Market Update

December 2018

Some Coal in Our Stockings This Year

Suffice it to say, events of the week of December 17 caused an increased level of angst in the financial markets. First, comments by the Federal Reserve were not as accommodative for 2019 as many investors hoped and anticipated. Our perception is it wasn't necessarily the number of expected rate hikes that was the primary issue, but rather the perceived lack of understanding by the Fed that financial conditions are tighter than they realize. Global liquidity has been contracting while a variety of additional headlines including Brexit, the price of oil, the slope of the yield curve and the climate in Washington have been in play. Many have become concerned that a recession will be in the cards much sooner than the post-2020 scenarios many economists have been prognosticating. These various dynamics, combined with a "buyers' strike" and a significant, continued wave of tax loss selling as we near year-end, have resulted in additional equity pressures while bond prices have actually rallied, resulting in lower interest rates on bonds of most types.

As we enter 2019, volatility will likely remain elevated due to continued headline and event risks. Markets will be looking for direction on multiple fronts and we believe should calm with a Fed pause, a more tranquil geopolitical horizon, including a China trade deal, and proof that corporate earnings will continue to be on the rise versus recent fears of contraction. Assuming a recession is not imminent, what has transpired has seemingly been due more to a decline in liquidity as mentioned than one in economic activity per se, including an increase in the cost of capital, albeit over a relatively low starting point. That being said, what has been the key driver the last few years, the American consumer, has continued to be strong, although the impact of the decline in the stock market could take a toll at some point. Lastly, on the international front, although emerging markets may be in the midst of a bounce, Europe will likely be a continued headwind.

From the domestic perspective, the government shutdown as of midnight on the 21st adds an interesting layer to the current circumstances. Shutdowns are not unprecedented. The typical length has been one to five days, with the longest being twenty-one in 1995/1996. The current scenario has somewhat of a unique wrinkle in that Congressional membership is slated to shift next week. Historically, the result has been a limited disruption in government services as the shutdown avoids "mandatory programs" and pertains to what have been deemed "non-essential services". Overall, this concerns approximately 25% of government spending. Given the current atmosphere of anxiety, this could certainly add to the short-term volatility despite the typically limited economic impact. However, it does make one at least contemplate what this portends for the already tense environment in Washington over the next two years, if not longer.

Markets like this are not overly unusual; patience during them, even though potentially very difficult to maintain, is usually a virtue. Please keep in mind that your Country Club Trust Company/Tower Wealth Managers team is here to help in any way we can.

Enjoy the holidays, and best wishes for a happy 2019!

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