Macro Summary

- The Federal Reserve signaled no additional interest rate increases (down from two increases in previous projections), and only one increase next year;
- Economists expect 1.5 percent Gross Domestic Product (GDP) growth for the first quarter due to the headwinds of the government shutdown and inclement weather;
- Second quarter GDP growth should increase toward 2.5 percent, benefitting from carry over growth from the first quarter, though expectations should decline toward 2.2 percent in the second half of 2019;
- The 3.8 percent unemployment rate is 0.3 percent below levels from a year ago, while the unemployment rate has been flat for the past eleven months;
- Nominal wage rates have accelerated from year-over-year levels, with the overall wage rate up 3.2 percent, the best levels during the current economic expansion thus far;
- The personal savings rate increased significantly to 7.5 percent in January and the consumer debt service rate remains near historically low levels;
- The Personal Consumption Expenditure (PCE) Index deflator in January dropped to a 1.4 percent annual rate of increase, with the Core PCE holding steady at 1.8 percent;
- Relatively low retail gasoline and stable food prices have kept consumer inflation expectations low;
- The Conference Board Consumer Confidence Index rebounded in February, following three months of consecutive declines;
- In the first quarter HOME survey by the National Association of Realtors, 65 percent of people believed that now is a good time to buy a home, which is a slight increase over the previous quarter;
- Mortgage rates continue to drift lower and are beginning to stabilize the housing market, with increased spending on residential construction and existing home sales; and
- The price of West Texas Intermediate oil rose 5.1 percent during the first quarter, as supply remained steady in the face of improving demand.

	Q1 RETURN	YTD RETURN
Standard & Poor's 500	13.6%	13.6%
Balanced Portfolio - 60 / 40	9.0%	9.0 %
Dow Jones Industrial Average	11.8%	11.8%
MSCI EAFE	10.4%	10.4%
Barclays Aggregate Bond	2.9%	2.9%
Barclays Municipal Bond	2.9%	2.9%

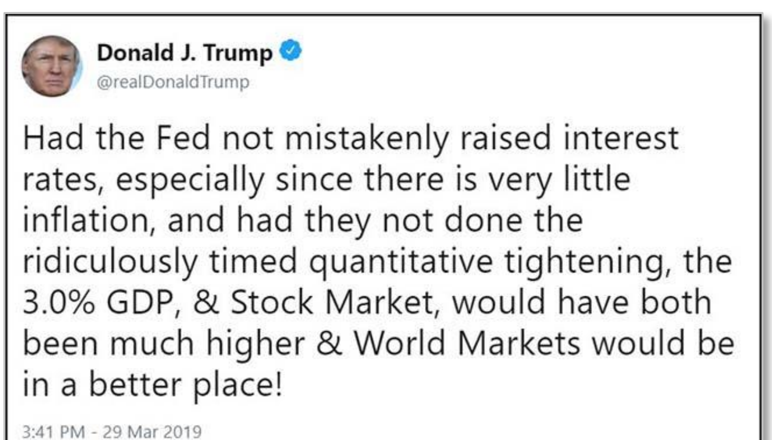
So, what caused the rebound in the financial markets? Simply put, it was the Powell Pivot.

SEPT. 2018		JAN. 2019
Fed still expects one more rate hike in 2018, three for 2019	→	Fed Signals End of Interest Rate Increases
- CNBC		*- New York Times*

Bond investors liked it. Stock investors were exuberant. The President and White House worked magically so that it appeared that the Federal Reserve Board members were not acting out of their own accord. The magnificent performance began at the end of December and after a few missteps, the show ran perfectly. First, the Federal Reserve conveyed that they would stop shrinking the balance sheet, and then that they would stop raising interest rates. Investors around the world clapped and cheered like they found Dorothy's ruby red slippers as the financial markets roared to their best first quarter in years.

What did we learn over the past three months?

- Rule #1: Don't fight the Federal Reserve
- Rule #2: The President of the United States (POTUS) wants to be re-elected
- Rule #3: Chairman Jerome Powell is influenced by the POTUS


Donald J. Trump
@realDonaldTrump

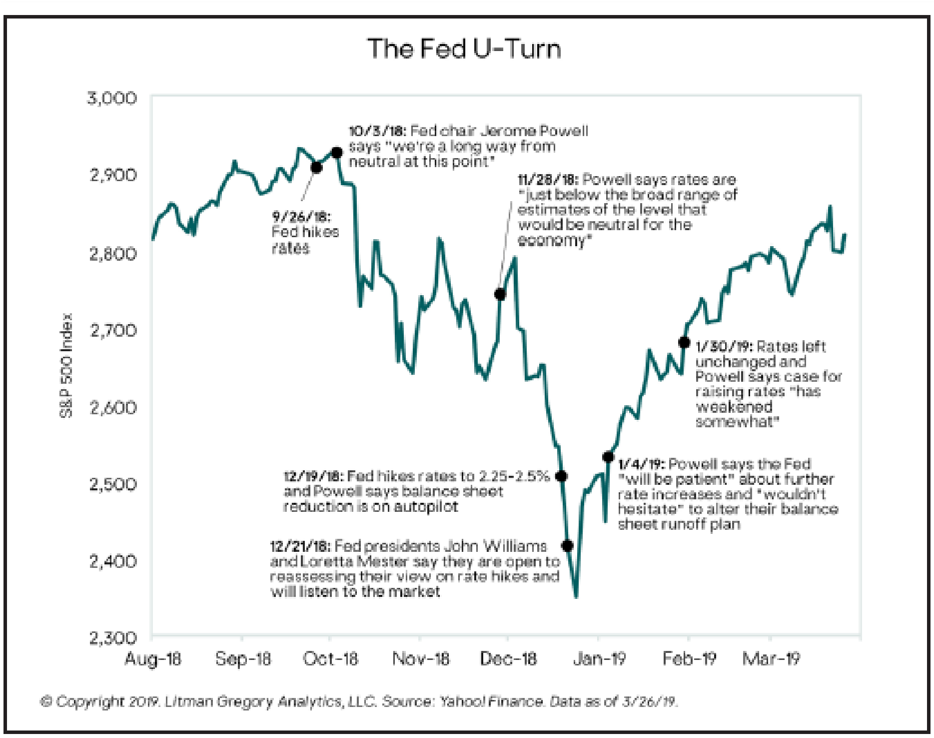
Had the Fed not mistakenly raised interest rates, especially since there is very little inflation, and had they not done the ridiculously timed quantitative tightening, the 3.0% GDP, & Stock Market, would have both been much higher & World Markets would be in a better place!

3:41 PM - 29 Mar 2019

The Federal Reserve

Since the late 1970s, the Federal Reserve has operated under a directive from Congress to promote maximum employment and price stability, commonly referred to as the Fed's 'dual mandate.' Price stability, in this sense, relates to a stated inflation-rate target of 2 percent. With inflation elusive and stock prices cratering in the final months of 2018, we wonder if perhaps they are also motivated by an unwritten third mandate to support risk assets.

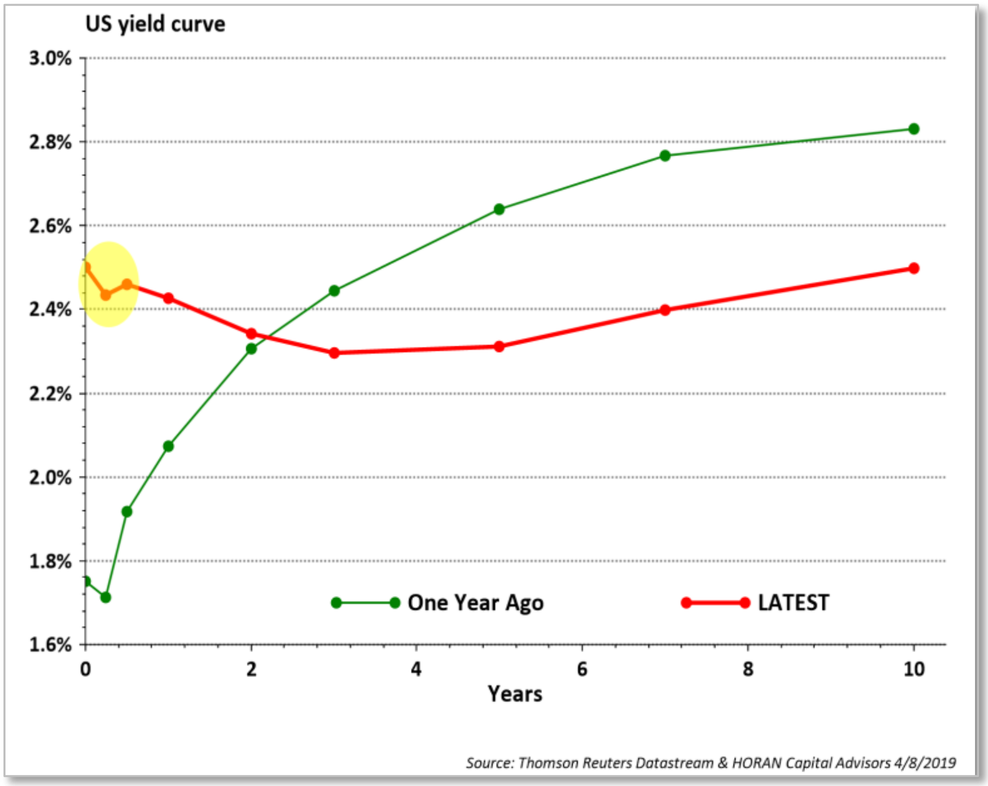
After a three-year tightening cycle and a mission to reduce the Federal Reserve's bloated balance at a run-rate of $600 billion this year, as recently as late September policymakers forecasted a handful of additional rate increases over 2019 and 2020. In early October, Chairman Powell's comment that rates were 'a long way from neutral' and, in any event, the Fed 'may go past neutral' is what set off the fourth-quarter swoon, capped by the worst December stock market performance since 1931. One sharp decline is all it took for the Fed to blink. Now, just a few months later, policymakers say that further rate hikes are unlikely – in fact the financial markets are already pricing in lower rates – and the quantitative tightening will conclude this fall, at which point the central bank will be left with a frighteningly large balance sheet in excess of $3 trillion.



In hindsight, the December 19, 2018 rate increase was probably ill advised. With nine increases already in this cycle (plus the policy-tightening equivalent of several hundred basis points of additional rate increases from balance sheet reduction), and acknowledging the lagged impact of monetary policy, the Federal Reserve may have inadvertently tightened us into a slowdown.

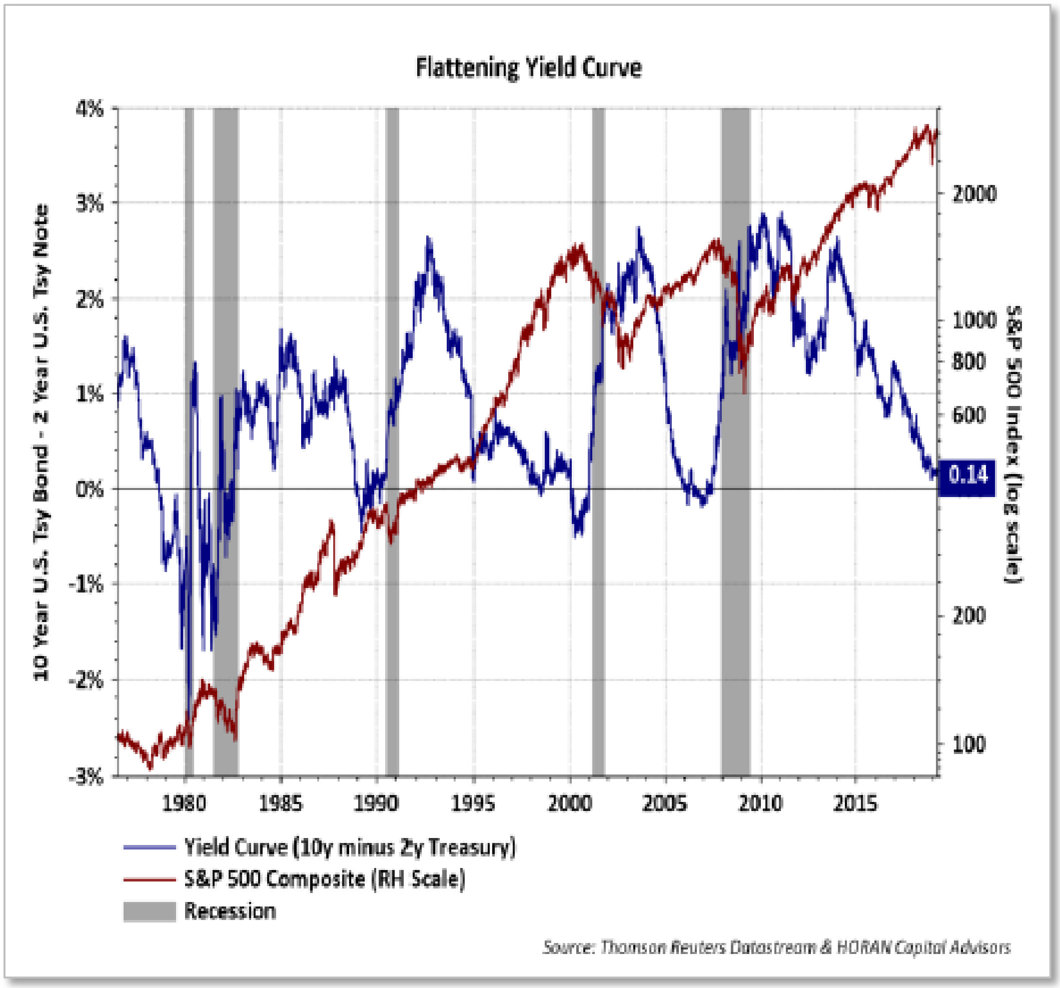
A Focus On The Yield Curve

Interest rates and the yield curve remain worthy of mention, particularly the Federal Reserve's dogmatic approach to short-term interest rate increases (as previously mentioned), raising nearly every quarter for the last two years. Chairman Powell has noted repeatedly the Committee will be 'more patient and flexible' on further rate increases.



The increase in short-term interest rates, with a commensurate decline in long-term market rates, has resulted in portions of the interest rate curve inverting. This means short-term rates are higher than long-term rates. When the spread between short-term and long-term interest rates narrow, it has historically been an indication that economic growth will fall in the future. On March 22nd the 3-month Treasury interest rate surpassed the 10-year Treasury interest rate which resulted in a 3-month/10-year inversion, the first since 2007. The 3-month/10-year inversion has subsequently unwound as I write this commentary.

At Next Generation Wealth Management, we tend to focus more on the 2-year rate versus 10-year rate and this portion of the curve has yet to invert. Our heightened focus of the yield curve inversion is the result of being a reliable indicator of forthcoming economic slumps, having preceded every recession since 1960, but two yield curve inversions have not been associated with recessions (1966 and 1968). However, the recessions were not immediate and both the financial markets and economy tended to perform well over the subsequent 12-18 months.



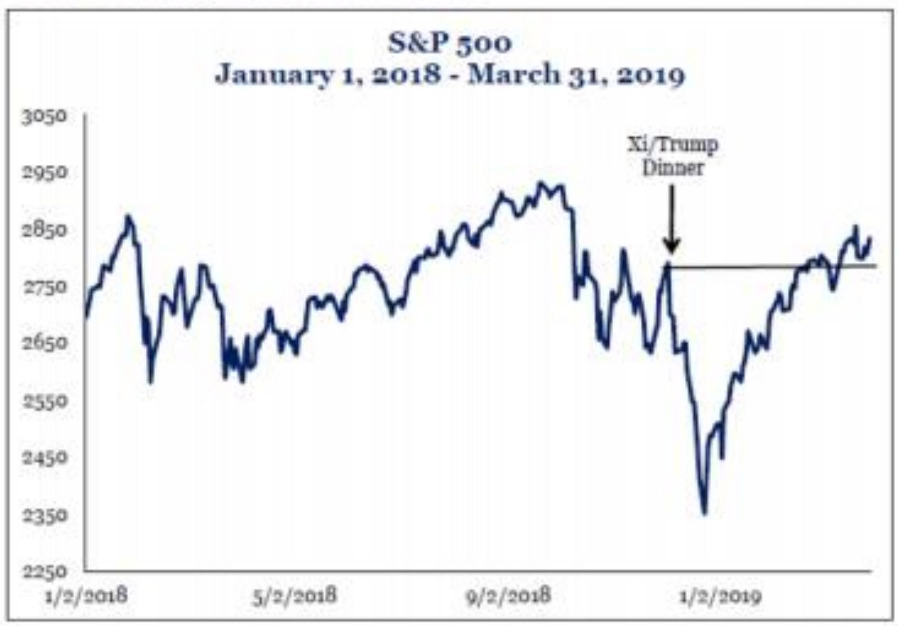
With all that said, please allow me to remind you that recessions are a normal part of the business cycle and cannot be staved off indefinitely. Forests that become choked with too much overgrowth are prone to burn, increasing the risk of uncontrollable wildfires. Small, regular fires can clean out dry shrubs and small trees and play an important role in maintaining forest health. Similarly, recessions cleanse the market's excesses, making for a safer subsequent investment environment.

While a run-of-the-mill recession cannot be ruled out, we in no way expect a catastrophic wildfire. The financial crisis a decade ago was driven by overleveraged banks; the US banking sector has recapitalized and can now withstand even large economic stress. The corporate sector, on the other hand, is awash in debt - much of it of questionable credit quality – and this is of concern and bears close monitoring. But the risk, just to be clear, is not a repeat of the last recession.

The Financial Markets

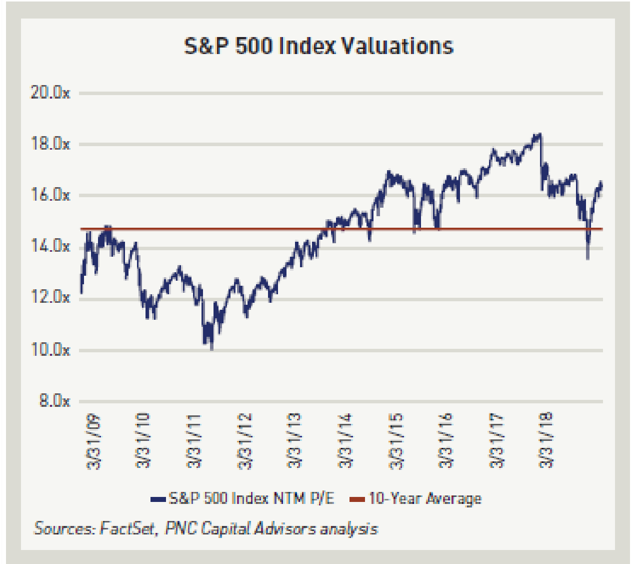
Global stocks staged a strong recovery in the first quarter after their precipitous decline during fourth quarter last year. In fact, 2018 was the worst performing year for stock markets since 2008, and December was the worst final month of the year since the Great Depression. Then sentiment abruptly turned positive as we headed into 2019, leading January to become the best start to the year in 30 years. A variety of factors, including easing trade relations between the United States and China, solid corporate earnings, and a more dovish Fed helped spur the strong rally. US equities outperformed both developed and emerging international markets.

Source: Strategas Research Partners

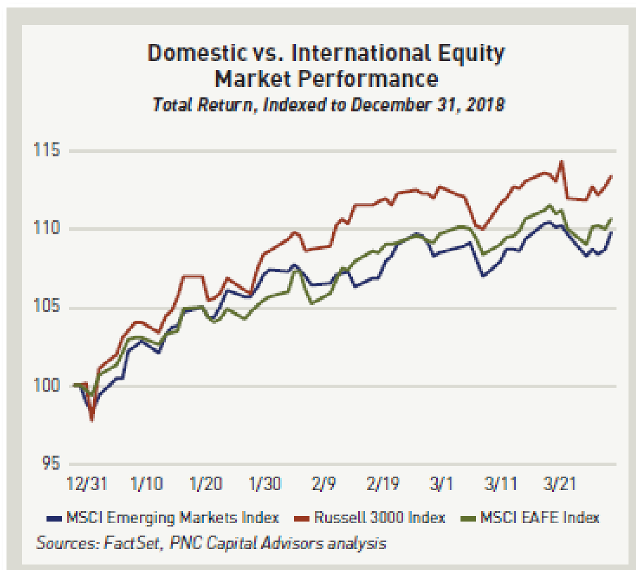


On a market capitalization basis, small companies outperformed large companies during the first quarter after their underperformance at the end of last year. All sectors within the Standard & Poor 500 Index delivered positive returns for the quarter, with some of the fourth quarter 2018 underperformers, including Information Technology, Industrials, and Energy, demonstrating the strongest performance. Energy rebounded along with crude oil prices during the quarter. Healthcare was the overall sector laggard after being the best performing sector during the second half of 2018, but still posted a 6.5 percent return. Healthcare performance was undermined by regulatory uncertainty facing managed care and underwhelming guidance from large company bio-pharmaceutical companies.

Growth stocks outperformed value stocks across both large and small market caps during first quarter, consistent with the hallmarks of a 'risk-on' environment. Additionally, while fourth quarter 2018 was marked by a shift towards higher quality companies (e.g., stocks with consistent earnings, high return on equity, strong free cash flow, and low debt), this reversed during the first quarter as investor sentiment improved. As a result of this shift in sentiment, stocks with low return on equity, high debt, and high beta generally outperformed. Valuations also rebounded off December's lows, but remained off the 10-year highs seen during 2017.



Looking overseas, emerging market equities rallied to near six-month highs on trade optimism, a rebound in global equities, a stable United States dollar, higher oil prices, and a more dovish Federal Reserve. However, towards the end of the quarter, this enthusiasm was tempered due to renewed global growth fears. While anxiety over US & China trade negotiations may have calmed, investors are now increasingly focused on the potential unraveling of global supply chains. What's happening in Germany is the perfect case in point. With other various trade-stymying developments on the horizon like Brexit or the US closing its border to Mexico, there may be some validity in these fears.



The financial markets are currently caught between incoming data pointing to slower global growth and forward-looking factors that suggest improvement later in the year. We think a modest improvement in global economic conditions is likely predicated by three important policy changes:

- The Federal Reserve: With the stress in financial markets, the slowdown in global growth, and, importantly, the US economy's participation in that slowdown in late

December, Federal Reserve Chair Jerome Powell abruptly shifted course, stressing a much more patient approach to monetary policy. Powell's thesis is that with core inflation failing to threaten the central bank's 2 percent target, the Federal Open Market Committee can be patient to wait and see how the economy evolves in the months ahead.

- President Trump: The United States aggressively pursued tariffs and other punitive measures against China over much of 2018 in an effort to extract concessions. But late in the year, with domestic financial markets and business confidence under pressure, President Donald Trump reversed course and now regularly professes confidence in his negotiators' progress toward a deal. Politics aside, this step away from brinksmanship is a positive for corporate fundamentals and markets. Our team expects a trade agreement will be announced in the second quarter of 2019, although the exact contours of that deal and the durability of any agreement remain hard to forecast with any degree of confidence.

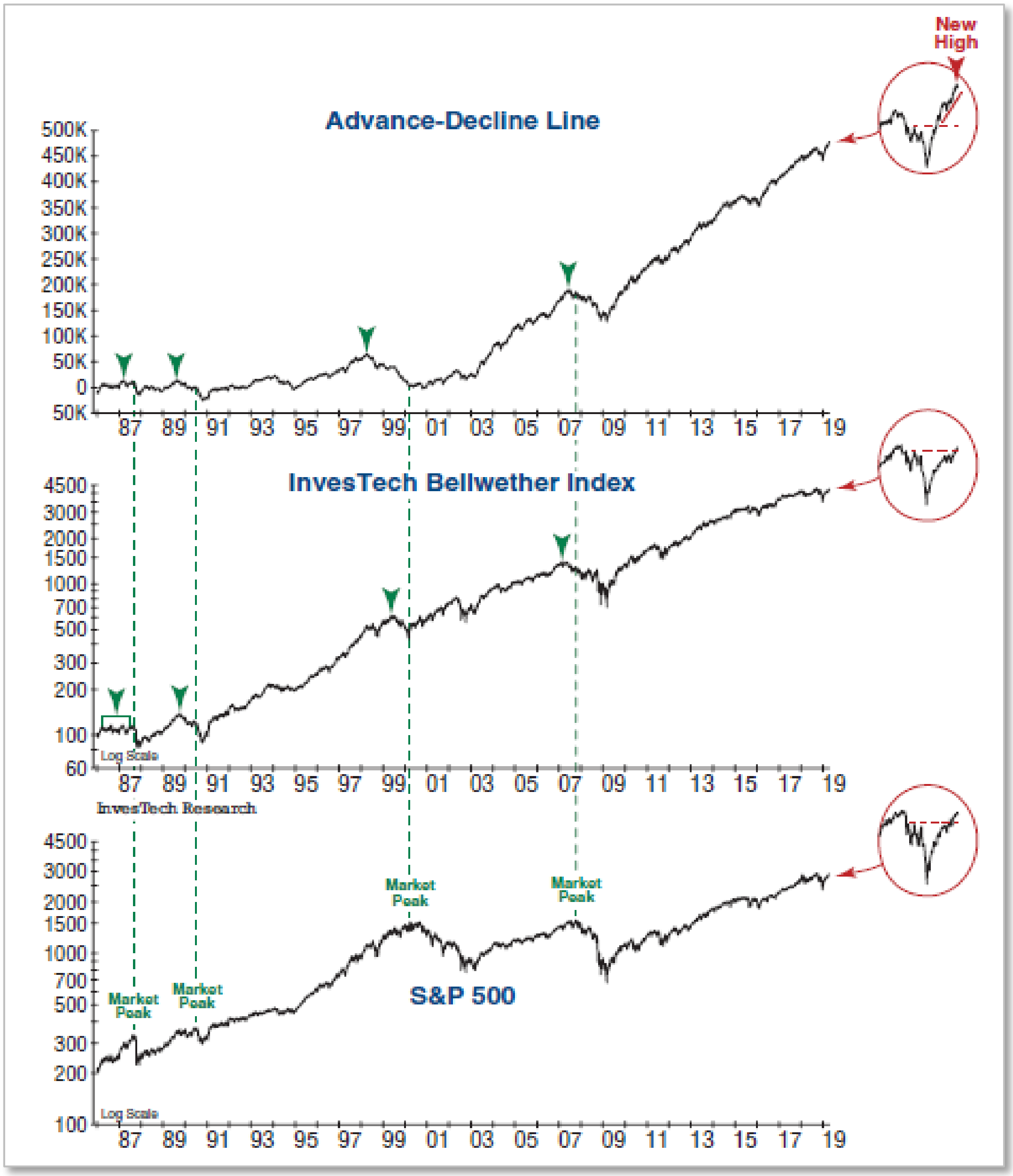
- China: Chinese stimulus is ramping up in a way that is likely to stabilize economic growth at or above 6 percent in 2019. The United States economy looks like it is responding to the Powell pivot, Trump shift, and Chinese stimulus. There is tentative evidence that lower mortgage rates are stabilizing the housing market. Meanwhile, US consumer fundamentals continue to look robust, as declining unemployment rates and moderate wage inflation buoy household income.

A Picture Is Worth A Thousand Words

In order to provide you with a shorter read, as everyone's time is valuable, on the following page are several charts from our friends at InvesTech Research. We hope you enjoy them as much as we do.

Several technical indicators displaying the strength of the financial markets have made encouraging moves since the December 2018 correction. As shown in the top graph, the Advance-Decline (A-D) Line has reversed course. The A-D Line tracks the cumulative sum of NYSE daily advancing issues minus declining issues, and gauges how broadly the market is participating in this rally.

The sharp rise of the A-D Line to new highs ahead of major indexes this year provides the single, most positive indication that this bull market is not over yet. During the past 15 months, however, the Standard & Poor 500 Index has struggled to move above previous peaks.



Another important leading indicator is the InvesTech Bellwether Index (middle graph), which contains stocks in the Financial, Consumer Discretionary, and Utilities sectors that are sensitive to rising interest rates or a slowing economy. As shown by the green arrows, this Index has peaked ahead of every market top going back to 1986.

Concluding Thoughts

We appreciate your trust and confidence in the Next Generation Wealth Management team, and are always available to discuss our thoughts further. Please contact us at (414) 257-4248 or visit our website for company news and reports at www.ngwealth.com.

Respectfully,

David

David A. Massart
President