Q1 2019 LOOK AHEAD

Disclaimer

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Wall Street Parlor Tricks

Market Comparison: 2018 Predictions to Present	S&P 500	S&P 500 Price Return (%)	U.S. GDP Growth	10-Year Treasury Yield
Avg. Est. (January 2018)	2769	3.58%	2.20%	2.68%
Actual*	2507	-6.23%	3.40%	2.69%

*Actual data as of market close on December 31, 2018. GDP data as of the third estimate for Q3 2018 ending 9/30/18. Data sourced from Bloomberg, L.P.

2019 Predictions

Wall Street's 2019 Market Predictions

Firm	Predicted S&P 500 Target	Predicted S&P 500 Price Return (%)*
Bank of America	2900	15.68%
Barclays	3000	19.66%
Citi	3100	23.65%
Credit Suisse	3350	33.63%
Deutsche Bank	3250	29.64%
Goldman Sachs	3000	19.66%
HSBC	3150	25.65%
Morgan Stanley	2750	9.69%
RBC	2900	15.68%
Stifel Nicolaus	2800	11.69%
UBS	3200	27.64%
Wells Fargo	3079	22.82%
Average	**3040**	**21.26%**

*Based on the closing price on December 31, 2018

- Last year's predictions overestimated market returns by 9.81%
- GDP growth exceeded analyst estimates by 1.20%, due in part by tax reform
- Analysts forecast the best stock market returns for 2019 since 2013

2019 Projected GDP Growth

	United States	China	Japan	Euro Area	Global
U.S. Federal Reserve	2.40%	-	-	-	-
IMF	2.50%	6.20%	0.90%	2.00%	3.70%
World Bank	2.50%	6.30%	0.80%	1.70%	3.00%
Average	**2.47%**	**6.25%**	**0.85%**	**1.85%**	**3.35%**

Data Source: Bloomberg, https://www.zerohedge.com/news/2018-12-02/wall-street-forecasts-2019-are-most-optimistic-financial-crisis, https://www.stlouisfed.org/publications/regional-economist/fourth-quarter-2018/forecasters-gdp-growth-2019, https://www.imf.org/external/datamapper/NGDP_RPCH@WEO/OEMDC/ADVEC/WEOWORLD/USA/CHN/EUQ, http://www.worldbank.org/en/publication/global-economic-prospects. No representation or warranties either expressed or implied are made as to the accuracy of the information presented.

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Bracing For The Bear

- Here's what to expect if the markets reach a 20% decline:
  - The average bear market sees a total drop of 31.8%
  - Historically, bear markets last a fifth as long as bull markets
  - Once the 20% threshold is hit, the S&P 500's performance for the following year has been positive nearly 77% of the time
- Keep in mind, this next bear market may not be as bad as we think; this would be due to significantly less risk within the financial system than in 2007

Post-WW2 S&P 500 Bear Markets*

									S&P 500 % Change Once -20% Threshold is Hit				
Cycle	Start	-20%	Days to Bear	End	Days from -20% to End	% Chg from -20% to End	Full Bear % Chg	Full Bear # of Days	Next Week	Next Month	Next 3 Mths	Next 6 Mths	Next Year
Bear	5/29/46	9/3/46	97	5/19/47	258	-8.20	-28.47	355	-2.73	0.00	-2.40	4.33	2.20
Bear	6/15/48	6/13/49	363	6/13/49	0	0.00	-20.57	363	3.84	9.08	16.16	23.03	39.70
Bear	8/2/56	10/21/57	445	10/22/57	1	-0.43	-21.63	446	3.24	1.97	5.64	9.32	30.11
Bear	12/12/61	5/28/62	167	6/26/62	29	-5.73	-27.97	196	3.73	-5.23	5.93	11.23	25.89
Bear	2/9/66	8/29/66	201	10/7/66	39	-1.78	-22.18	240	3.26	3.46	7.94	17.64	24.30
Bear	11/29/68	1/29/70	426	5/26/70	117	-19.14	-36.06	543	0.25	4.69	-4.96	-8.93	11.55
Bear	1/11/73	11/27/73	320	10/3/74	310	-34.92	-48.20	630	-2.20	2.13	0.54	-9.21	-28.08
Bear	11/28/80	2/22/82	451	8/12/82	171	-8.22	-27.11	622	1.54	1.76	2.87	1.28	32.12
Bear	8/25/87	10/19/87	55	12/4/87	46	-0.41	-33.51	101	1.26	8.09	7.91	14.71	22.53
Bear	3/24/00	3/12/01	353	9/21/01	193	-18.16	-36.77	546	-0.79	-1.00	6.41	-7.42	-1.19
Bear	1/4/02	7/10/02	187	7/23/02	13	-13.34	-31.97	200	-1.57	-1.63	-15.61	-1.15	8.88
Bear	10/9/07	7/9/08	274	11/20/08	134	-39.55	-51.93	408	0.05	1.72	-20.87	-27.16	-29.34
Bear	1/6/09	2/23/09	48	3/9/09	14	-8.99	-27.62	62	-5.72	8.45	22.47	38.05	49.06
Bear?	9/20/18	?	?	?			?	?	?	?	?	?	?
		Average	261		102	-12.22	-31.85	362	0.32	2.58	2.46	5.06	14.44
		Median	274		46	-8.22	-28.47	363	0.25	1.97	5.64	4.33	22.53
		% Positive	--		--	--	--	--	61.5%	69.2%	69.2%	61.5%	76.9%
		Avg. All Periods							0.16	0.66	2.05	4.20	8.67

*Bear Market definition of 20%+ decline that was preceded by a 20%+ rally, all on a closing basis.

Decreased risk in the financial system

Bank risk-weighted-capital ratio	2007	2017
US	8.5%	13.9%
Europe	8.0%	16.0%
Bank liquid assets as % of short term liabilities	**2007**	**2017**
US	41%	48%
Europe	35%	40%
Bank loan-to-deposit ratio	**2007**	**2017**
US	97%	76%
Europe	139%	105%

Source: Fed, FDIC, ECB, JPMAM. 2018.

Type of decline	Average frequency[1]	Average length[2]
-5% or more	About 3 times a year	47 days
-10% or more	About once a year	115 days
-15% or more	About once every 2 years	216 days
-20% or more	About once every 3 ½ years	338 days

Data Source: Phillips & Co., Bespoke (Premium), http://phillipsandco.com/files/1215/4646/9959/Eye_on_the_Market_12-26.pdf. http://phillipsandco.com/blog/inflection-point1/. No representation or warranties either expressed or implied are made as to the accuracy of the information presented.

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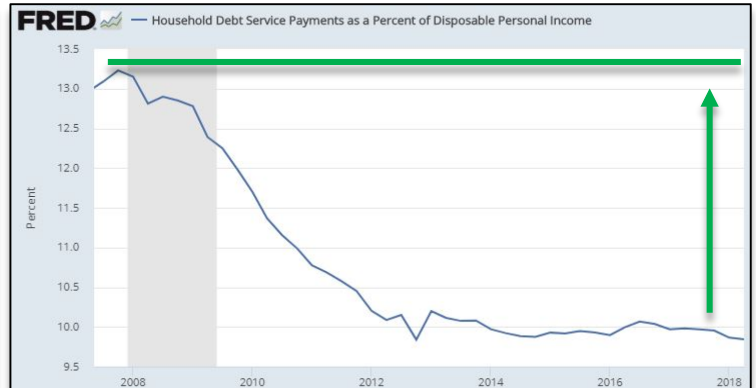
U.S. Consumer Strength

Wage Growth: 3.1%



Household Debt Service Payments as a % of Disposable Personal Income

Consumer Sentiment

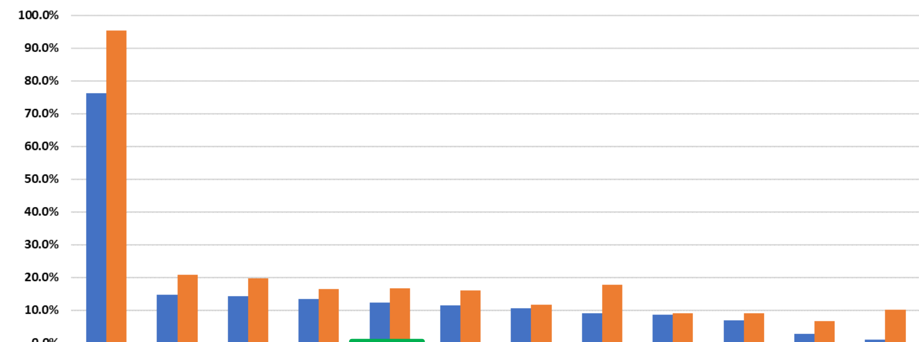
Personal Savings Rate

- ❑ Wage growth increased above 3 percent for the first time in over a decade, further supporting the consumers' appetite to spend
- ❑ A return to peak levels of debt service payments as a percent of disposable income could add \$5 – \$6 trillion in consumption over the next 10 years
- ❑ After the government change in calculating the Personal Savings Rate, the Personal Savings Rate shows limited declines over the past five years, further suggesting that the U.S. consumer has ample room to increase spending; prior to the change in calculation, the Personal Savings Rate matched the lows recorded prior to the Great Financial Crisis
- ❑ Consumer Sentiment remains at elevated levels, despite a slight downtick year-over-year, which suggests that the consumer remains confident and likely to continue their appetite for spending

Data Source: Economic Research Federal Reserve Bank of St. Louis: https://fred.stlouisfed.org/series/CES0500000003, https://fred.stlouisfed.org/series/TDSP, https://fred.stlouisfed.org/series/UMCSENT, https://fred.stlouisfed.org/series/PSAVERT, Phillips & Co. http://phillipsandco.com/blog/questions-for-2018/

Corporate Earnings

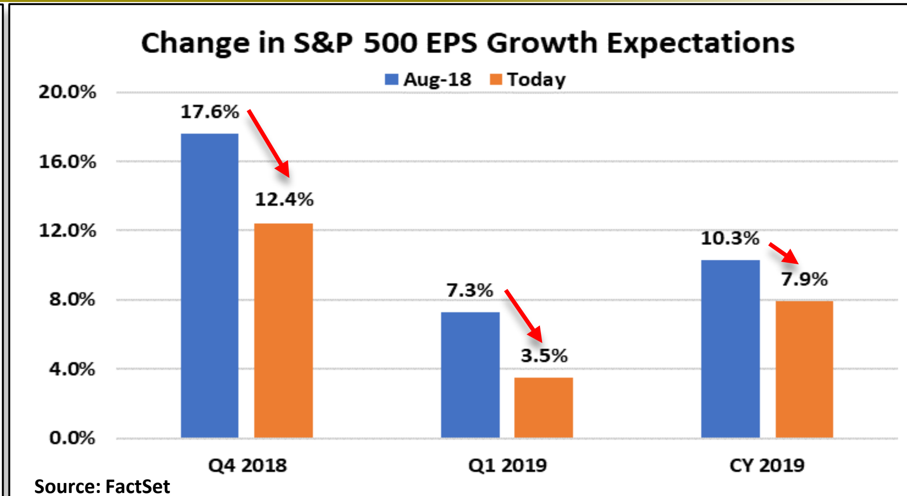
S&P 500 Earnings Growth: Q4 2018



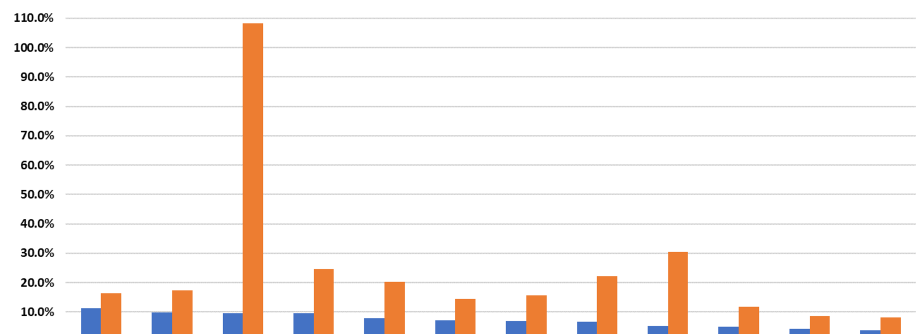
	Energy	Industrials	Financials	Comm. Services	S&P 500	Consumer Disc.	Health Care	Materials	Real Estate	Info. Technology	Consumer Staples	Utilities
Today	76.3%	14.6%	14.2%	13.3%	12.4%	11.5%	10.5%	9.1%	8.7%	6.9%	2.7%	1.1%
30-Sep	95.4%	20.7%	19.8%	16.4%	16.6%	16.1%	11.7%	17.7%	9.1%	9.1%	6.7%	10.2%

Source: FactSet

Today 30-Sep



S&P 500 Earnings Growth Projections: 2019 vs. 2018



	Industrials	Consumer Disc.	Energy	Financials	S&P 500	Health Care	Info. Technology	Comm. Services	Materials	Utilities	Consumer Staples	Real Estate
2019	11.4%	9.8%	9.7%	9.5%	7.9%	7.3%	7.0%	6.6%	5.2%	4.9%	4.3%	3.9%
2018	16.5%	17.3%	108.3%	24.6%	20.3%	14.5%	15.7%	22.2%	30.5%	11.9%	8.6%	8.2%

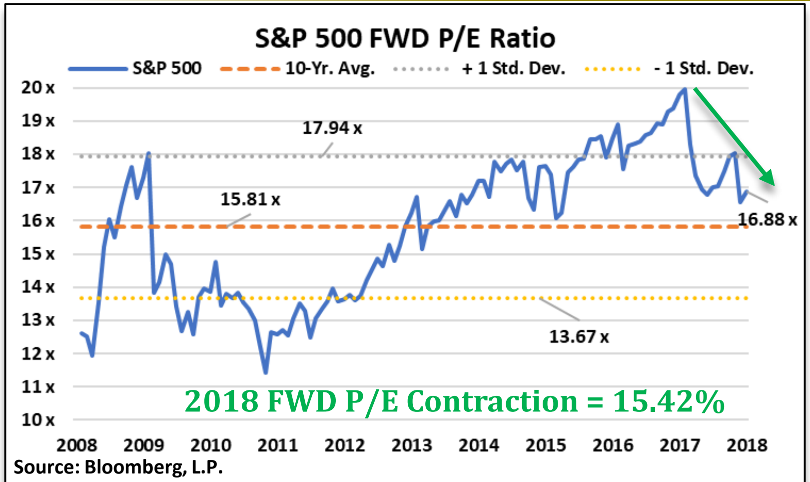
Source: FactSet

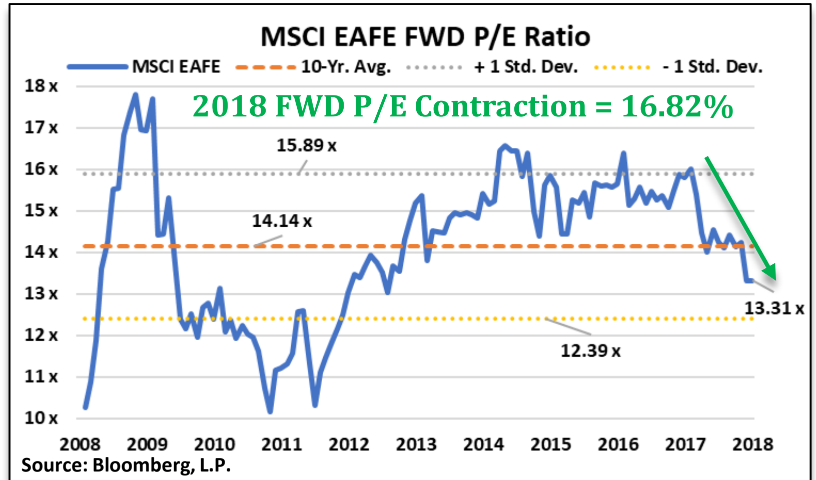
2019 2018

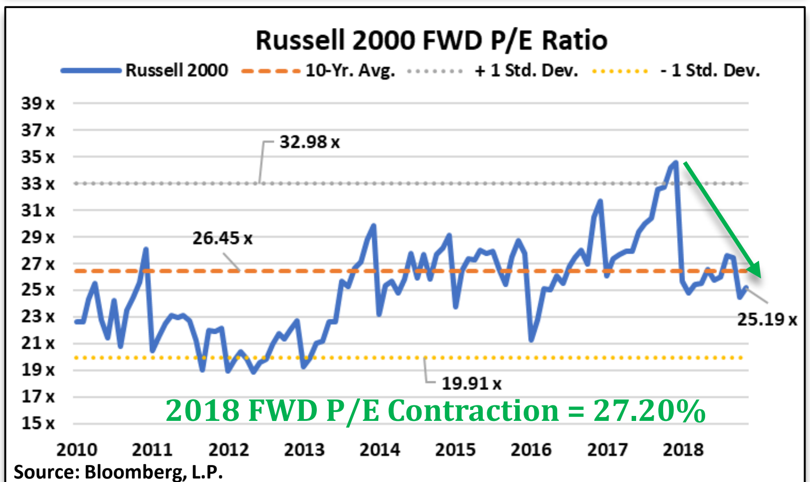
- ❑ Earnings growth should start to slow in 2019, as the effects of the 2018 tax cuts begin to wear off
- ❑ Full-year 2018 earnings growth projections are still expected to be higher than 20 percent; however, projections for earnings growth in 2019 are significantly less
- ❑ Over the last five months, analysts have drastically downgraded their earnings growth projections, potentially opening up a window for companies to outperform analyst expectations

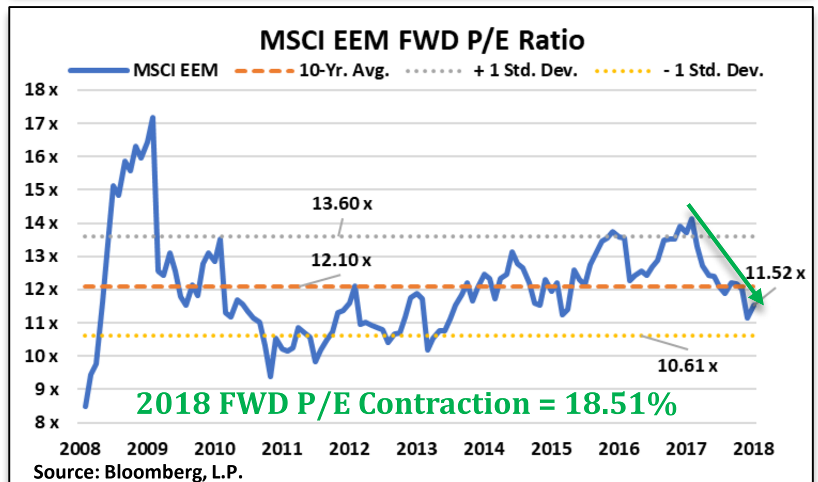
Data Source: Phillips & Co., https://www.factset.com/hubfs/Resources%20Section/Research%20Desk/Earnings%20Insight/EarningsInsight_122118.pdf, https://www.factset.com/hubfs/Resources%20Section/Research%20Desk/Earnings%20Insight/EarningsInsight_081018.pdf. No representation or warranties either expressed or implied are made as to the accuracy of the information presented.

Valuations





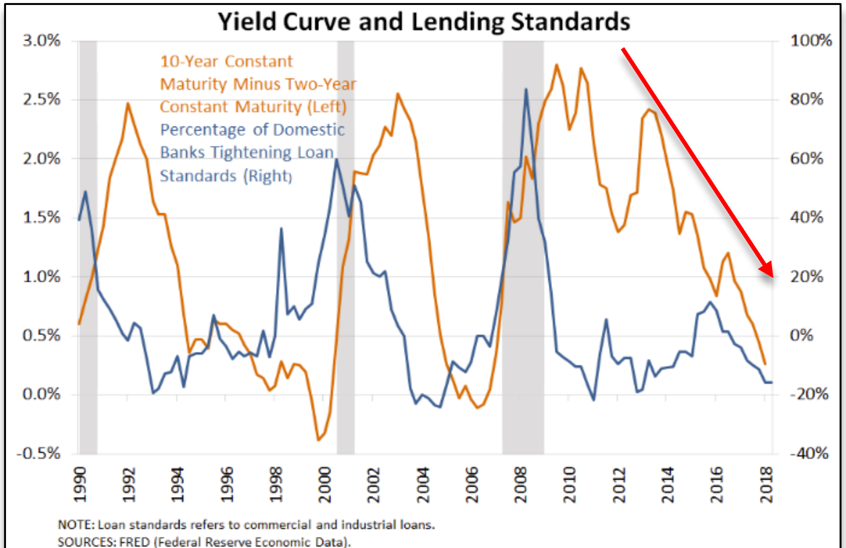


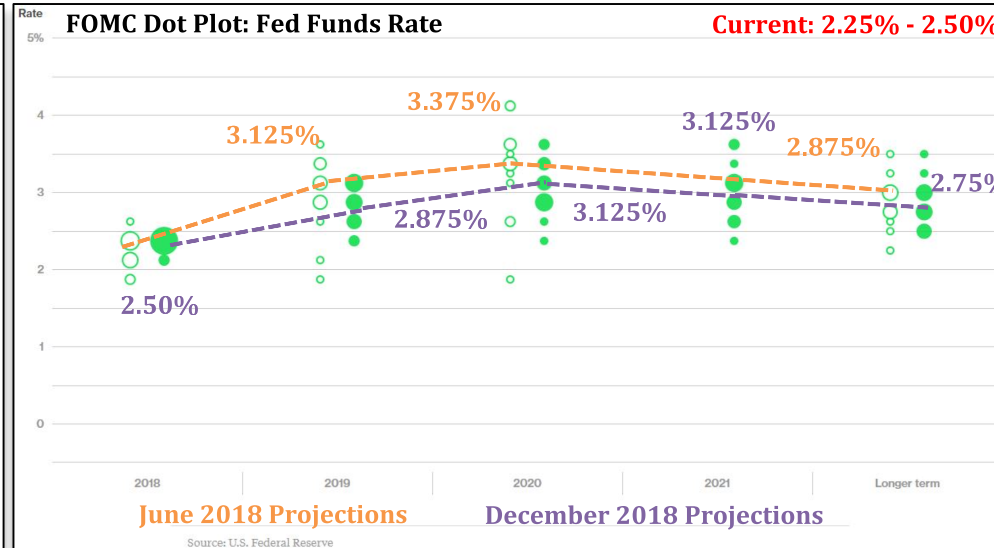


- Valuations at these levels are likely to bring buyers back into the Equity markets
- Depending on which market you're looking at, Forward P/E ratios have contracted between 15% - 30%

Data Source: Bloomberg, Phillips & Co. Data is from sources deemed to be reliable. No representation or warranties either expressed or implied are made as to the accuracy of the information presented.

U.S. Interest Rates





Flattening Yield Curves & Equity Market Returns

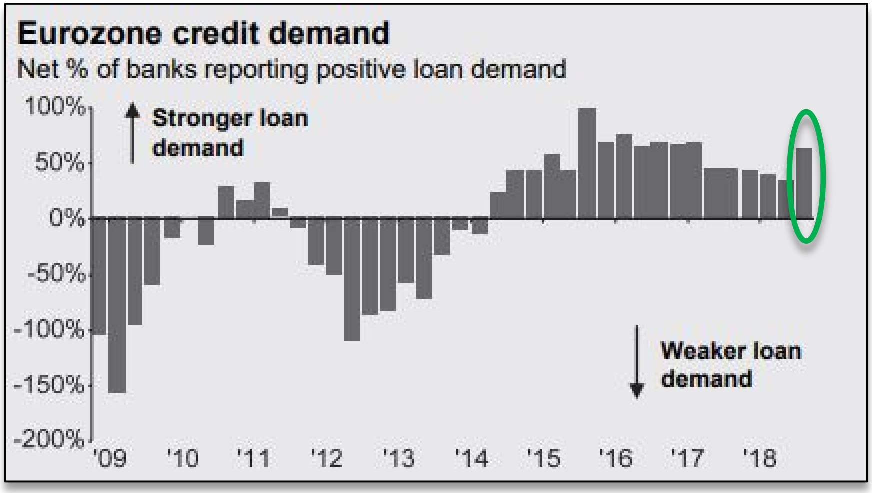
Curve	Current Level (%)	Current Percentile	Previous Instances	S&P 500 1 Month	S&P 500 3 Month	S&P 500 1 Year
3m10s*	0.543	0.157	84	2.34	4.51	15.10
2s10s*	0.122	0.120	73	1.94	5.18	16.18
2s30s*	0.384	0.149	114	0.36	3.59	17.01
5s30s**	0.396	0.217	68	1.61	6.64	23.49

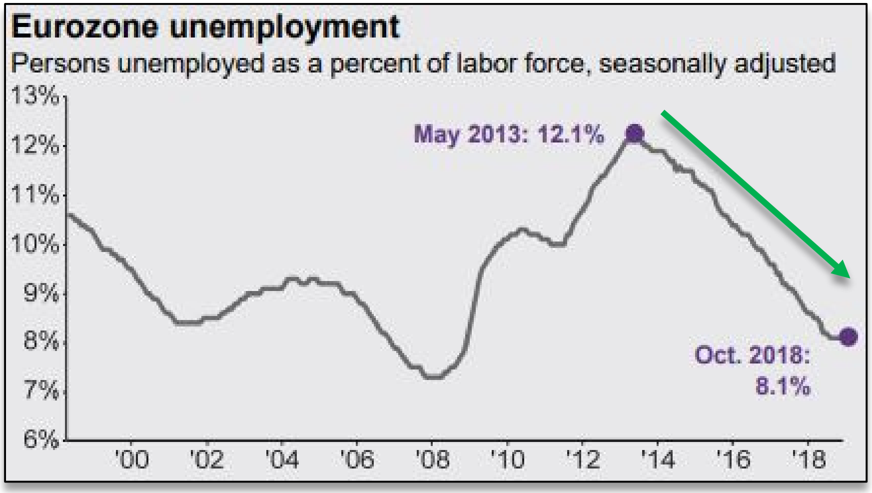
When curve has* ***flattened* *over past 3 months.*

When curve has* ***steepened *over past 3 months.*

- As the yield curve continues to flatten (**Yield Curve and Lending Standards** – Top Left), the inversion of 2-Year and 10-Year Treasury yields typically leads to a the tightening of bank lending standards, which more often than not is the root cause of a forthcoming recession
- The U.S. Fed Funds Rate (**FOMC Dot Plot: Fed Funds Rate** – Top Right) finished 2018 at 2.50 percent; however, the Fed's rhetoric has begun to transition from hawkish to dovish suggesting expectations for slower growth and fewer interest rate increases throughout 2019 and 2020
- While interest rates are often leading indicators of future economic stress, a flattening yield curve, on average, has led to double-digit forward 1-Year returns for the S&P 500 (**Flattening Yield Curves & Equity Market Returns** – Bottom Left)

International Developed Markets





- Loan demand throughout the Eurozone has been at its highest in the last 5 quarters, suggesting businesses and consumers continue to have an appetite for growth
- Unemployment throughout the Eurozone continues to trend toward historic lows, further supporting the appetite for individuals and businesses to allocate greater amounts of capital towards growth and consumption
- Labor markets, specifically in Japan, appear to be accommodative towards growing corporate profits; this is evidenced by a consistent decline in the unemployment rate matched by benign wage / declining wage growth

Data Source: Phillips & Co. http://phillipsandco.com/files/4415/4507/1326/MI-GTM_4Q18_December.pdf. Data is from sources deemed to be reliable. No representation or warranties either expressed or implied are made as to the accuracy of the information presented.

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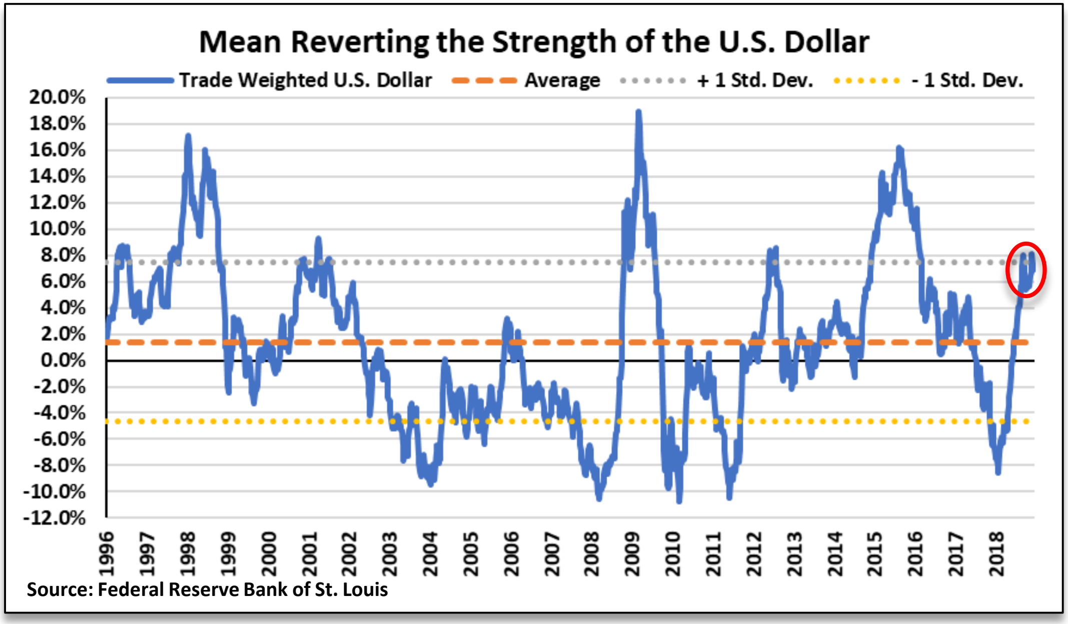
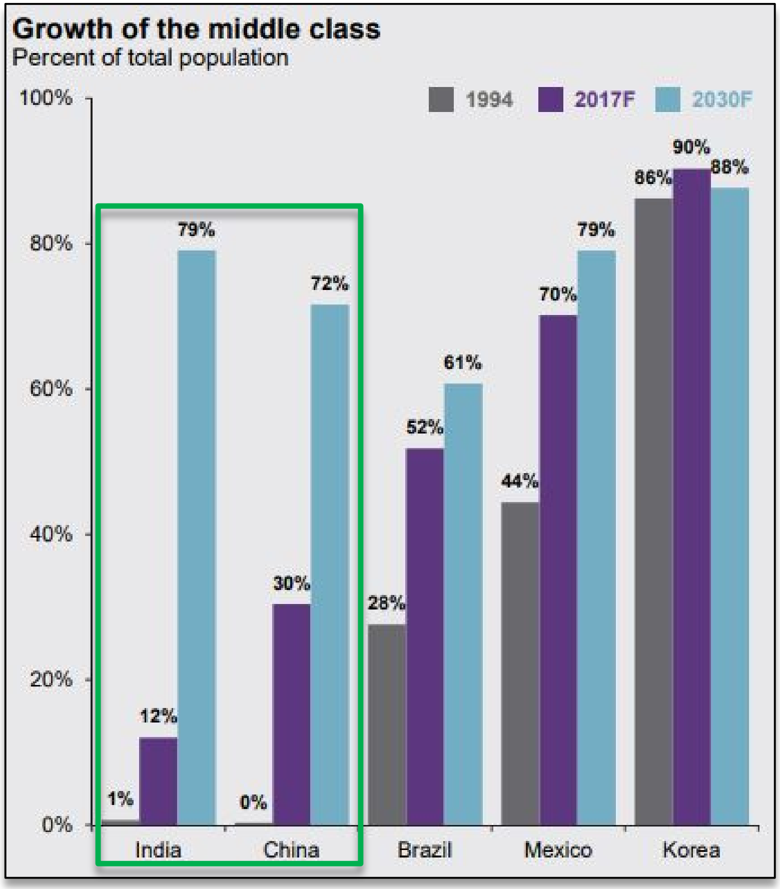
Emerging Markets (EM)





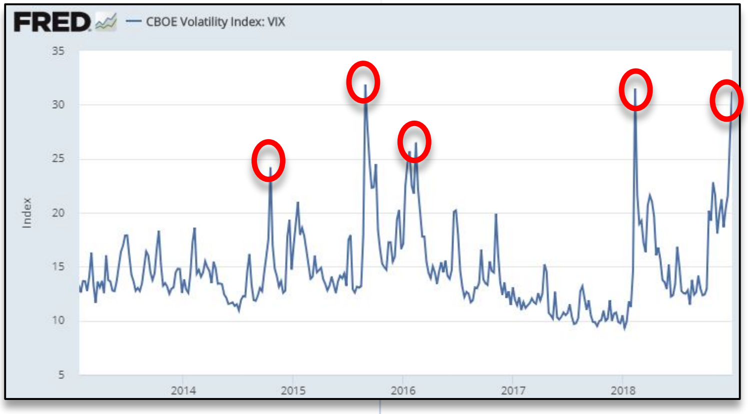
- ❑ Data supports a weakening U.S. dollar in 2019 for two reasons:
  1. Using data going back to 1996, the strength of the U.S. dollar has reached a potential inflection point at the one standard deviation level above its mean
  2. A more dovish Federal Reserve is leading to a lower consensus surrounding the magnitude at which the FOMC is likely to tighten monetary policy, further supporting the case for a weakening U.S. dollar

- ❑ The projected growth of the middle class in large EM countries, paired with a weakening U.S. dollar, is likely to support economic growth and corporate earnings

Data Source: Phillips & Co., Federal Reserve Bank of St. Louis FRED- https://fred.stlouisfed.org/series/TWEXB#0, http://phillipsandco.com/files/4415/4507/1326/MI-GTM_4Q18_December.pdf. Data is from sources deemed to be reliable. No representation or warranties either expressed or implied are made as to the accuracy of the information presented.

Trump: Promises Kept / Promises to Keep

Promises Kept



- ✓ Pulled U.S. troops out of Syria
- ✓ Began the process for leaving the Paris Agreement on climate change
- ✓ Withdrew the U.S. from the Trans-Pacific Trade Partnership trade negotiations
- ✓ Withdrew from the Iran nuclear deal
- ✓ Placed tariffs on a large number of Chinese goods

Promises to Keep

- ❑ Reduce U.S. troop presence in Afghanistan
- ❑ Increase European defense spending and impose tariffs on imported automobiles
- ❑ Win the trade war with China
- ❑ The U.S. and China both remain in the World Trade Organization
- ❑ Complete the renegotiation of NAFTA, now known as United States-Mexico-Canada Agreement (USMCA), which has not yet been approved by Congress
- ❑ Bring peace to the Israeli-Palestinian conflict
- ❑ Implement the $1 trillion plan to build up U.S. infrastructure
- ❑ Secure funding for, and build, the U.S. – Mexico border wall

Data Source: http://phillipsandco.com/files/4015/4647/2265/trump-campaign-promises-2016-election-syria-climate-iran.pdf. Data is from sources deemed to be reliable. No representation or warranties either expressed or implied are made as to the accuracy of the information presented.

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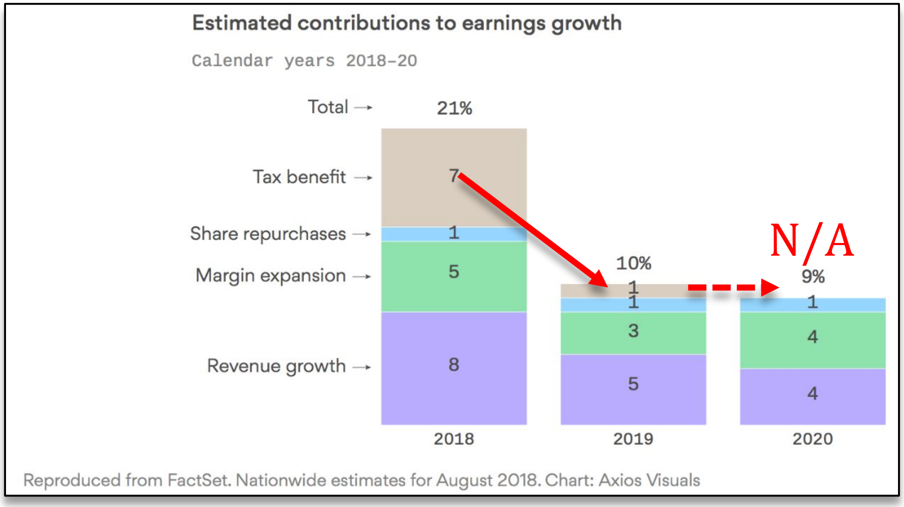
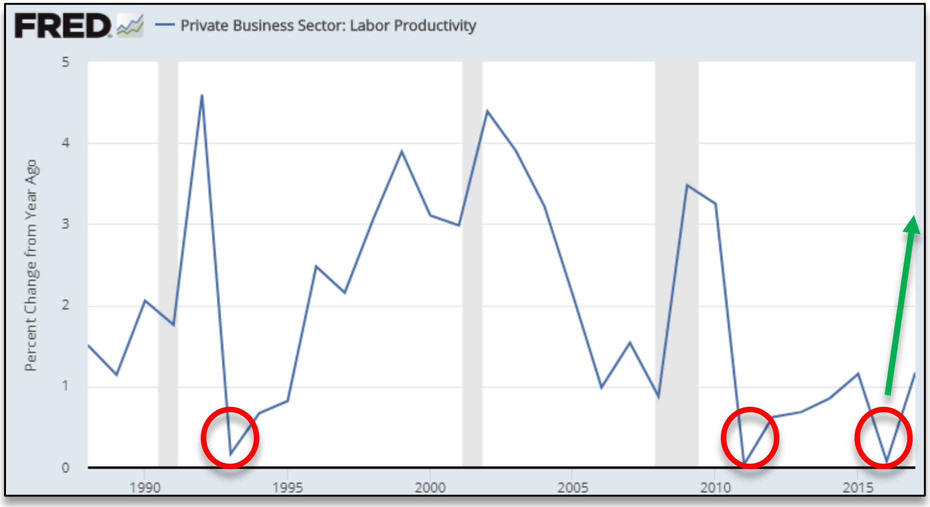
Goodbye, Tax Reform Boosts; Hello, Productivity





- Tax reform was a large contributor to the earnings growth we experienced in 2018
- As this effect wears off on earnings, we'll be looking for revenue growth and margin expansion to be the primary contributors
- As productivity rebounds off its lows (matched in 2011), the increase in productivity is likely to support further margin expansion and revenue growth

Data Source: Bloomberg, https://fred.stlouisfed.org/series/MPU4900062, https://www.axios.com/end-sugar-rush-tax-reform-212b820c-bcc6-429e-894c-17a3894edb51.html. Data is from sources deemed to be reliable. No representation or warranties either expressed or implied are made as to the accuracy of the information presented.

Mean Reversion Dashboard

Style Current P/E as a % of 20-Yr Avg. P/E

	Value	Blend	Growth
Large	98.5%	99.2%	98.1%
Mid	96.4%	97.4%	96.5%
Small	89.3%	99.9%	112.8%

Regional Fwd P/E as a % of 10-Yr Avg. Fwd P/E

ACWI	EAFE Index	EM Index	United States	Germany	U.K.	China	Brazil	India	Russia
90.9%	87.1%	90.4%	92.9%	92.8%	87.1%	89.6%	88.2%	119.8%	84.6%

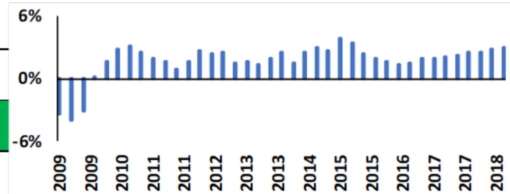
Sector Fwd P/E as a % of 20-Yr Avg. P/E

Financials	Technology	Health Care	Industrials	Energy	Cons. Discr.	Cons. Staples	Comm. Services	Utilities	Real Estate	Materials
92.1%	79.2%	97.0%	94.4%	78.9%	111.7%	109.5%	92.9%	119.7%	117.0%	105.0%

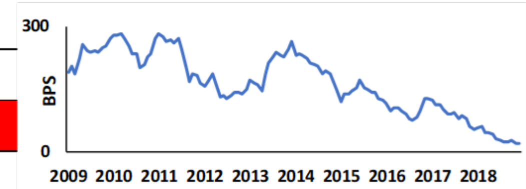
Data Source: Bloomberg LP; JP Morgan Asset Management - http://phillipsandco.com/files/4415/4507/1326/MI-GTM_4Q18_December.pdf. Data is from sources deemed to be reliable. No representation or warranties either expressed or implied are made as to the accuracy of the information presented.

Economic Dashboard

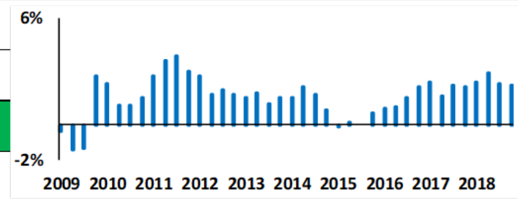
U.S. GDP Growth	*As of 9/30/2018*
Latest Level	3
Change from Prior Quarter	0.1
Latest Direction	Improving
Frequency	Quarterly



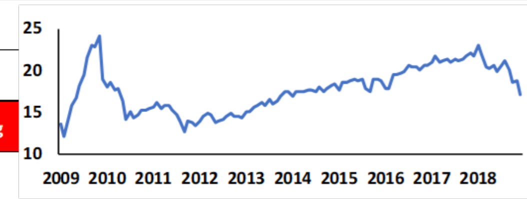
U.S. Treasury Spread 2-Yr vs. 10-Yr Spread	*As of 12/31/2018*
Latest Level	19.6
Change from Prior Month	-0.5
Latest Direction	Flattening
Frequency	Monthly



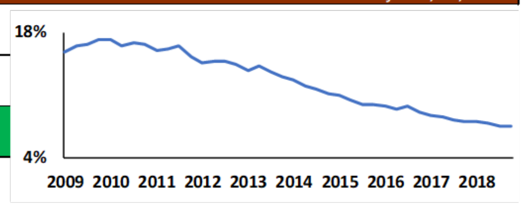
U.S Inflation	*As of 12/31/2018*
Latest Level	2.2
Change from Prior Quarter	-0.1
Latest Direction	Decreasing
Frequency	Quarterly



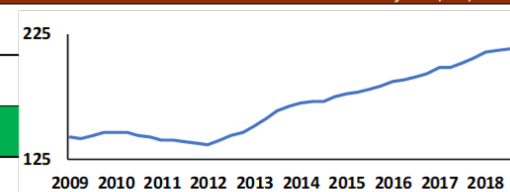
S&P 500 P/E Ratio	*As of 12/31/2018*
Latest Level	17.1
Change from Prior Month	-1.7
Latest Direction	Decreasing
Frequency	Monthly



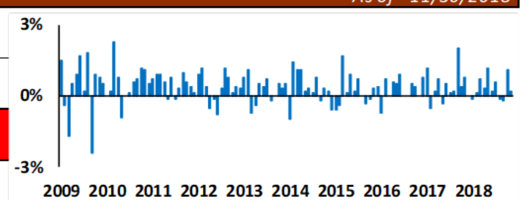
U.S. U-6 Unemployment Rate	*As of 12/31/2018*
Latest Level	7.6
Change from Prior Year	-0.5
Latest Direction	Decreasing
Frequency	Quarterly



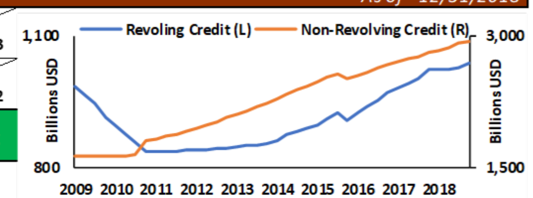
Schiller Home Value Index	*As of 12/31/2018*
Latest Level	213.6
Change from Prior Quarter	0.9
Latest Direction	Increasing
Frequency	Quarterly



Retail Sales	*As of 11/30/2018*
Latest Level	0.2
Change from Prior Month	-0.9
Latest Direction	Decreasing
Frequency	Monthly



Credit: Revolving / Non-Revolving	*As of 12/31/2018*
Latest Levels	1037.4 / 2926.3
Changes from Prior Quarter	9.2 / 16.2
Latest Direction	Expanding
Frequency	Quarterly



Data Source: Bloomberg LP. Data is from sources deemed to be reliable. No representation or warranties either expressed or implied are made as to the accuracy of the information presented.

Phillips & Company

Our View and Recommendations

Our View

- Economic indicators still remain positive for the United States, but brace yourself for a bear market in equities
- The yield curve between 2-Year and 10-Year hasn't inverted yet, but it's on its way and remains a leading indicator of a potential recession in the United States; keep in mind that it's the tightening of bank lending standards that is directly linked to the slowdown in economic activity
- As the yield curve continues to flatten, be mindful that rolling three-month periods of flattening, on average, has led to double-digit forward-looking returns for stocks
- Expect continued volatility driven by political instability throughout the U.S.
- The U.S. dollar is likely overvalued relative to other currencies; the future projected weakness, as well as the growth of the middle class, supports allocating capital to Emerging Markets
- Valuations across major indices have contracted significantly in 2018, paving the way for buyers to step back into the equity markets
- A more dovish rhetoric from the Federal Reserve could be accommodative for equity investors

Recommendations

- Continue U.S. portfolio weightings to policy targets of +/- 2%
- Continue portfolio weightings toward Small Cap equities; +/- 2% of policy targets
- Tilt to growth vs. value
- Rebalance back to target for EM
- Rebalance Developed Markets to policy
- Remain active in Fixed Income, but be mindful of where you sit in the capital structure and the covenants associated with what you own
- Continue to favor moderate durations close to the benchmark as Fed action will likely impact short-term rates and the flight to safety will likely impact long-term rates
- Look for opportunity in noncorrelated assets to help mitigate risk and reduce beta in the overall portfolio

Data Source: Phillips & Co.

THANK YOU

tphillips@phillipsandco.com