STIR

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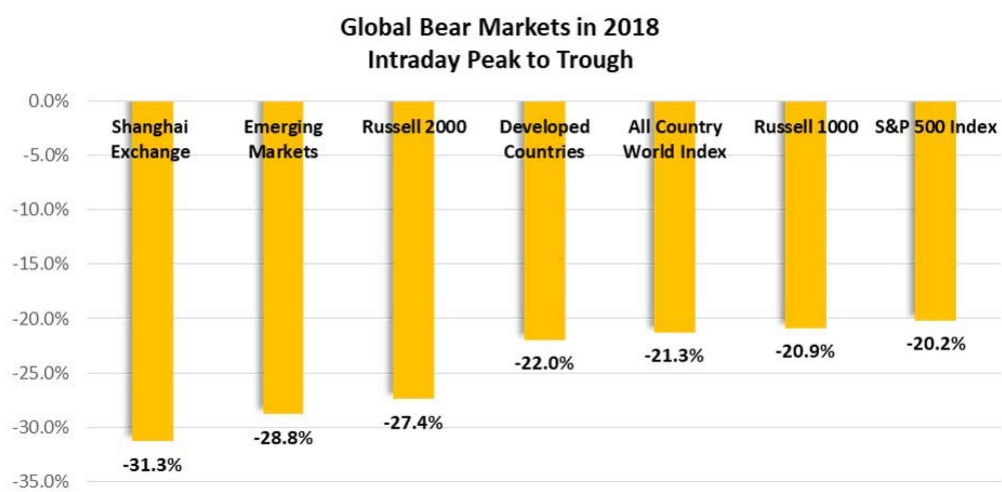
STIR 2019 MARKET OUTLOOK

BEAR MARKET ENDS, NEW BULL MARKET MOVES TO NEW HIGHS!

Investors will be pleased with returns in 2019 over the results of 2018. While the year may begin with further downside before the global cyclical bear market ends, it should be followed by the start of a new cyclical global bull market.

In a surprising reversal from history, Q4 is normally one of the stronger quarters of the year and especially in a mid-term election year. However, U.S. stocks tanked and joined the rest of the world by moving into bear market territory. Until this occurred, the U.S. was the bright spot.



Global Bear Markets in 2018

Q1 2019: Bear Market ends, but expect continued volatility.

Investors ended 2018 focused on the possibility of a recession in 2019 or 2020. Market declines precede an actual recession as investors begin selling before the actual event occurring. Market analysts are trying to sooth investors' concerns by commenting that the market decline will not be bad because there is no recession in sight. The consensus by investors links bear markets and recessions as 'they go hand-in-hand'. With memories of the last recession in 2008-2009, and a bear market of over -50% it is no wonder investors are apprehensive.

Looking at history, not all recessions are preceded by bear markets, and bear markets can occur without a recession. STIR researched the data of the past 70 years and separated market decline (MD) data into four categories.

1. MD with No recession in a secular bull market.
2. MD with a recession in a secular bull.
3. MD with No recession in a secular bear.
4. MD with a recession in a secular bear.

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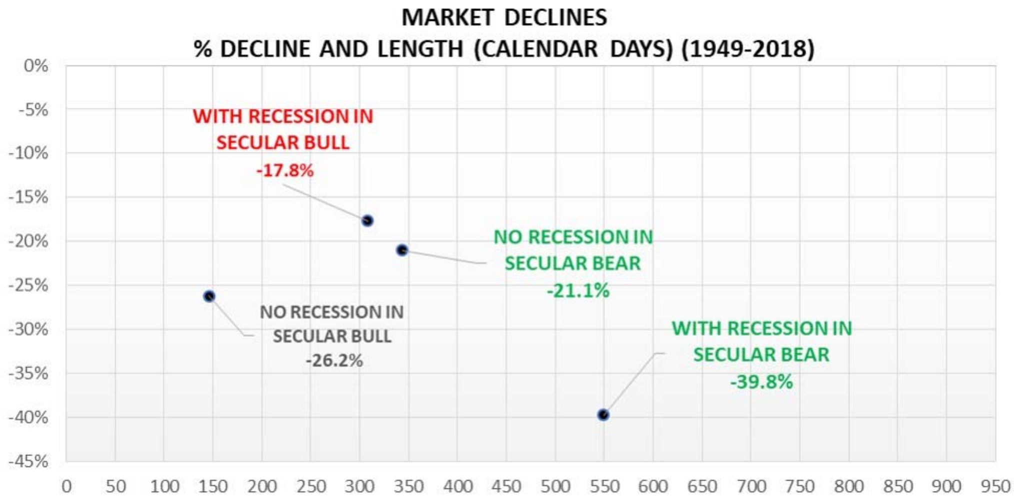

Market Declines

Rightfully, an investors' worst nightmare is the market declines that occur when a recession occurs in a secular bear. They run up big losses, averaging almost 40%, and drag out on average of 1 ½ years. The last combination of a recession in a secular bear was just over a decade ago, and still a painful memory to many investors. From its October 2007 peak to its March 2009 low, equities lost over half of their value.

Surprisingly, history tells us that the second weakest combination is a market decline with No Recession in a secular bull (NRSBull), which is the case today. When this has occurred, the market falls on average 26%. So far, the decline at its most recent low has been just over 20%. Three of the previous market declines (NRSBull) were under 22%, so it is possible most of the damage has already been done. The worst case was the 1987 debacle of -33% (NRSBull).

The good news, of the four possible combinations shown above, Market Declines where there is No recession within secular bulls are the shortest! The average decline eats up only 160 calendar days, and as of the low on 12/24/2018 it was at the 95th day.

In Q2, Q3 and Q4: Expecting a Global Market Recovery

With a bear market behind us, a new cyclical bull market can begin. The annualized gain in cyclical bulls in a secular bull is one of solid double-digits, from the low teens to high thirties! If the new cyclical bull was just average over the following three years it could push the Dow to over 40,000!

One of the winners in the coming global bull market may be Emerging Markets (EEM). It may have the biggest rebound as it is one of the cheapest markets. Historically, Emerging Markets has the strongest relative performance on all the major regions after the end of global slowdowns. We are already seeing signs of early strength. Emerging Markets hit its bear market low in October after peaking last January. Since that October 29th low, EEM has gained over 5% while the S&P has fallen another 5% (as of 12/31/18). That is a powerful sign that more over performance is to come.

Consumer Services (Discretionary). Record employment, rising wages (the best in over a decade), high consumer confidence and low gas prices add up to a great combination for higher consumer spending. It was the third best performer in 2018. Retailing may emerge as the winner within the broader Consumer Services sector.

Healthcare. It was the leading sector in 2018, one of three that was able to post a gain, and should maintain that leadership going into 2019. Demographics continue to be the driving force but do expect growing focus by politicians on drug pricing.

Technology and Industrials will benefit with a resurgence in Capex (capital expenditures). With the end of the global slow-down by mid-year, a recovery in oil prices, rising business optimism, and record high cash flows, this has produced one of the best environments for Capex. Technology will be a big beneficiary and to a smaller degree, Industrials.

Financials could emerge as a leader as fears of recession ebb and global growth resumes. That could cause a small gain in yields and a steepening yield curve, both a necessity for any meaningful recovery. This scenario would also hurt bond proxy sectors like real estate, utilities and telecom. An outlier could be **energy** and energy services if oil prices stabilize and recover after their bear market.

View any Q1 weakness as a buying opportunity.

- Q4 2018 was so bad (-14% for the S&P and -18% for NASDAQ), that it becomes good. Ned Davis did a study that since WWII large quarterly drops of over 15% in the S&P 500 are often followed by higher prices: on average, one year later stocks may gain over 23% and by 43% over the following two years!
- Over the past six decades, the S&P 500 has gained an average of 30+% in the following year from the midterm year lows. With the 2018 midterm year low occurring on Christmas eve (12/24/2018) of 2350, that could give investors a nice 2019 Christmas present of 3050+ on the S&P!

2019 Market Outlook is for 3100 for the S&P 500, Double Digit Gains!

What could go wrong? Plenty of things but on the top of our list is the current government shutdown which could last a lot longer than anyone is forecasting. Another big concern is what if the China - U.S. trade talks drag on or turn negative? Either of these scenarios could prolong the global economic slowdown and the higher levels of uncertainty could push P/E multiples lower off setting any gains in expected earnings in 2019.

As always, the STIR Research quantitative analysis will react to actual market trends to guide us through 2019. The STIR Market Outlook gives us an educated glimpse based on history of what may occur.