 were down 11.9% in Q4, besting most U.S. equity indexes (i.e. down less), but still lagged those same indexes for the year.
- Japanese stocks as represented by the Nikkei 225 index were down 17.0% in Q4 as tariff concerns reached their shores.





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FIXED INCOME RATES

DESCRIPTION	9/30/18	12/31/18	QTD CHANGE IN BASIS POINTS	DESCRIPTION	9/30/18	12/31/18	QTD CHANGE IN BASIS POINTS
90 Day Treasury Bill	2.19%	2.45%	26	Federal Funds Rate Target	2.00%-2.25%	2.25%-2.50%	25
10 Yr. Treasury Note	3.05%	2.69%	-36	Prime Rate (U.S.)	5.25%	5.50%	25
30 Yr. Treasury Bond	3.19%	3.02%	-17	LIBOR (3 month)	2.40%	2.81%	41
15 Yr. Mortgage Rate	4.14%	3.89%	-25	5-Year CD	1.88%	2.02%	14
30 Yr. Mortgage Rate	4.74%	4.50%	- 24	New-car Loan (48 month)	3.93%	4.58%	65

***One basis point is equal to 1/100th of 1% or 0.01%**

Sources: FactSet, Wall Street Journal, U.S. Treasury

FIXED INCOME MARKETS COMMENTARY

- Bonds posted nice gains in Q4 as interest rates fell in the quarter. The yield on the 10-year Treasury decreased from 3.05% to 2.69%, as equity investors fled to the perceived safety of bonds. Due to this decrease in interest rates, the widely followed Barclay's Aggregate Bond Composite Index posted a 1.6% return for Q4, allowing that index to post a 0.0% gain/loss for the year.
- High-yield bonds significantly underperformed in Q4, suffering from some of the same concerns affecting stocks – mainly fears of a looming economic recession and the perceived potential for increased corporate defaults. As seen on the attached chart, high-yield rates spiked in Q4 relative to safe U.S. treasuries (also called the "spread" to treasuries), and to the highest levels since the summer of 2016.
- The Federal Open Markets Committee of the U.S. Federal Reserve (the Fed) voted during its December meeting to raise the Fed Funds Target Rate range by 25 bps to a range of 2.25% to 2.50%, a move that was widely expected. This is the ninth rate hike since the Fed started raising the Fed Funds rates in late 2015 and the fourth rate increase in 2018. The Fed is still expected to raise rates further in 2019, but with the significant drop in stocks in Q4 amid concerns around slowing economic growth, some market observers are questioning the need for further rate increases. As usual, upcoming economic and inflation data will guide the Fed's decisions.
- The drop in mortgage rates in Q4 by roughly one-quarter percent should spell a bit of welcome good news for the housing market, which has seen weakness in existing and new home sales for most of 2018.

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U.S. ECONOMIC HEALTH

INDICATOR	DESCRIPTION	9/30/18	12/31/18	QTD CHANGE
Average Weekly Initial Claims for Unemployment Insurance (Thousands)	The number of new filings for unemployment insurance benefits. **Claims stayed low for another quarter, reflecting strength in the labor market.** *Most economists believe claims below 300,000 indicate a healthy labor market environment.*	207	231	+11.6%
Unemployment Rate	The percentage of total labor force that is unemployed but actively seeking employment. **The unemployment rate remains near low levels last seen in late 2000.** *The U.S. Federal Reserve targets a long-run unemployment rate of between 4.5% and 5%.*	3.7%	3.9%	+20 bps
Average Weekly Earnings	The average weekly salary earned by private, nonfarm employees. **Wages rose during the quarter, likely a result of a tightening labor market. This suggests more disposable income for consumers and may attract more workers to join the labor force.**	$937.40	$948.06	+1.14%
Index of Consumer Sentiment	This index reflects consumer attitudes towards the state of the economy. **Consumer sentiment decreased a bit but stays near post-recession highs.**	100.1	98.3	-1.8%
Manufacturers' New Orders for Consumer Goods and Materials (Millions) *	The number of new orders placed for consumer goods. **New orders increased, indicating higher demand for U.S.-produced consumer goods and validating still-high consumer confidence and low unemployment.**	$213,304	$216.957	+1.7%
Manufacturers' New Orders for Nondefense Capital Goods, Excluding Aircraft (Millions) *	This index is the producer's counterpart of new orders of consumer goods and materials. **New orders for nondefense capital goods increased only very slightly during the quarter**.	$68,491	$68,684	+0.0%
US Capacity Utilization: Manufacturing (as of 11/30/18)	The ratio of production capacity being used to produce finished products compared to the total capacity available. **Utilization decreased modestly and remains within the mid-70% range it has been in since 2012.**	76.6%	76.3%	-30 bps

***These items are as of 10/31/18, the date of the most recently published statistics (the federal government shutdown precluded more current data)**

Sources: Federal Reserve Bank of St. Louis, The University of Michigan, U.S. Census Bureau, U.S Department of Labor

U.S. ECONOMIC HEALTH

- Initial Claims for Unemployment Insurance ticked up a tad to end Q4, after having reached the lowest level since December 1969 to end Q3. Several other labor market indicators all point to a very tight labor market that is causing upward pressure on wages that will begin to either reduce corporate earnings or, if able to be passed along to consumers, show up in higher core inflation rates.
- As seen below, the U.S. created 312,000 new jobs in December - a relatively high level that does not happen very often. The 2018 monthly average job creation was 220,000, a 21% increase over 2017 and indicating a vibrant economy.
- As noted above, the December Unemployment rate ticked up a bit to 3.9% from the 3.7% seen at the end of Q3, which might seem surprising given the large number of new jobs created, as previously mentioned. This is due entirely to more people entering the labor force (likely due to more job openings at increasing wages) and thus causing the labor participation rate to increase.
- As seen below, U.S. Real GDP (i.e. adjusted for inflation) grew at a 3.4% rate for Q3 2018, the last reported data. Real GDP growth has averaged a robust 3.3% rate for the three reported quarters in 2018.