Sound Investments Inc.

1st Quarter 2019

DJIA 25928 S&P 500 2834 Nasdaq 7729

Summary

The bull market recently celebrated its 10th birthday in March. After the decline in the markets in December, many are asking if the bull market can last much longer. Investors are concerned about rising interest rates and a slowing global economy.

We disagree since both the yield curve and the leading economic indicators show a recession is at least 1 1/2 years away.

We believe the market can reach new highs.

See attached article entitled, "Why the Bull Has Room to Run".

This investment letter is mailed quarterly to our clients and friends.

Milestones

It's been 20 years since Sound Investments Inc. was established. I started working as a stockbroker in 1982. At that time, we simply bought and sold stocks with the occasional mutual fund thrown in. The crash of 1987 is an event that I remember well.

In the late 1990's, the laws and technology changed. An advisor who held the CFP (Certified Financial Planner) designation could register with the state and become an RIA (Registered Investment Advisor). This was a better way to serve my clients and I jumped at the opportunity. At that time, my custodian was Jack Wright and I received my daily updates via fax. Later, Jack Wright was acquired b y TD Ameritrade and data was converted to the internet.

In January 1999, my paperwork was accepted by the state and I became a "fee only advisor." As a Registered Investment Advisor, I am a fiduciary and put my clients interests first rather than the broker dealers. It's been a pleasure to help people meet their life goals.

A Quick Turnaround

You may recall that the S&P 500 Index bottomed out below 2,400 on December 24th, 2018. At that point, it had fallen 20% from its high of above 2,900 on October 3rd. The stock market was officially in bear market territory and falling fast.

Since then, stocks have staged a remarkable recovery. As I write this on April 16th, the S&P has nearly recovered all of last year's fourth quarter decline by hitting 2850 for the first time since early October.

So, what is driving the recovery? The Federal Reserve changed its intentions from two interest rate increases in 2019 to a potential zero increase this year. Despite the concerns that this pivot was due to weakening growth, the overall effect of the Fed policy change was positive for both U.S. and global stocks. A low interest rate environment makes valuations more reasonable.

The third and fourth year of the President term are generally great for the stock market as can be seen below.

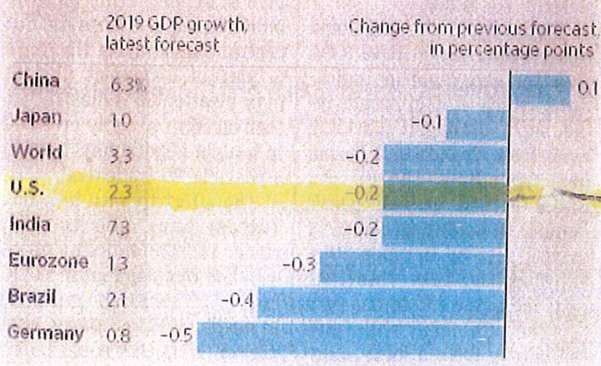
.. **The Presidential Term Anomaly**

Winner	Inaugural Year		Second Year		Third Year		Fourth Year	
Coolidge	1925	29.5%	1926	11.1%	1927	37.1%	1928	43.3%
Hoover	1929	-8.9%	1930	-25.3%	1931	-43.9%	1932	-8.9%
FDR -- 1st	1933	52.9%	1934	-2.3%	1935	47.2%	1936	32.8%
FDR -- 2nd	1937	-35.3%	1938	33.2%	1939	-0.9%	1940	-10.1%
FDR -- 3rd	1941	-11.8%	1942	21.1%	1943	25.8%	1944	19.7%
FDR / Truman	1945	36.5%	1946	-8.2%	1947	5.2%	1948	5.1%
Truman	1949	18.1%	1950	30.6%	1951	24.6%	1952	18.5%
Ike -- 1st	1953	-1.1%	1954	52.4%	1955	31.4%	1956	6.6%
Ike -- 2nd	1957	-10.9%	1958	43.3%	1959	11.9%	1960	0.5%
Kennedy / Johnson	1961	26.8%	1962	-8.8%	1963	22.7%	1964	16.4%
Johnson	1965	12.4%	1966	-10.1%	1967	23.9%	1968	11.0%
Nixon	1969	-8.5%	1970	4.0%	1971	14.3%	1972	18.9%
Nixon / Ford	1973	-14.8%	1974	-26.5%	1975	37.3%	1976	23.7%
Carter	1977	-7.4%	1978	6.4%	1979	18.4%	1980	32.3%
Reagan -- 1st	1981	-5.1%	1982	21.5%	1983	22.5%	1984	6.2%
Reagan -- 2nd	1985	31.6%	1986	18.6%	1987	5.2%	1988	16.6%
Bush	1989	31.7%	1990	-3.1%	1991	30.5%	1992	7.6%
Clinton -- 1st	1993	10.1%	1994	1.3%	1995	37.6%	1996	23.0%
Clinton -- 2nd	1997	33.4%	1998	28.6%	1999	21.0%	2000	-9.1%
Bush, G.W. -- 1st	2001	-11.9%	2002	-22.1%	2003	28.7%	2004	10.9%
Bush, G.W. -- 2nd	2005	4.9%	2006	15.8%	2007	5.5%	2008	-37.0%
Obama - 1st	2009	26.5%	2010	15.1%	2011	2.1%	2012	16.0%
Obama - 2nd	2013	32.4%	2014	13.7%	2015	1.4%	2016	12.0%
Trump	2017	21.8%	2018	-4.4%	2019		2020	
Percent Positive		58.3%		62.5%		91.3%		82.6%
All (Avg)		10.5%		8.6%		17.8%		11.1%
Positive Years (Avg)		26.3%		21.1%		21.6%		16.9%

Source: Global Financial Data and FactSet, as of 1/14/2019.[41]

Dimmer Outlook

The International Monetary Fund lowered its growth projections for several key economies and the world as a whole.



*Previous forecasts made in January
Source: IMF

In 2018 growth was over 3% but in the 5 years prior growth was 2%. Therefore 2.3% is in range.

We focus on staying invested in the part of the market that is moving and we believe that it's important to own a diversified and balanced portfolio that allows you to weather the markets ups and downs.

Continued Expansion But At A Slower Pace

The bull market recently celebrated its 10th birthday in March. After the decline in the markets in December, many are asking if the bull market can last much longer. Investors are concerned about rising interest rates and a slowing global economy. Let's look at two key indicators:

1. **Inverted Yield Curve.** This occurs when short term rates rise above long term rates and has predicted every recession over the last six decades. This did occur briefly but the historical record indicates a 9 to 18 month lead time from inversion to recession. Also, the inverted yield curve must persist for at least three months in order for it to be relevant.
2. **The Leading Economic Index – LEI.** This is a leading indicator intended to forecast future economic activity. It contains statistics such as consumer expectations, house sales, building permits, etc. The LEI suggests that the economy, in the near term, will continue to expand but may slow down by the year end. Over the past sixty years, a slowing LEI has led to a recession, which occurred within 7 to 12 months of the slow down. This is similar to the Inverted yield curve. This indicates a recession may or may not begin by 2021.

The International Monetary Fund also forecasts a slower growth rate (see chart) estimated at 2.3%, which is in line with the results from the past 8 years. In addition, we are in the third year of the presidential term which normally has a positive effect on the market.

Can The Market Reach New Highs?

I believe it can. The chart on the back of this page illustrates how the market reached new highs on Jan 26th and Aug 30th, 2018. As I write this on Apr 16th, the market is approximately 3.2% away from the all-time high which is outlined on the chart. Our optimism is substantiated as first quarter earnings have been stronger than expected and China's economic growth has held at 6.4%. Rumor has it, the trade spat with China will end soon.

It is entirely possible that equities may go up and down as the market approaches an all-time high, repeatedly, before it convincingly breaks through. Translation – stocks may waver and at times wobble and appear to move in slow motion as they near last year's highs. We believe the market can go higher and we look for confirmation in the earnings, employment and inflation fronts, which I believe will be forthcoming.

Conclusion

Essentially, we believe business expansion will continue with the GNP averaging 2% or more over the balance of 2019. Expectations that the Federal Reserve Bank could possibly lower interest rates are very motivating. We anticipate markets to be higher a year from now.


Index of 7000 Stocks.
New Resistance Line
Jan 26 2018
Aug 30th 2018
49.58
47.593
Trump Rally
Secondary Support Resistance Line
Broke Through
New Support Level
D
Approximately 4% From High
Election Day Nov. 2016
Market Timing
Oversold
Year End Dates
50.00
45.00
40.00
35.00
2.00
0.00
-2.00
-4.00
2016
Jan 2017
Apr 2017
Jul 2017
Oct 2017
Jan 2018
Apr 2018
Jul 2018
Oct 2018
Jan 2019
Apr 2019

OPINION

Why the Bull Has Room to Run

By Jason DeSena Trennert

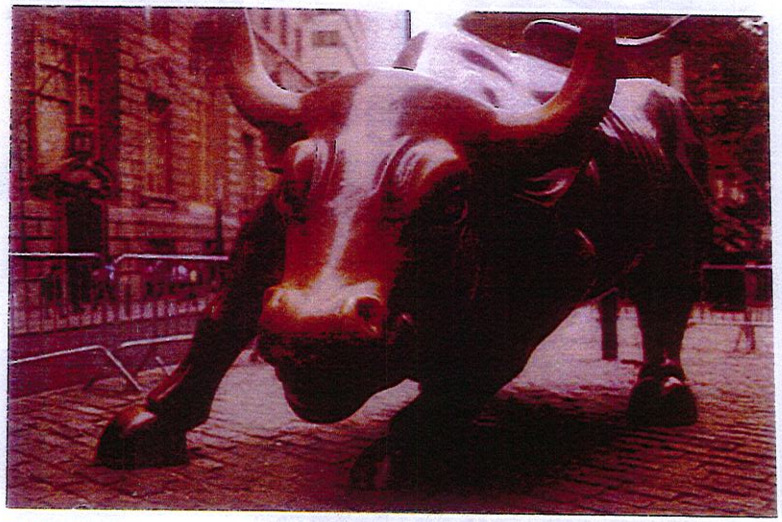
The bull market started March 9, 2009, 10 years ago Saturday. The S&P 500 had dropped to a close of 676 in the midst of the financial crisis, 2,072 points or 75% lower than its current 2,748 level. Given that the Federal Reserve has quintupled the size of its balance sheet in the intervening years, and that the heavy regulatory hand of the Obama administration gave way to a more salubrious attitude toward commerce under President Trump, perhaps the duration and the magnitude of the current bull market shouldn't surprise us.

What is surprising, for those of us who lived through the decades before the financial crisis, is how joyless the market's current ascent has been. Long gone are the marching bands and giddiness that accompanied successive highs during the dot-com era. Instead, what remains is a cynicism, likely the result of two 50% declines in the broader market from 2000-02 and 2008-09. Institutional and individual investors believe the bull market has been little more than an elaborate magic trick that will be revealed, in the end, to be ephemeral.

Euphoria kills economic expansions. The mood on the street now is best described as skepticism.

The good news for the contrarian investor is that this level of skepticism might mean that the bull market will last longer than anyone thinks possible. As legendary investor John Templeton said, "Bull markets are born on pessimism, grow on skepticism, mature on optimism, and die on euphoria."

Aside from a few brief flirtations with cryptocurrencies and cannabis stocks, it would be very difficult to describe today's investing public as especially open to risk-taking. Remarkably, fund-flow data suggest that individual investors have actually been net sellers of the market over the last decade. Since 2009, the roughly $1 trillion in inflows to domestic equity exchange-traded funds has been more than offset by the $1.3 trillion in outflows from higher-cost domestic equity mutual funds.



The Wall Street bull statue in New York.

A few years ago we at Strategas started calling the current bull move the "Jake from State Farm" market. It was an oblique reference to an amusing commercial that depicts a wife confronting a husband who's on the phone at 3 a.m. She thinks he's talking to a paramour when in fact he's speaking with Jake, a State Farm insurance agent. Even after she speaks with Jake, the suspicious wife can't accept that he's simply an insurance salesman in khaki pants: "She sounds hideous!" To which her husband replies, "Well, she's a guy, so . . ." Investors are expressing similar levels of skepticism today with regard to the current bull market and economic expansion. Despite enormous evidence to the contrary, no one quite believes that it's real or that it can last.

There is no shortage of things to worry about. But the biggest threats to the American economy are starting to fade, little by little. The current policy mix appears broadly supportive of further economic prosperity and market gains. The most important development has been the Fed's reassurances this year that monetary policy won't be left on "autopilot" as the central bank exits quantitative easing and excessively low interest rates. With the real federal-funds rate at a mere 0.5%, it is difficult to describe monetary policy as especially tight. (Of the eight recessions since 1960, none has started with a real fed-funds rate of less than roughly 2%.)

Regulatory policy, especially toward finance and energy, has eased dramatically during the Trump administration. The 2017 Tax Cuts and Jobs Act created real incentives for companies to curtail financial engineering in favor of capital expenditures, the mother's milk of productivity and wealth creation. Perhaps the biggest potential policy hurdle has been the uncertainty surrounding trade. But here, too, it seems the worst has been avoided.

The Trump administration seemed willing to fight simultaneous trade wars with every nation on Earth last summer. But it has since negotiated deals with Mexico, Canada and South Korea. An agreement with China seems imminent, though what it will contain is anyone's guess. It seems clear that at the very least, both sides want a deal that calms the fears of businessmen on both sides of the Pacific.

With the S&P 500 off to its best start since 1991, it is reasonable to expect a pause in the upward trajectory of stocks. But with the market trading at 16.5 times 2019 earnings expectations and 10-year Treasury notes yielding 2.6%, the actual risk-reward profile of the market is favorable.

The biggest risk to the long-term health of the economy and the market today is the desire of policy makers from both parties to allocate capital. This process is always best left to the collective wisdom of markets. Mercifully, such excessive meddling seems unlikely until at least 2020, or perhaps 2024.

Mr. Trennert is chairman of Strategas, an investment-strategy, economic and policy research firm.