Hamilton-Bates
Market Update

March 1, 2019

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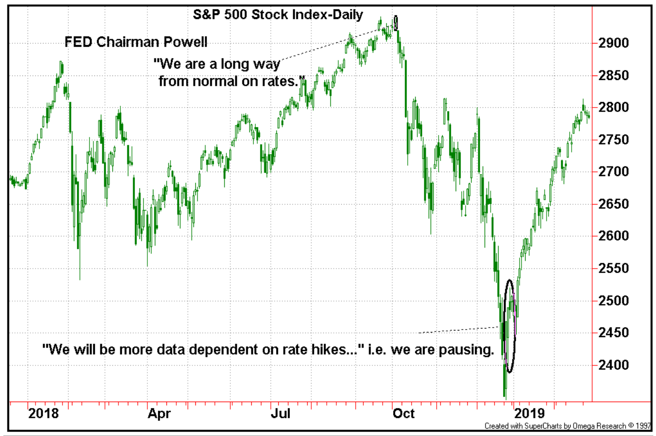
The market is now poised for its 10th straight week of gains. We've not made up the losses from the 4Q of 2018 just yet– but its getting close. But is this as good as it gets? Or are things just getting good? The Fed had its foot on the throat of the markets last year, but fortunately it seems it took its foot off before lasting damage was done (to the market and the economy). We fully expect the market to recover to new highs in the fullness of time, but its not likely to be as linear as it has been these past several weeks.

It really was the Fed that was the problem as we maintained last year. <u>You can essentially boil down the massive rally we have seen to the complete 180-degree flip by the Federal Reserve</u>. They went from **doggedly** pursuing and talking up rate hikes in Oct-Nov despite slowing data and a collapsing market, to a flip-flop around the Christmas Holiday. It was indeed a Christmas Market Miracle. All it took was a 20% market decline coupled with collapsing sentiment, and a President more than willing to place the blame squarely on their heads for them to finally cave.

The chart on this page shows the S&P along with Chairman Powell's comments that neatly bracket the market's sell-off. The Fed caused it, but in the end they reversed course before sending the economy into a recession.



The above chart illustrates just how powerful the Fed is; and how much monetary policy affects the stock market. The market peaked in October when the Fed chair spoke what were deemed 'overly hawkish' comments; and finally bottomed when it became apparent they (the Fed) were changing course on rate hikes.

Earnings, Interest Rates, and the Economy

For all the volatility in the stock market, both UP and DOWN, the overall economy and earnings really haven't moved all that much. GDP came in at 2.6%, down from 3% expectations, but not nearly as bad as some expectations that called for less than 2%. Earnings growth has come down from the lofty levels of 2018, as expected given the tariff uncertainty and the fact that much of Europe and Japan is seeing a pretty sizable slowdown. The market has come back largely on the back of the Fed's flip-flop, earnings expectations have not rebounded nearly as much. The coming weeks will show weather earnings can rebound given the Fed's change, and what appears to be a clear improvement in the US-China trade situation. It seems very likely that a deal will be reached in the next month or two. The housing market remains very weak, so the spring selling season could tell us much about the underlying strength of the economy. A poor season might have us tempering growth expectations for the remainder of 2019.

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Market Outlook and Investment Strategy
Nothing makes us happy like seeing the market rally, so rally has been a very welcome sight. Going back to comments written around Christmas, we were expecting a bounce, although not as robust as what we have seen. But at that time we could not have know the Fed was about to do a complete about face! Needless to say, the Fed's decision to pause has taken a lot of pressure off the stock and bond markets, and should help beleaguered sectors like housing.

The strength of the rebound tells us it has much more to go, even if we see a pullback in the coming weeks. We have had 10-weeks of rally, so some give back would be understandable. We did some buying in late December and in January, and we will look to deploy more capital and get more aggressive should we see that pullback.

Money-flow tells us many investors and managers sold late last year and are now missing this rally. There are a lot of folks that need to get back in at some point. This won't prevent a pullback, but is likely to keep it much more shallow than it otherwise might be after such a large move up. 3-5% would seem to be about what we could see when the market needs a rest. If a trade-deal gets done, and the Fed doesn't do yet another about face, we could see continued gains for the rest of 2019.

Market Chart—S&P 500 Moves Above Key 200-Day Average

The S&P finally cleared its 200-day average, the level which triggered its December slide when the market failed to move above it. That failure saw the massive selling wave in December. The move above it is a big positive for the market, and we expect new highs eventually, but there are some concerns. The buying volume continues slow down on the way up (not shown), and the market is now very overbought given its big run. But we don't want to get too negative. There are pullbacks, and then there are beat-downs. What we saw in last year's 4Q was a beatdown. Right now even a small pullback could easily do the job. In fact, a small pullback here would actually be of great benefit, cooling off an overheated market before it races into a situation where there's little choice but to start taking profits in such a way that the selling becomes self-sustaining. As long as one of the familiar moving averages (50-day/ 65-day) serves as a support during any stumble, the bigger trend is still a bullish one.