WINFIELD
ASSOCIATES

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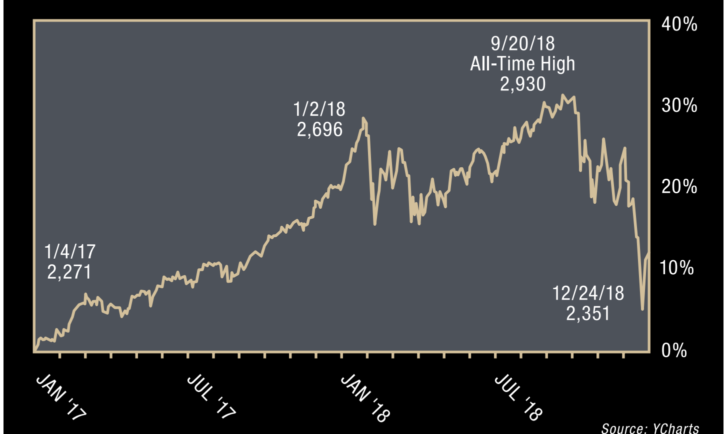
Customized Investment Portfolios and Private Wealth Advisory Services

MARKET COMMENTARY

When it comes to equity market volatility, 2018 was the inverse of 2017. Calm, upwardly trending equity markets throughout 2017 gave way to inconsistent and volatile price swings for most of last year. The S&P 500, like many equity indexes, did not have one day up or down more than 2% in 2017. In contrast, the S&P 500 had twelve days in 2018 when the index rose or dropped more than 2%. Five of those volatile days occurred in the first quarter, one in the second quarter, and six in the fourth quarter alone. December was particularly turbulent as the S&P 500 index experienced ten moves of at least 1%, most of them to the downside. The two-year graph of the S&P 500 index clearly illustrates the relatively steady, almost complacent performance of U.S. equity markets in 2017 followed by the volatility of 2018.

2017-2018 S&P 500 LEVEL % CHANGE



Source: YCharts

The S&P 500 reached its all-time closing high of 2,930 on September 20, up over 29% from where the index began 2017 and over 10% from the start of 2018. Concerns over slowing global growth and corporate earnings began to surface late in the third quarter, resulting in the downturn that persisted throughout the remainder of the year. For the fourth quarter, the index posted a loss of -13.5%, its worst quarterly performance since the Great Recession. Yet, despite the fourth quarter drawdown, the index finished the two-year period up almost 12%.

From the peak on September 20 to the trough of 2,351 on December 24, the S&P 500 index fell –19.7%. Most investors define a bull market as a period in which a market rises without experiencing a drop of 20%. Whether the longest bull market in history came to an end in December, or it merely tested the boundaries, does not particularly matter.

Bull markets tend to end with a recession, and while financial markets are signaling trouble ahead, the economy is not showing excesses that would normally foreshadow an end to the business cycle. The unemployment rate stands at 3.9%, up slightly from a 49-year low of 3.7% in November. Initial jobless claims, reported weekly, remain in the 200,000 – 230,000 range (as compared to 320,000 – 350,000 at the beginning of the Great Recession). Wages are rising at just above 3%, and inflation seems contained at close to 2%. A barrel of oil (West Texas Intermediate crude) is trading at $52, down -13% from the beginning of 2018 and down -32% from the peak in 2018. Consumer spending continues to grow at 3.5% and accounts for nearly 70% of US GDP. While most economists predict these trends will slow in 2019, the signs of an imminent recession are not clear.

In our October *Market Commentary*, we outlined four upcoming concerns for the fourth quarter. Three of the four concerns remain: rising interest rates, increased US protectionism, and slowing international growth. The fourth concern, US mid-term elections, has evolved into political gridlock and a government shutdown. The performance of financial markets in 2019 will almost certainly depend on the outcomes of these risks:

- ***Rising interest rates***
  At its December meeting, the Federal Open Market Committee (FOMC) hiked rates for the fourth time in a year, but marked down its median projection for 2019 rate hikes from three to two. Market reactions clearly indicated that this was too hawkish. In the coming months, investors will look for signals that the Federal Reserve is more concerned that the risk of causing recession through excessive tightening is far higher than the risk of inflation rising rapidly.

- ***Increased US protectionism***
  The meeting between President Donald Trump and China's President Xi Jinping at the G20 Summit in Buenos Aires on December 1 provided hope that the United States and China can reach a deal that avoids escalation in trade, economic, and geopolitical tensions. However, the G20 agreement provided little progress toward that outcome, other than a 90-day hiatus in the implementation of additional tariffs. Without progress in trade and intellectual property negotiations, the US will implement a tariff rate increase on $200 billion worth of Chinese goods on March 2, 2019.

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- ***Slowing international growth***
  Eurozone economic growth slowed considerably in 2018. The economies of Germany and Italy both contracted in the third quarter while overall Eurozone growth fell to an annualized rate of 0.6%. Adding to potential policy errors, the European Central Bank (ECB) ended its asset purchase programs in December. And, perhaps the greatest political risk facing international markets in 2019 will be the March 29 deadline for Brexit.

- ***Political gridlock***
  The US mid-term elections on November 6 led to a change in the control of the Congress, and within a matter of weeks, to a near standstill in the federal government. On December 22, the impasse between President Trump and the Democrats in the House of Representatives regarding the border wall forced a partial government shutdown, affecting approximately 800,000 federal workers. While the shutdown has had minimal market impact so far, the situation offers a preview of a divided government in the months ahead.

Ten years ago, the Federal Reserve Bank and the US Treasury commenced a great experiment in monetary policy expansion, using low interest rates, quantitative easing, and asset purchases to stem the effects of the financial crisis. The resulting economic expansion is less than six months away from becoming the longest in US history. While we recognize that at some point a recession is inevitable, we also note that the current recovery has been the slowest since World War II. As such, we believe that many of the usual excesses that require correcting in a recession are not forthcoming. Nonetheless, increased volatility in financial markets is an indication of increasing risk. While equity valuations appear attractive, we are mindful of potential financial vulnerabilities and the need to offset allocations to risky assets with higher than usual allocations to short term fixed income and cash.

RETIREMENT CONTRIBUTION LIMITS

	401(k)	IRA
Annual limit per individual	$19,000	$6,000
Age 50+ catch-up amount	$6,000	$1,000
Penalty-free access, if needed	Yes (via a loan)	No

REVISED SALT DEDUCTION

The Tax Cuts and Jobs Act of 2017 put a $10,000 annual cap on the deduction for state and local taxes. The popular deduction (known as SALT) includes state and local property taxes as well as state and local income taxes. The change is likely to affect most taxpayers who itemized deductions in the past, especially those living in higher tax states. We recommend consulting with your tax professional earlier this year to discuss how these changes might affect your 2018 federal income tax bill.

MARKET PERFORMANCE

	4Q 2018	2018
Dow Jones	-11.3%	-3.5%
S&P 500	-13.5%	-4.4%
Nasdaq	-17.3%	-2.8%
Russell 2000	-20.2%	-11.0%
MSCI EAFE	-12.5%	-13.8%
Barclays Agg	1.60%	0.0%

WHEN TO WORK WITH WINFIELD

PRIVATE INDIVIDUAL INVESTORS
- Manage accumulated wealth, inheritances and settlements

ENDOWMENTS AND FOUNDATIONS
- Manage assets with a long-term growth strategy while meeting investment policy requirements

BUSINESS OWNERS
- Customize investment portfolios to lessen risk of concentrated assets
- Defer taxable earnings in profit sharing plans
- Manage and advise 401(k) plans

BUSINESS PROFESSIONALS
- Customize investment portfolios, manage stock options and consolidate 401(k)/IRA plans to lessen risk of concentrated assets

RETIREES
- Customize investment portfolios with the option of drawing income
- Management of IRAs, trusts and taxable accounts

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