Half Year Report to Clients, 2019

August, 2019

Market Review

What an interesting six months!

We ended December 2018, with the equity markets posting one of the worst quarterly performance in 11 years. The MSCI World Index fell 13.9.

Successive Federal Reserve rate hikes and the prospect of more in 2019, evidenced the decoupling of market implied wisdom and the Federal Reserve's determination to absorb the stimulus injected into the financial system to offset the tight money reality of the 2008 recession.

By January, however, the Chairman of the Federal Reserve had walked back the Board's more aggressive sentiment on the condition of the economy and indicated that any future rate increases would be data dependent. For some time to come interest rates would remain relatively as is. In addition, the roll off of the Federal Reserve balance sheet of purchased securities approximating $3.6 trillion of select bank assets acquired as a tool to increase liquidity would proceed only consistent with evolving market conditions.

In the first quarter of 2019 the equity markets reversed direction. Gains offset almost all of the losses experienced in Q-4 of 2018.

The Trump tariffs imposed on $250 billion of Chinese imports remained in place. However, the White House signaled that negotiations with China were ongoing and there was reasonable prospect of an acceptable agreement by the end of March, 2019.

President Trump initiated trade confrontation with the Chinese government in October 2018, in response to the imbalance in trade between the two countries and because of intellectual property theft by Chinese companies with the knowledge of and support of the Chinese government. This the Chinese government denies

Not limiting his ire of trade imbalances to just China, the President also threatened Canada, Japan, Mexico, South Korea and the European Union with various levels of tariff on select US imports, absent renegotiated trading terms with the United States.

The Federal Reserve position reversal on interest rates is understandable in the face of global trade turmoil.

Europe has never fully recovered from the 2008 Recession. U.S. and China import and export tariffs have slowed China export manufacturing. The impact of these retaliatory tariffs, because they impact Chinese manufacturing, have slowed raw material as well as finished goods imports into China. The ripple effect has reduced business economic confidence and activity globally.

US economic performance continues strong despite market convolutions. However, there is increasing concern that the global economic slowdown will impact the US economy. When and to what extent remains uncertain.

US- China tariff battles are not resolved and at the end of July President Trump upped the ante by indicating additional tariffs will be leveled on items beyond the initial 300 billion dollars of items. China has pledged to respond and has indicated they do not fear a tariff battle with the United States.

By early Q-2, 2019, the US and Europe had reached some accommodation on the matter of trade. Nevertheless, the US President has recently revisited the topic, suggesting that absent some concessions on the import of American beef the subject of tariff on European cars would be revisited.

Automobile, manufactured and farm product imports from Canada and Mexico have concerned the US President and spurred the negotiation of a new North America trade agreement to replaces the old NAFTA. Congressional approval of this new agreement, however, remains elusive.

Discussions with China in an effort to resolve the tariff dispute are ongoing though in a less robust manner that either side would like

US concerns regarding China's 2025 economic plan to dominate certain areas of world technology, in particular artificial intelligence, has complicated reaching a solution to these talks. Concessions by the Chinese government on how it manages its economy and supports state owned enterprises are not forthcoming. It is unlikely the trade talks will quickly reach agreement.

By the second quarter of 2019 the financial markets were pricing in a Federal Reserve interest rate tax cut before year end.

June job creation numbers signaled a slowing of the U.S. economy.

The decision of the European Central Bank to stimulate the Euro Zone by reducing interest rates has strengthened the U.S. dollar.

This action provided yet again an opportunity for President Trump to criticize the Federal Reserve Board and its Chairman for the 2018 end-of-year interest rate increase and no subsequent decision to reduce interest rates.

The President's threat to replace the Fed Chairman, a move that is highly questionable as to its legality, has heightened the discussion around what is the appropriate strategy for addressing a possible slowing of the US economy. Mr. Powell, the Fed Chairman, has indicated that he has no intention of stepping aside regardless of the President's threats to remove him and has committed himself to preserving the independence of the Fed from political intervention.

On July 31, the Fed lowered short term interest rates by 0.25 basis points (BPS).

Welcomed in some quarters, support for the rate reduction, however, was not universal. July employment numbers were strong after an upward revision to the June numbers.   Job creation was back to the 150,000+ plus levels and consumer spending held steady.

The Fed Chair explained lowering interest rates is an insurance measure. Much of the data used to evaluate the health of the economy are trailing indicators. By the time the data actually identifies that a recession is ongoing, the economy will have been in that recession for several months. He and his board believe the economic environment has changed significantly since 2008. His argument is that low inflation, interest rates and unemployment coupled with a slowing global economy recommends a rate cut to get ahead of a further slowing of economic activity and the preserving of the positive business cycle the United States enjoys.

Concern exists among some economists and market watchers, that lower interest rates and more easily available money may create financial bubbles that could well undermine the economic expansion the Fed hopes to preserve.

Occurring almost simultaneously with the Feds decision, the Presidents announced an additional 10% tariff on the remaining $300 billion of China imports to take effect in September. The President believes the Chinese have not followed through on representations made to purchase US farm products.

On August 4, the Chinese government retaliated by allowing its currency to devalue and suspending further imports of US agricultural products.

This latest round of U.S./ China tariffs will directly impact the American consumer. The initial tariff avoided directly targeting the American consumer, farmers and export manufacturers.

Self-imposed trade conflict remains the single most destabilizing issue to the global economy as we begin the third quarter of 2019.

Seslia News

We have used the past months to open new brokerage accounts for our clients at Charles Schwab. We are encouraged that our decision was correct in changing our business strategy. Most securities brokerage accounts, appropriate for utilizing this new Registered Investment Advisory service, have elected to remain as clients.

Believing that Index, Exchange Traded and managed funds are more prudent investment vehicles for use in meeting the investment objectives of our clients, we have transitioned client holdings away from ordinary equity shares to investment pools, whether these are open or closed portfolios or mutual funds. Information flow and trading advantage all benefit the professionals at brokerage firms and disadvantage the retail investor. We believe there is downside risk protection, price-yield benefit and growth advantage, which supports our decision to reposition client investment holdings accordingly.

We are continually assessing the cost effectiveness of certain investment return from mutual, exchange traded and index fund managed products. Based on management strategy, multi-year performance against industry benchmarks, and product cost we upgraded client holdings by selling those we believe are less attractive and acquiring stronger performers.

Finally, we focus attention on ensuring that client assets are continuously invested and minimize the cash holdings in accounts.

Market Indicators

Q-1 Indices performance (from Robert W. Baird & Co.) *:

Standard & Poor's' 500 Index-
Q1- +13.7%
Q2- +4.3%
Dow Jones-
Q1- +11.2%
Q2- +3.2%

Q-1 Bloomberg Barclays US Aggregate Bond Index*-
Q1- +2.9%
Q2- +3.08%

*The above market data is provided for illustration purposes only and has limited applicability to investment portfolios differently constructed. The indices described serve as an indication of overall market performance for both US domestic and fixed income instruments.