STOLPER ASSET MANAGEMENT
1924 S. UTICA, SUITE 805
TULSA, OK 74104-6516

www.stolperassetmanagement.com

918.745.6060
866.692.3066 Toll Free
918.745.6583 Fax

Stolper Asset Management
An Independent Registered Investment Adviser

Portfolio Comments
For the Quarter Ending December 31, 2018

In the words of the larger-than-life Greek shipping magnate of the last century, Aristotle Onassis: “We must free ourselves of the hope that the sea will ever rest. We must learn to sail in high winds.” And so, we now find ourselves navigating some decidedly tempestuous equity market conditions as we leave 2018 behind and confront a litany of unknowns for the coming year. Lurching valuations and sharp index swings are unsettling and often self-perpetuating, but we must focus on the fact that we are investing in corporations and an underlying long-term faith in economic resilience, not in the current divisive political and policy landscapes. Reframed from that perspective, an opportunistic skew is that many high quality stocks are looking distinctly conservatively priced right now.

That said, there is no sugar coating the numbers for the final quarter, which decimated any gains posted through the end of September and dragged down the whole year. The S&P 500 closed on December 31st at 2,507 representing a loss of -13.52% for the final quarter of 2018, which included a sharp overall drop in the final trading weeks, and losing -4.38% for the year. Similarly, the Dow Jones Industrial Average (DJIA) ended December at 23,327 for a return of -11.31% in the past three months and -3.48% for 2018. The record-high territories inhabited by the indices around the start of the quarter appear a surprisingly distant memory given the scant few months that have passed. The DJIA did, however, set a record of note the day after Christmas with its largest one-day point gain in history with a jump of 1,086. Such wild swings may point more to the rise of algorithm or automated trading, rather than investor herd mentality.

There is no single or simple answer to the big ‘why?’ of this relatively sudden downturn in investor confidence, rather we have been subject to a confluence of related circumstances and events, mostly centering on news and tensions surrounding both Washington and the Federal Reserve. The spike in market turbulence began at the start of October with an accelerated U.S. government bond sell-off which led to a fall in global equities dubbed “Red October”. Stocks hardest hit were those that had formed the core of the preceding run-up, notably big-name technology shares. Given their significant weights within indices, this sent global equities into correction territory, defined as a 10% drop from a recent peak. What followed has been an unpredictable roller coaster for the markets, with any sense of stability yet to be re-established. To

Stolper Asset Management is a Registered Investment Adviser that offers investment advisory services to private and institutional clients.

Stolper Asset Management is not a registered broker/dealer and is independent of Raymond James Financial Services, Inc., member FINRA / SIPC. Securities offered through Raymond James Financial Services, Inc. Investment advisory services offered through Stolper Asset Management.

provide some context, two of the tech darlings, **Apple Inc. (AAPL-Nasdaq)** and **Amazon.com, Inc. (AMZN-Nasdaq)**, both hit paradigm-breaking market capitalizations of $1 trillion in the third quarter but are now valued below $750 billion.

In December, the Federal Reserve raised interest rates for the fourth time this year, to a range of 2.25 – 2.50%, signaling its determination to press ahead with tightening as well as shrinking its balance sheet. This represents the ninth rise since March 2015. Fed Chair, Jerome Powell, spooked markets with his affirmation that the contraction of the Central Bank's bond holdings at the pace of $50 billion a month was on "automatic pilot". Such a rigid course guarantees investors will incrementally lose easy liquidity going forward. There is also the broader argument that since the Fed believed Quantitative Easing (QE) through bond buying supported the market, it cannot reasonably believe unwinding is entirely benign. Simultaneous rising rates also unavoidably lead to a certain amount of repricing in riskier assets such as equities and corporate credit, which experienced greater demand while interest rates were closer to zero.

Mr. Powell has given assurances that only two rises are on the agenda for 2019, down from a previously predicted three, but concern remains that the Fed may err toward over-tightening and tip the economy into recession. President Trump, for one, has been vocal in urging the Federal Reserve to pause in ratcheting up rates, and an unhelpful rumor circulated that Mr. Trump had considered relieving the Fed Chair of his position. The converse argument is that it is healthier in the long run to stay the policy course and weather these periodic downturns as investors adjust, rather than tread too lightly and set the stage for much more aggressive measures later.

Political tensions are also contributing to the climate of investor uncertainty. On December 22nd at midnight, a partial shutdown affecting around a quarter of the federal government, went into effect following the President's refusal to sign the bill passed by the Senate to continue funding the government at its current levels into February. A major sticking point is Mr. Trump's determination to secure $5 billion in funding in order to follow through on his campaign promise to build a wall on the Mexican border. The current Republican-controlled House had passed a measure on December 20th that included $5 billion for border security, but could not secure the 60 votes needed in the Senate (theoretically all 51 Republican votes plus 9 Democrats), hence the Senate's funding status-quo solution.

The President has vocally put the onus on the Democrats to reverse the shutdown by capitulating to his demand, but Democratic leverage is set to rise sharply on January 3rd when the Party takes control of the House following their recent November mid-term election gains. The House bill passed with the $5 billion earmarked funding will then have died. The same elections saw the Republicans widen their majority in the Senate by two, but not enough to garner 60 votes in any case. With heels dug in on both sides, the length and outcome of the showdown are impossible to call yet. Drawn out sparring, however, will only serve to decrease approval ratings for all involved.

President Trump also continues to face a stormy political environment surrounding questions regarding his personal conduct and that of his close advisors, especially in the period running up to his election. Specifically, Special Counsel Robert Mueller's ongoing 85-week investigation is creating an increasingly unnerving overhang. This, despite the facts that the ensuing report is unlikely to be made fully public and its findings won't necessarily result in immediate

Stolper Asset Management is not a registered broker/dealer and is independent of Raymond James Financial Services, Inc., member FINRA / SIPC. Securities offered through Raymond James Financial Services, Inc. Investment advisory services offered through Stolper Asset Management.

consequences. Michael Cohen, Mr. Trump's former lawyer recently pleaded guilty, and was sentenced to three years in prison, for criminal charges surrounding tax evasion as well as behavior Mr. Cohen claims he carried out in part to protect the then Presidential candidate.

Mr. Mueller's mandate from the Department of Justice was to investigate "any links and/or co-ordination" between the Trump campaign and the Russian government. Avenues explored have focused on the timing of the Trump Organization's attempts to build a tower in Moscow, former national security adviser Michael Flynn's communication with Washington's Russian ambassador, and overtures apparently made by Russian intelligence operations offering potentially damaging information on the President's Democratic adversary, Mrs. Clinton, and whether such approaches were welcomed or even involved collusion. There is also the question of whether any information provided by Mr. Trump contradicts facts uncovered by Mr. Mueller. Even if the findings were to be unequivocally incriminatory, the removal of the President by articles of impeachment would require around 20 Republican senators to break ranks with their leader. We believe the most imminent danger to the stability of our political system and economy is therefore the acrimonious climate of mistrust and bipartisanship likely to be exacerbated by split control of the House and Senate.

In related White House turmoil, President Trump fired attorney-general Jeff Sessions the day after the mid-term elections. He has been temporarily replaced by Matthew Whitaker, Mr. Sessions' chief-of-staff. Mr. Whitaker, who has repeatedly disparaged the idea of Mr. Mueller's investigation, will now be its overseer. John Kelly, the White House Chief of Staff is also leaving to be replaced by Mick Mulvaney, the White House budget director.

On top of this, on December 20th it was announced by the President that James Mattis, the Secretary of Defense is retiring, although Mr. Mattis himself publicly framed it as a resignation on principle. Mr. Trump said Deputy Defense Secretary Patrick Shanahan, a former Boeing executive, would take over on an acting basis from January 1st. The departure announcement came immediately on the back of Mr. Trump's decision to withdraw America's 2,000 troops from Syria. Such a move raises questions surrounding the U.S.'s ability and commitment to quash the rise of the Islamic State (IS) and gives freer rein to Russia's leader, Vladimir Putin, in the region. There is also a reported plan to withdraw half of America's 14,000 troops from Afghanistan. Tellingly, even the Republican leader of the Senate, Mitch McConnell commented, "It is regrettable that the President must now choose a new Secretary of Defense."

In other areas of global relations, the U.S. trade war with China is in a state of truce while attempts are made to negotiate a deal by March 1st. President Trump had resolved to narrow America's trade deficit, but in the ten months to the end of October this year it added up to $503 billion, a $52 billion increase over the same period in 2017. It is set to widen further next year. The administration's tax cuts have increased consumer spending power, and a significant portion of these dollars are being spent on imports. Manufacturers are also stockpiling foreign supplies and components, fearing trade tariffs may cause price hikes.

On the converse side of the equation, some major foreign economies are looking fragile, dampening demand for U.S. goods. China's slowdown continues, with knock-on effects throughout Asia's emerging markets. Over in Europe, antigovernment protests in France have disrupted business and economic confidence, and

Italy keeps teetering on a recession amid a budget deficit compromise with the European Union.

Brexit negotiations continue to make concerning headlines, the latest being British Prime Minister Theresa May's postponement of a December parliamentary vote on her most recent negotiated Brexit proposal. She subsequently faced, and survived, albeit not resoundingly, a vote of no confidence in her leadership. Donald Tusk, the president of the European Council, has made it clear that there are no current options for further renegotiations, which lays bare the worrisome prospect of a 'no deal' Brexit going into effect on March 29th 2019. If a formal withdrawal treaty has not been signed by this deadline, all EU rules and regulations will immediately cease to apply to the UK. There are major incentives for all involved to stave off this cliff face scenario, but time is running out.

Amid these shaky foreign economic conditions, the U.S. dollar continues to gain strength, making our exports more expensive, and imports relatively cheaper thereby mitigating the effect of tariffs. This is all against a backdrop of record-high world debt. The number is estimated by the Institute of International Finance to stand at nearly $250 trillion, or three times the volume of 20 years ago. The figure itself, which unsurprisingly ballooned during the zero-interest rate era tells us little, until we achieve greater clarity on whether the funds have been judiciously put to work, and how smooth the transition is away from zero-rates. These are unchartered financial territories.

So, unlike the season's gifts, it has not been straightforward to wrap the investment narrative of 2018 into an appealing package and place a bow on top. Especially in the final quarter, there have been too many moving, and oftentimes opposing, forces creating uncertainty. Washington has proved an instigating, rather than a placating factor in this period of volatility and the international economic backdrop has provided added jitters for investors. Behind this noise, however, corporate earnings remain fundamentally robust with consensus earnings growth for the U.S. market forecast above 20%. This, combined with share price drops, means that valuations are looking decidedly less expensive. The price / earnings ratio for the S&P 500 based on next year's projected earnings stands at 15.4x, which is below the current five-year average of 16.4x. More good news emerged in December including positive U.S. economic data, which is outpacing most of its global counterparts, and better than expected industrial production and retail sales. Oil prices haven't fared so well, entrenched in a bear market that has seen them fall over a third from October $77 / barrel four-year highs.

All in all, going into 2019, we cannot argue with Fed Chair Mr. Powell's observation that: "There is a mood of concern, or a mood of angst about growth going forward." The S&P 500 suffered its worst December since the Great Depression, and conservative valuations do not signal a market bottom, but perhaps we may cautiously say, or at least hope, that most of the negative headlines are now priced in. We go so far as to refute anyone's claims that they can time the market no matter how long their string of lucky guesses. And so we neither attempt to time the market, nor buy the entire market and instead stick to our discipline of investing in quality companies at reasonable prices, avoiding some of the over-exuberance but not being immunized from participating in the pullback. No matter what the landscape, we sincerely appreciate our role as your financial advisor on this journey and wish you and your family, health, happiness and prosperity for the coming year and beyond.

The S&P 500 is an unmanaged index of 500 widely held companies and over 80% of the U.S. equities market. The Dow Jones Industrial Average (DJIA), commonly known as "The Dow", is an index representing 30 companies maintained and reviewed by the editors of the Wall Street Journal. The information contained in this report does not purport to be a complete description of the securities, markets or developments referred to in this material. The information has been obtained from sources considered to be reliable, but we do not guarantee that the foregoing material is accurate or complete. Any opinions are those of the investment adviser representatives of Stolper Asset Management and not necessarily those of RJFS or Raymond James. Expressions of opinion are as of this date and are subject to change without notice. Investing involves risk and you can lose principal. There is no assurance any strategy will be successful. There is no guarantee that any forecasts made will come to pass. Past performance may not be indicative of future results. This information is not intended as a solicitation or an offer to buy or sell any security referred to herein. Dividends are not guaranteed and must be authorized by the company's board of directors.

Sector investments are companies engaged in business related to a specific sector. They are subject to fierce competition and their products and services may be subject to rapid obsolescence. There are additional risks associated with investing in an individual sector, including limited diversification. Inclusion of these indexes is for illustrative purposes only. Keep in mind that individuals cannot invest directly in any index, and index performance does not include transaction costs or other fees, which will affect actual investment performance. Individual investor's results will vary. Raymond James Financial Services, Inc., its affiliates, officers, directors or branch offices may in the normal course of business have a position in any securities mentioned in this report. Raymond James & Associates, has performed due diligence and provides research coverage on Amazon.com and Apple, Inc. Please consult your Raymond James financial advisor for a copy of the most recent report. Raymond James & Associates, Inc., Member New York Stock Exchange, an affiliate of Raymond James Financial Services, Inc., makes a market in AMZN and AAPL. Closing stock prices as of 12/31/18 are: AMZN ($1501.97) and AAPL ($157.74).