



QUARTERLY MARKET COMMENT Third Quarter 2018

The aging bull market was unaware that the 3rd quarter typically experiences more negative than positive returns. Historically, September alone has been down 54.4% of the time with an average decline of 1%. With the tug of war continuing between politics and fundamentals, U.S. large cap stocks charged ahead with a gain of 7.20%. Year to date through September 30th they were up 8.99%. U.S. small caps had been the darlings through the 2nd quarter, but lost some steam in the 3rd quarter ending up 3.26%. Year to date small cap stocks were still the best performing with a return of 10.49%. Small cap stocks specifically benefited from the trade tensions in the 2nd quarter. Whereas large, medium and small stocks are all benefiting from the boost in tax cuts that took effect this year. The momentum in the market is still favoring growth stocks over value stocks. However, valuations in growth are very much stretched right now. International developed markets eked out a positive 0.76% return for the quarter. Emerging markets struggled to a lesser degree in the 3rd quarter than they had in the 2nd quarter, but still experienced a negative quarter, down 2.02%. Both are in negative territory for the year and their returns have been impacted, in part, by the short-term strengthening of the dollar. Long-term the dollar has been weakening against other currencies and this is projected to resume at some point. Turning to fixed income, the Federal Reserve continued their objective of raising the federal funds rate by one-quarter of 1% for the third time this year (8th increase since 2015) and another is projected in December. The direct impact of the Fed normalizing interest rates is an increase in short-term rates and a negative market adjustment along the yield curve for other bonds with longer maturities. U.S. Government bonds ended the quarter down 2.04% and year to date it's return was -4.64%. Domestic real estate remained fairly flat for the quarter and was slightly positive for the year at 1.22%. Global real estate, impacted by the stronger dollar, was slightly negative for the year at -0.94%. Commodities were the laggard of the pack and continue to be in negative territory for the year. The quarter was surprisingly calm with 0 days of 1% volatility moves. The last +1% day move was June 1st. Economist don't expect this to last going into the 4th quarter with mid-term elections and trade agreements being negotiated, but then again that's what they said about the 3rd quarter.

The U.S. economy continues to chug along and has quickened its pace in 2018 with 4% growth in the 2nd quarter and roughly 3% year-over-year. Strong spending by consumers and businesses and a sharp improvement in the trade deficit all contributed. Much of the other economic data presents a positive and healthy environment that is fueling an upward stock market and is supporting the Federal Reserve's objective of increasing the federal funds rate. So what's next?

The backdrop may look rosy, but that does not mean the markets are easy to navigate at this stage in the cycle. The key is to remain focused on the long-term and to not be swayed by lofty returns where valuations are not supporting the price. Long-term we have found added value in rebalancing portfolios annually and maintaining all-weather diversified portfolios. We appreciate the opportunity to work with you and if you have any questions or concerns, please do not hesitate to let us know.

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Asset Index Category	YTD 3Q 2018 %	YTD 2018 %	3-Year Average %	10-Year Average %
S&P 500 Index-Large Companies	7.20	8.99	14.92	9.59
S&P 400 Index-Mid-size Companies	3.48	6.26	13.84	10.75
Russell 2000 Index-Sm Companies	3.26	10.49	15.51	9.58
Natural Resource Funds	-0.32	-1.12	13.53	3.97
Gold	-5.36	-8.72	1.78	2.81
US Real Estate Funds	0.58	1.22	7.24	7.13
Global Real Estate Funds	-0.74	-0.94	6.19	5.75
MSCI EAFE-Developed International	0.76	-3.76	6.27	2.42
MSCI EM Index-Emerging Markets	-2.02	-9.54	9.78	2.91
Barclays U.S. Aggregate Bond Index	0.02	-1.60	1.31	3.77
Long U.S. Government Bond Index	-2.04	-4.64	0.37	4.85
Emerging Market Bond Index	0.30	-6.21	5.13	4.75

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