



REVIEW OF CURRENT MARKET VOLATILITY

After the sell-off in October the stock market staged a pretty nice rally the first part of November. But here we are again probing the October lows. While extremely uncomfortable this market action appears to be consistent with a normal, healthy correction.

Let's explain what we mean by a healthy correction. **If the market didn't have occasional corrections, greed would take over and prices would move to unsustainably high valuations ultimately resulting in a major decline that could negatively impact the overall economy.**

Think of the damage done during the tech wreck at the turn of the century and the financial crisis ten years ago where overvaluation and over confidence not only affected the market but had a significant impact on the economy.

We would argue that the stock market has been in correction mode for almost a year now. A majority of stock sectors had corrected even before this latest rout. What is encouraging is that the FANG+ stocks are leading the decline while quality and defensive stocks are moving higher. For example, we bought Pepsi and Johnson & Johnson in the spring and summer and they are up roughly 16% and 20%, respectfully. This market action is a change from the initial decline in January where the FANG+ stocks fell less than other stocks and rallied more during the recovery.

Because of still strong earnings, valuations are starting to look quite good, plus financial leverage appears to be contained. Credit markets are downright calm which is very positive. Our biggest worry is that the stock market is signaling a looming recession at some time in the future. However, while slowing, the world economy is still growing led by the U.S.

In January we said the pertinent message of the return of volatility is that above average returns will not continue and that a more active approach to portfolio management best characterized as selling stocks into strength and buying into weakness is warranted. We still believe in this strategy and have used our cash to buy during this correction. If the market finds its sea legs and rallies over the next few months we expect to raise cash into strength.

Please feel free to call us with any questions. Best wishes,

Jim Tillar, CFA, Steve Wenstrup