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4th Quarter 2018 Recap

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After a long period of respectable returns, many equity investors experienced losses during the fourth quarter of 2018. The fourth quarter was filled with a great deal of uncertainty. Interest rate hikes and trade wars caused major concerns. As a result, U.S. equity markets posted their worst October numbers since the financial crisis of 2008. Even though equity markets calmed down in November, much of this quarter's losses came during December. In that month, all three major U.S. indexes dropped at least 8.7%. The Dow Jones Industrial Average (DJIA or Dow) and S&P 500 also recorded their biggest monthly loss since February 2009.

The S&P 500 and NASDAQ dropped 14% and 17.5% respectively in the fourth quarter. These were their worst quarterly performances since the fourth quarter of 2008. The Dow recorded its worst quarter since the first quarter of 2009, falling nearly 12%. As bad as they were, the final numbers do not fully explain just how crazy December really was for investors. Based on the lowest levels of the S&P 500 on Christmas Eve, the index was down over 20% from its record high on an intraday basis. This briefly met the requirement for a bear market. The stock market would then come rising back in the next session, with the Dow over 1,000 points on December 26. This marked its biggest point gain ever.

Many market analysts felt the declines were driven by concerns of an economic slowdown and fear the



MONEY RATES (as posted in Barron's 12/31/2018)		
	LATEST WEEK	YR AGO
Fed Funds Rate (Avg. weekly auction -c)	2.36%	1.42%
Bank Money Market -z	0.22%	0.14%
12-month Cert -z	0.88%	0.42%

c- Annualized yields, adjusted for constant maturity, reported by the Fed Reserve on a weekly average basis. z- Bankrate.com (Source: Barron's; bankrate.com)

Federal Reserve might be making a monetary policy mistake. In December, the Fed raised interest rates once again by 0.25%. This elevated the U.S. Federal Funds rate range to 2.25 - 2.50%. The Fed has forecasted additional rate hikes in 2019 which will not be helpful for equity markets.

The continuing concern over ongoing trade negotiations between China and the U.S. also pressured equities this quarter.

While corrections (defined as a drop of over 10%) in equity markets are not uncommon, intraday volatility was one interesting characteristic of the fourth-quarter market. During the fourth quarter, the Dow had a record number of sessions with intraday 500+ point swings. That is roughly 2% of the current level of the Dow. The Dow had five consecutive sessions with 500+ point swings from December 4 to December 11. This unusually high intraday volatility attracted a lot of media attention and it seemed as if the stock market was one of the main discussion topics every night on the news (Seeking Alpha 12/2018).

	MONTH	QUARTER	2018
Dow	-8.7%	-11.8%	-5.6%
S&P 500	-9.2%	-14%	-6.2%
Nasdaq	-9.5%	-17.5%	-3.9%

(Source: Barron's 12/31/18)

A Review of 2018

After 2017 featured strong equity returns and an environment of very low volatility, 2018 tested the commitment of long-term investors. In 2018, the S&P 500 and Dow fell for the first time in three years, while the NASDAQ broke a six-year winning streak. 2018 was characterized by the return of volatility, record highs, and sharp reversals. It also resulted in the first time the S&P 500 posted a decline after rising in the first three quarters. Additionally, it was the first time, since 1978, that the Dow finished out the year in the red after rising in the first three quarters.

According to Morningstar Research, results for 2018 “were even worse for those invested in markets outside the United States.” The MSCI EAFE Index (an equity - index which captures large and mid-cap representation across 21 Developed Markets not including the US and Canada) plunged about 14% in U.S. dollar terms. Morningstar noted that a variety of concerns hurt international markets. These included local political issues and troublesome economic data. Many foreign markets also posted deeper losses than those in the U.S. For example, China’s Shanghai Composite entered a bear market in June and declined nearly 25% in 2018. The Shenzhen Composite (which includes many of the country’s tech firms) dropped by over 33% for the year.

A variety of problems affected foreign-stock funds. Economic growth in the U.S. was much stronger than that of Europe, where the trends that finally had moved in a positive direction reversed course, with growth

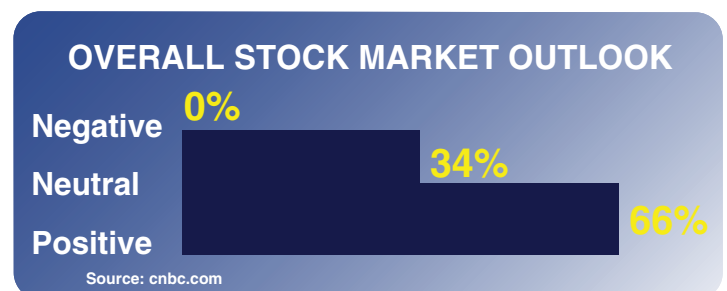
rates down to near zero or even dipping into negative territory in some countries. Europe's biggest market, the United Kingdom, has been stressed by uncertainty over the details of its path to exit the European Union. Political difficulties in Italy and other European countries did not help matters.

For the past decade, income vehicle returns have been significantly lower than equity returns and cash equivalents brought in very little. Although they add less return, low return cash equivalents and income vehicles provided less volatility and stress. Many investors abandoned diversification and fully allocated to potentially higher returning stocks. This strategy can be advantageous when markets rise, but dangerous when they fall. Sometimes, investors are emotionally driven to change their allocations, but doing so could add additional risk.

2018 was a confusing and difficult year for investors after almost a decade of strong equity returns. After the sour year-end close, it is easy to forget that the Dow recorded 15 new highs in 2018, (ahead of the annual average of 11 new highs per year since inception). While the Dow reached more new highs in 2017 (71 in total, more than any year in history), there have been 53 calendar years when the DJIA notched at least 1 new high and 70 when none were recorded. For most investors, 2018 fully tested their commitment and patience (Seeking Alpha 12/2018).

2019 Outlook

Stocks may be coming off their worst year since the financial crisis of 2008, but for 2019, many analysts feel that equity markets will head higher. Over 65% of 29 respondents to CNBC’s exclusive “Halftime Report Stock Survey” said their overall stock market outlook is positive. Over 58% feel that equities look cheap at current valuations. CNBC noted that no one responded that he or she believes equities are overvalued at current levels. About 41% believe stocks are correctly valued, and nearly 60% felt current valuations look cheap, which indicates an overall bullish sentiment (CNBC 1/7/2019).



Key Points

1. Q4 finished 2018 with poor returns for equity investors.
2. After a quiet 2017, volatility returned to equity markets in a historic way in 2018.
3. The Fed raised U.S. Fed Fund rates to 2.25 - 2.50% in December and could raise interest rates again in 2019.
4. Key economic data indicators are still reasonable.
5. Analysts suggest 2019 will have positive equity returns.
6. Investors need to still be very cautious and watchful.
7. Focus on your personal goals and call us with any concerns.

Forbes, in a 2019 Outlook asked, "What do stocks do after a down year?" They felt 2018's decline might not be the best forecast and shared, "Let's pull out all the down years from 1926 through 2017, of which there were 24. The average return in the year following a down year was 10%, the same as the overall average." They also shared, "Uncertainty about the future course of stocks is large, so investors should fall back on a few fundamental principles. Diversification of investments reduces risk" (Forbes 1/5/2019).

Barron's 2019 Outlook reported, investors will be happy to bid good riddance to 2018, a stressful year marked by two stock market corrections, rising interest rates, an ugly trade battle, and growing fears that a bear market lies just around the corner. All 10 of the market strategists that Barron's consulted in late December had 2019 targets for the S&P 500 index finishing the year higher (Barron's 12/14/2018).

Seeking Alpha notes that, "Forecasting how 2019 will play out may be pure guesswork under the current circumstances." They also add that, as we begin the year, there is a shut-down of important U.S. government services and a new political landscape (a Democratic Congress). They also report that although the Federal Reserve has raised rates and the global trade war is far from being resolved, current economic indicators are not pointing to an immediate recession. They cite that, on the employment front, we now have a tightening labor market with unemployment down to 3.7%. They share that, The Index of Leading Economic

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Interest Rates Are Still Critical

Three years ago, the Fed moved away from the near-zero rate that had been in place since the days of the global financial crisis. In December, the Fed raised interest rates for the fourth time in 2018 to move the target range for its benchmark fund to 2.25% to 2.5%. As of that session, Fed officials forecasted two more hikes in 2019, down from three rate raises previously projected. This is because Gross Domestic Product (GDP) was seen as rising 3% for the full year of 2018, down one-tenth of a percentage point from September, and forecasted for 2.3% for 2019, a 0.2% point reduction.

While investors wanted certainty about rate hikes ending, the Fed included in its statement that further "gradual" rate hikes would be appropriate. Charlie Ripley, senior investment strategist for Allianz Investment Management said that "while this was a

dovish hike from the stance that the Fed was in before, this is somewhat not as dovish as many participants probably wanted.” He also added that “It would have been a difficult move for the Fed to completely remove some of the 2019 hike expectations, but I think they’re making the message clear that they’re going to remain more data dependent as we go into 2019.” The Fed’s official meeting notes described economic growth as “rising at a strong rate” and therefore the door is still open for further rate hikes (CNBC).

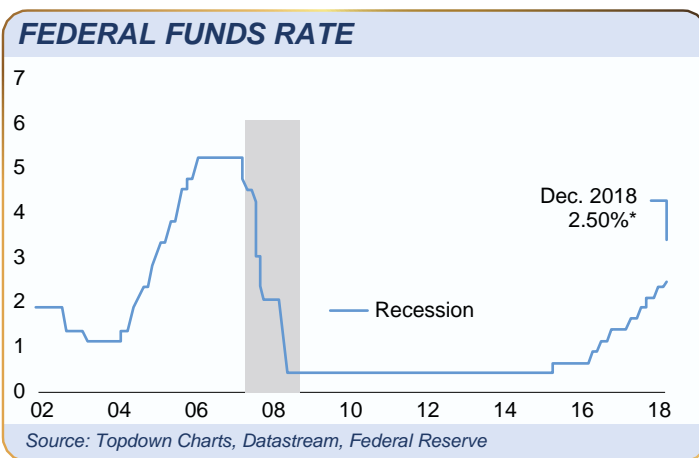
Besides potential rate hikes, further trade wars with China can keep markets quite volatile in 2019. Trade wars and signs China’s economy is slowing have added to the global uncertainty. Interest rates, trade wars, and worldwide growth rates should all be on an investor’s watch list for 2019

fears are resolved in 2019, that it could be a good year for stocks. While strategists see volatility continuing in 2019, they felt that the biggest worries for investors are still trade wars and the Fed’s interest rate movements. While many analysts remain optimistic, investors should prepare for continued volatility and not a straight-line uptrend.

Knowledge is Powerful

While the nightly news and financial tabloids like to use harsh and scary language to attract viewers, oftentimes their quick views of equity market performance include media magnification, which is the act of making something look larger or more important than it really is.

Currently, equity markets are volatile and have experienced a correction (some are even in bear market territory) but not a crash. As our chart shows, most corrections are not market crashes. The October 19, 1987 market drop of 508 points (a 22.6% decline) clearly was a market crash. The same percentage decline for the Dow, if it happened on January 2, 2019, would have been over 5,000 points (which clearly did not happen). It is often said that an emotional investor can make decisions that might not work out best. An informed and knowledgeable investor can often be less emotional. Differentiating a correction (with a frequency on average of once a year) from a bear market (with a frequency on average of once every three years) can help investors when making decisions (NASDAQ).



Conclusion:

What Should an Investor Consider?

While numerous analysts remain optimistic, investors should not expect a straight line uptrend. Corrections and bear markets will always be a part of the investment sequence. Although the old Wall Street joke can remind us that 10 out of 9 analysts can correctly predict the next recession, predicting exactly when equity markets will start back upward is near impossible. Investors with very long-time horizons of 10 to 20 years or longer can often accept more risk than those with shorter horizons. While past performance is no indication of future performance it still gives us data to consider. Based on the DJIA, 10-year returns since the index’s inception have averaged over 83%. This year, despite the negative performance, the 10-year return is an impressive 165%. How is that possible? It’s because this most recent 10-year period began after the DJIA was beaten up during the financial crisis. Since then, the DJIA has risen from approximately 8,800 to over 23,000 (Seeking Alpha 1/4/2019). CNBC reported on January 1st that some strategists are saying if the stock market’s two worst

Most correction are not crashes.

In perspective...
what a 22.6% declines means in Dow points - then and now...

October 19, 1987 crash

↓ 508 points



Same % decline if it happened on Jan2, 2019

↓ 5,011 points

What Should Investors Do?

Completely avoiding market risk may not be appropriate for most investors and today’s traditional fixed rates might not help you achieve your desired goals. Most investors attempt to build a plan that includes risk awareness. Often, this can lead to safer but lower returns. Traditionally, bonds have been a nice

hedge against market risk, but with interest rates projected to rise, investors must be extremely cautious.

**For 2019, let's focus on
YOUR personal goals and strategy.**

We focus on your own personal objectives.

During confusing times, it is always wise to create realistic time horizons and return expectations for your own personal situation and to adjust your investments accordingly. We try to understand your personal commitments, so we can categorize your investments into near-term, short-term and longer-term.

Now is the time to make sure you are comfortable with your investments.

Equity markets will continue to move up and down. Even if your time horizons are long, you could see some short-term downward movements in your portfolios. Make sure your investment plan is centered on your personal goals and timelines. Peaks and valleys have always been a part of financial markets and it is highly likely that trend will continue.

**CAUTION in 2019
is still the principal notion for investors.**



Investors need to be prepared. Market volatility has caused concern, but panic is not a plan. Market downturns happen and so do recoveries. This is the ideal time to ensure that you fully review and understand your time horizons, goals and risk tolerances. Looking at your entire picture can be a helpful exercise in determining your strategy

Common Market Terminology	
% Drop	Typically Referred to as:
Less than 5%	Dip
5 to 10%	Pullback
10% +	Correction
20% +	Bear Market

Stock market crash - a sudden and significant decline in equity prices of a very short period of time.

Recession - an economic term that refers to a general slowdown in economic activity, generally defined as two consecutive quarters of negative GDP growth. While the effects of a recession often cause the stock market to fall, **the term itself doesn't refer to a specific type of market activity.**

Discuss any concerns with us.

Our advice is not one-size-fits-all. We will always consider your feelings about risk and the markets and review your unique financial situation when making recommendations. **If you would like to revisit your specific holdings or risk tolerance, please call our office or bring it up at our next scheduled meeting.**

We pride ourselves in offering:

- consistent and strong communication,
- a schedule of regular client meetings, and
- continuing education for every member of our team on the issues that affect our clients.

A skilled financial advisor can help make your journey easier.

Our goal is to understand your needs and then try to create a plan to address those needs. We continually monitor your portfolio. While we cannot control financial markets or interest rates, we keep a watchful eye on them. No one can predict the future with complete accuracy, so we keep the lines of communication open with you. Our primary objective is to take the emotions out of investing. We can discuss your specific situation at your next review meeting or you can call to schedule an appointment. As always, we appreciate the opportunity to assist you with your financial matters.

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Sources: Barron's, Forbes, CNBC, Seeking Alpha, Morningstar, cnbc.com, NASDAQ, Market Watch; Academy of Preferred Financial Advisors, Inc. ©

FAN TEAM UPDATE

Winter 2018

The Financial Advisors Network Team has been busy working hard and having some fun too!

Here's what we've been up to lately...



Chargers Game in LA



Touring CU Boulder



Skiing in Winter Park



New Client & Advocate Dinner



FAN Christmas Party



Anaheim Ducks Game

Upcoming Events

Social Security & Medicare Seminar



Curious about the effects of Social Security on your financial situation? You and your friends are invited to this informative education event. Learn about how Social Security may affect your individual position.

Retired long-time Public Affairs Specialist at the Social Security Administration in Orange County, Frank Van Nostrand will present the “Nuts and Bolts” of Social Security and Medicare. Bring any questions you may have – Frank is an expert!

The seminar will be held **Wed, Feb 20 from 6:30-8:30pm** in the conference facilities at Financial Advisors Network located at 1432 Edinger, Suite 200 in Tustin.

Frank Van Nostrand is not affiliated with Financial Advisors Network, Inc. The information to be discussed is not intended to be a substitute for specific individualized tax or legal advice. We suggest that you discuss your specific situation with a qualified tax or legal advisor.

Property Inheritance Seminar

This seminar will be presented by Nicole Newman of Newman Law Group, our strategic alliance. She will provide important details on how to choose the right successor trustee. This is a great opportunity to plan for your loved ones. Nicole’s specialty is guiding families on how to choose the right successor trustee, even in the most difficult circumstances. Family members and heirs welcome.

The seminar will be held **Wed, Feb 27 from 6:30-8:30pm** in the conference facilities at Financial Advisors Network located at 1432 Edinger, Suite 200 in Tustin.

Nicole Y. Newman, Newman Law Group, and Financial Advisors Network, Inc. are separate entities. There is no obligation to use their services. The information to be discussed is not intended to be a substitute for specific legal advice. We suggest that you discuss your specific situation with a qualified legal advisor.

First Trust Deed Info Session



You are invited to our NEW First Trust Deed informational session! The informational session will be presented by Rod Kamps and our new Strategic Alliances Mitch Ohlbaum and David Rosenberg of Macoy Capital Partners, Inc. In this informational session you will learn about: what first trust deeds are, how they may be beneficial in a rising interest rate market, the potential risks associated with First Trust Deeds, and our strategic alliance with Macoy Capital Partners, Inc.

The seminar will be held **Wed, Mar 6 from 6:30-8:30pm** in the conference facilities at Financial Advisors Network located at 1432 Edinger, Suite 200 in Tustin.

First Trust Deed investments will be discussed. Investing in First Trust Deeds involves unique risk, including possible loss of principal. There is no assurance that the techniques and strategies discussed are suitable for all investors or will yield positive outcomes.

For more information or if you would like to attend any of these complimentary seminars, please contact us at macaela@fanwmg.com or (714) 597-6510.

Don't Forget!

**Come in for your Complimentary
Financial Check-up.**

We are happy to meet with you for a financial check-up, and will help you bridge your investments with your taxes. Make sure all the pieces of your finances are working together properly!

Contact Us

(714) 597-6510 or info@fanwmg.com

We would be happy to schedule a complimentary appointment.



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