BMT
BRYN MAWR TRUST

Market Summary - January 2, 2019

for the week ending December 31, 2018

This summary is provided by BMT Wealth Management.

A Wild Finish Caps Off A Wild Quarter

The slogan, "if you don't like the weather, just wait a few minutes," is often attributed to Mark Twain but can easily be applied to market behavior recently.

The last five trading days of 2018 encapsulates an entire range of prices, and perhaps emotions, as outlined in the oft-quoted and still popular benchmark Dow Jones Industrial Average (DJIA).

On trade-shortened Christmas Eve (Monday, Dec. 24), stock prices fell precipitously with the DJIA declining 653 points. Christmas Day provided a respite for weary investors, before Santa delivered a record 1,086-point gain to the beaten down benchmark on Wednesday (Dec. 26).

The following day (Thursday, Dec. 27), produced a most telling story, as the Index descended over 600 points late into the afternoon before turning around to the upside and closing the day ahead by 260 points.

On Friday (Dec. 28), the Index experienced an uncharacteristically narrow, but welcomed, trading day, losing just 76 points before the bell tolled.

The fifth trading day (Monday, Dec. 31) in this set of five days proved to be a positive one, as the DJIA climbed 265 points.

For the calendar year 2018, the broad-based S&P 500 Index produced a negative total return of -4.39%, the Index's first negative return since 2008. The DJIA dropped a lesser -3.48%, with the NASDAQ Composite declining -2.81%. Small cap stocks fared much worse, as the Russell 2000 plummeted -11.03% for the year.

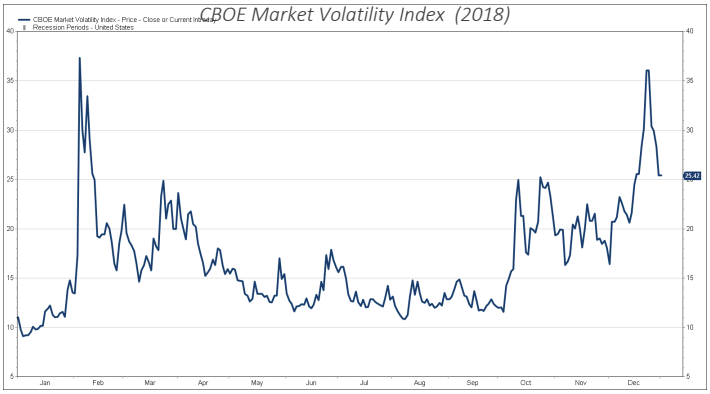
What is Driving the Extreme Market Volatility?

The word "volatility" can take on a variety of meanings to a host of different people. It is more useful to apply some empirical measure.

A well-accepted index or measure of volatility is the VIX, also known as the CBOE Market Volatility Index. In a nutshell, it is designed to measure the expected volatility of the S&P 500 and is often referred to as the market's fear gauge.

The graph below illustrates the price behavior of the VIX during 2018. As noted, the VIX spiked in early February 2018, as the S&P 500 declined 10% in a short two-week period.

The VIX spiked again in early October 2018, as the S&P 500 lost ground beginning early in the month. The VIX remained rangebound in November 2018, along with the market, before rocketing skyward amid the market sell-off in December.



Source: FactSet, Inc.

If the above information is the "what" part of the question, the more useful exercise is the "why."

There are numerous fundamental issues affecting market behavior, including:

- The administration of monetary policy and whether the Fed has made an error
- Corporate profit growth in 2019 and beyond
- Concerns on slowing global growth
- Trade war issues and China
- Energy prices and whether the decline is supply-induced or also a function of slowing demand

Counter to these more intrinsic and fundamental factors is the view that trading volume, and thus extreme swings in volatility, are being driven by changes in market dynamics over the last decade or so.

In a recent study conducted by J.P. Morgan, it was determined that 85% of trading volume came from non-fundamental sources, that is, entities without a view as to the intrinsic value of a company's prospects. The study cites these sources to include quantitative hedge funds (computer models), index investors, passive funds, and high frequency-traders, to name a few.

Why This is Not 2008

Our analysis suggests that a recession is not visible, at least yet. We have compiled a list of recession indicators and, while some have flipped into the neutral, if not negative column, most still support economic expansion into the middle part of 2019 and beyond. Clearly, given the latter stages of this economic cycle and the possibility of a policy error by the central bank, these indicators could take on a different complexion in the coming months.

There are several different indicators that do not line up with 2008 but one area that we would highlight are credit conditions and leverage. Loan demand and loan quality, as reported from the banking sector, have been steady and well-placed.

One of the key areas that we track is credit spreads or the yield difference between U.S. government and/or high-grade corporate debt and high yield (lower quality) corporate debt. Spreads have widened recently but not to the extent that approaches longer term data.

As always, we will continue to diligently monitor the market dynamics, along with our indicators, and communicate any changes in our thinking.

In Summary

Market corrections are never pleasant and often seem longer than our memories immediately recall. We continue to recommend that investors not make any significant changes to portfolio allocations based on short-term market gyrations.

BMT in the Press

Nine Sectors That Investors Should Watch in 2019 (12/27/2018)

U.S. News & World Report called upon Ernie Cecilia, Chief Investment Officer at Bryn Mawr Trust, to highlight potential areas of opportunity for investors to consider in 2019. Ernie discussed what he will be keeping a close eye on in the New Year from sectors like technology, consumer discretionary, energy, telecommunications, and aerospace.

Read the entire article at usnews.com.

U.S. Stock Futures Gain After Mnuchin Reiterates Fed Autonomy (12/23/2018)

Ernie Cecilia, Chief Investment Officer at Bryn Mawr Trust, spoke with Bloomberg about BMT's outlook on the markets after Treasury Secretary Steven Mnuchin dismissed rumors that Federal Reserve Chairman Jerome Powell would be removed from his position. While this news boosted U.S. futures in the short-term, Ernie explained that the markets are indicating a high possibility of a Fed policy error.

Read the entire article at bloomberg.com.

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