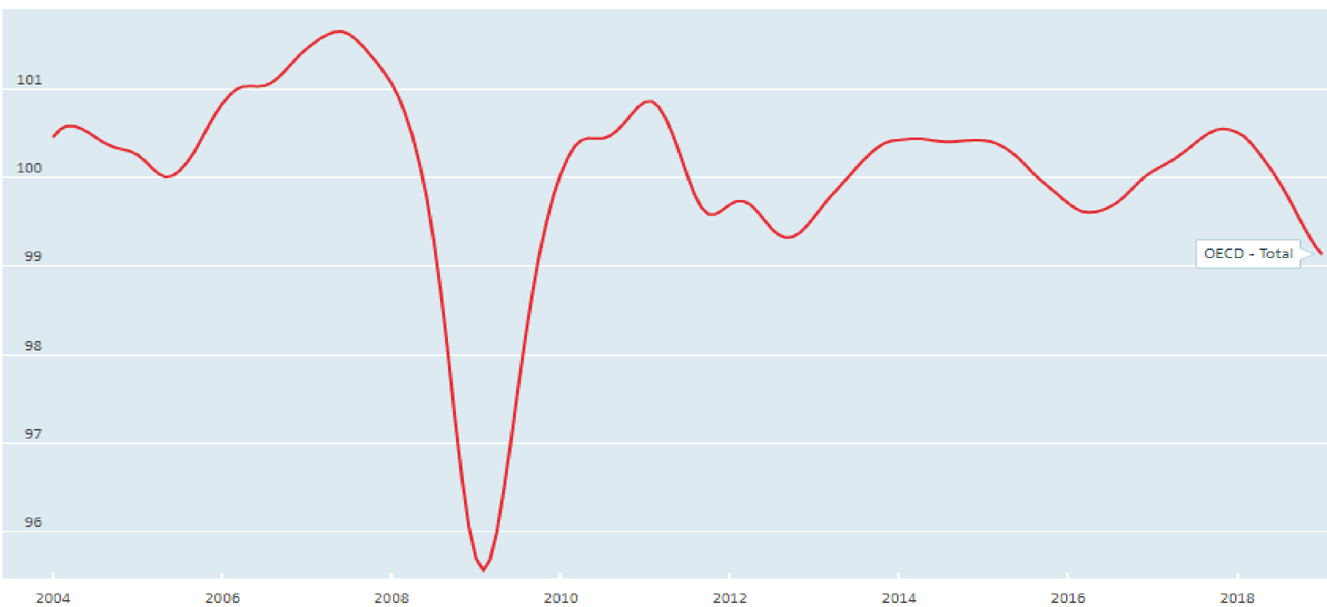
Mar 20, 2019

Market Insights for Week Ending Mar 15, 2019

"A Crazy Game of Poker"

Poker is a game that has gained popularity over the past 15 years, enough so that you can occasionally turn on ESPN and watch poker tournaments where the winner can walk away with over $5 million and a cool bracelet that would make Liberace take notice. The main game played in these tournaments is No-Limit Texas Hold'Em. In Texas Hold'Em, each player receives two cards that are dealt face down and then an additional three are dealt face up as community cards, making a five-card hand. After the initial deal, players begin betting and there is a total of two more cards that are dealt face up for a total of 7 cards, 5 community cards and 2 held by each player. Once all 7 cards have been dealt, the player who can create the best poker hand wins the pot. It is a game that requires you to play your opponent as much as simply playing your cards. Texas Hold'Em is also unique in that you can bet all your chips at any time in the game, so understanding your probability of success and acting accordingly is a major part of being a successful No-Limit player. This also makes the amount of chips you have at any moment a very important factor in the game. Those with larger stacks can play more aggressively without the fear of being wiped out by a bad bet. Once you are out of money, the game is over.



Source: data.oecd.org

The chart above shows the Organization for Economic Co-operation and Development (OECD) Composite Leading Indicator (CLI) going back to 2004. The OECD CLI is designed to provide early signals of turning points in business cycles. The CLI in January fell for the 16th straight month to 99.25. According to Ned Davis Research Senior Economist Alejandra Grindal, this was its lowest level in nearly a decade and its eighth straight month below its long-term average of 100. Based on the chart above, its fair to say that global growth is slowing.

Why Do We Care?

So how do poker and the OECD CLI have anything to do with one another? First, imagine being a player in a game of poker that has a slight twist from the rules we outlined above. In this game, once YOU run out of money, your game is over, and you must leave the table. However, your opponents have unlimited funds. Would you sit down at this table and attempt to play in this game? If so, would you feel confident in your read of their respective bets knowing that they aren't playing with any risk to themselves? One could argue that the risk to your capital by playing AGAINST opponents with unlimited resources is so high that you shouldn't play a single hand. While most likely no one would play poker under these terms, investors are playing a similar game right now, they just don't know it.

2018 was filled with hope and optimism offered by global central banks. Forecasts of growth and reflation were everywhere, along with forecasts of central bank interest rate hikes to keep inflation in check. Fast forward to today and things are certainly different. In January, the Federal Reserve lowered its expectation for rate hikes in 2019 and introduced the possibility of slowing or stopping the reduction of its balance sheet. China's central bank injected approx. $1 Trillion, with a "T", of liquidity into its financial system in January. Two weeks ago, the European Central bank opened the door to restart their version of Quantitative Easing. Point being, these aren't the actions of those who are concerned about strong growth turning into inflation. Who knows, maybe they have seen the chart above. And we must not forget that these players, the Fed, Chinese Central Bank and the ECB are playing with unlimited funds.

This is as good a time as any to remind ourselves that the market doesn't equal the economy. The ongoing rally that started on December 24th, 2018 has certainly been accelerated by the acknowledgement of central banks that more easing may be on the way. In fact, things seem so backwards that the worse the economic data, the better the market reaction since it may mean that central banks react with even MORE aggressive easing. The Fed concluded their two-day policy meeting today, Wednesday, Mar 20th, and forecasted no more rate hikes in 2019 and one in 2020, along with an end to its balance sheet run-off by September 2019. There is a strong sense among strategists this type of forecast could be the fuel needed for an additional leg higher in equities, with or without fundamental backing.

While investing certainly isn't a game of poker, the two share many similarities. One parallel that we focus on intently is our assessment of risk and the amount of capital that we will expose to that risk at any particular time. This assessment drives our equity over/underweights. Our goal is to be fully invested when risk is not excessive, valuations are fair and the long-term trend of the market in rising. We underweight our equity exposure when risk is excessive, valuations seem high and when the long-term trend has turned down. As the potential for aggressive monetary policy has been re-introduced, we have continued to evaluate our investment thesis to determine if changes to our portfolios are warranted. Any strategy change will be accompanied by additional communication via webinar.

Weekly Focus – Think About It

"I'd rather regret the things I've done than regret the things I haven't done."

-Lucille Ball

Market Activity

Performance last week for the four major asset classes were:

- U.S. Stocks – Russell 3000 (IWV) – Gain of 2.81%
- Developed Foreign Markets (EFA) – Gain of 2.76%
- Emerging Markets (EEM) – Gain of 3.46%
- Fixed Income (AGG) – Gain of .25%

(Note: performance is based on the change in price plus dividends)

Last Week's Headlines

-Global equities rallied across the board, led by energy and tech. Treasury yields were little changed as investors awaited clarity on US-China trade talks.

-The UK Parliament voted to delay Brexit and against leaving the European Union in a "no-deal" exit after Prime Minister May's withdrawal was rejected a second time.

-China's economic data for the first two months of 2019 showed signs that growth might have bottomed out.

Eye on the Week Ahead

-The FOMC forecasted no more rate hikes in 2019 and one in 2020. In addition, the bank said it would end its balance-sheet runoff by September 2019.

If you have questions please contact a member of HCM's Wealth Advisory Team:

Mike Hengehold (Mike@HengeholdCapital.com)

Casey Boland (Casey@HengeholdCapital.com)

Jake Butcher (Jake@HengeholdCapital.com)

Jim Eutsler (Jim@HengeholdCapital.com)

Greg Middendorf (Greg@HengeholdCapital.com)

Steve Hengehold (Steve@HengeholdCapital.com)

Doug Johnson (Doug@HengeholdCapital.com)

Disclaimer
Any tax or other advice contained in this document, including any attachments, is not intended and cannot be used for the purpose of avoiding penalties under Internal Revenue Code. No action should be taken on any information contained in this message without first consulting with your tax/legal advisors regarding the tax/legal consequences for your particular circumstances.

Additional Notes:

- The Standard & Poor's 500 (S&P 500) is an unmanaged group of securities considered to be representative of the stock market in general.
- Opinions expressed are subject to change without notice and are not intended as investment advice or to predict future performance.
- Past performance does not guarantee future results.
- You cannot invest directly in an index.
- Consult your financial professional before making any investment decisions.

• • •