J.W. Burns & Company

Investment Counsel

Quarterly Update - April 2019

A Quick Comeback But No Complacency Here

"What is the most common investor mistake? Trading. Getting in and getting out at all the wrong times, for the wrong reasons." - Ken Fisher

Dear Clients and Friends,

Stocks had explosive gains in the first three months of 2019, recording their best first quarter since 1991. The returns were broad based among all sectors and equity asset classes, with the S&P 500 Index up 13.65%, small and mid-cap stocks both up over 11%, and international stocks, as measured by the MSCI All World ex-USA Index, up 10.27%. Bonds also joined in the rally, with the Vanguard Total Market Bond Index up about 3%. Our positions overall did very well, and we believe the fundamentals underlying this 10-year bull market remain intact. However, the path ahead will likely be more volatile than the smooth-sailing quarter that just ended.

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The first quarter's powerful rally stands in sharp contrast to 2018's fourth quarter bloodletting, when the S&P 500 Index fell by almost 14%. These dramatic up and down movements should reinforce the simple truth that almost no one can successfully time stock market swings. As legendary value investor Seth Klarman has stated: ***"The single greatest edge an investor can have is a long-term orientation."***

So, what changed from last year's fourth quarter drop to our powerful rally in this year's first quarter? Essentially, the tone and comments from Federal Reserve Chairman, Jerome Powell, whose initially hawkish stance on raising interest rates sent markets into a free fall during the last three months of 2018.

However, on January 4, just two trading days into the New Year, Powell made a complete 180, promising the Fed would be "flexible, patient, and data dependent" with future rate decisions. Investors liked what they heard, the Dow Jones Industrial Average rose 747 points that day, and has not looked back since.

A quick comeback indeed.

We believe last year's sharp correction was healthy and dampened speculation and animal spirits, which should allow this long-running bull market to continue.

The Dow Jones Industrial Average dropped 19.7% from the highs reached in early October to the bottom on Christmas Eve. Historically, returns in the one-year period after a bottom average 38%.[1] In our last client letter, ***"Bears Sound Smarter, But Bulls Make More***

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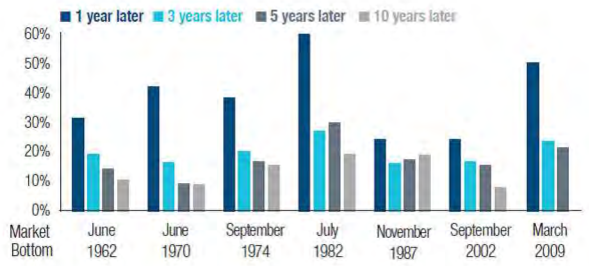
Money," we included a chart showing the returns on stocks after bear markets. While past performance is certainly no guarantee of future results, the chart below is worth reviewing again.

Recoveries From Bear Markets



Average Return After Bear Market	
1 Year Later	38.4%
3 Years Later	19.8%
5 Years Later	17.7%
10 Years Later	13.5%

Source: T. Rowe Price, data from 12-31-61 to 12-31-17

Because 2018's late year sell off ended on Christmas Eve, right toward the start of a new calendar year, 2019 is indeed shaping up to be a fine year for stocks, if history is any guide.[2]

Importantly, 2019 represents the third year in the presidential cycle, which historically is the best year for stocks by far, with the average return being 17.8%.[3] Furthermore, outside of recessions and world wars, stocks have never fallen two years in a row.[4] In fact, in my 32 years of experience in the investment counseling profession, a moderate economic growth and low interest rate environment – such as the one we have now – has provided the strongest returns.

Of course, markets climb a wall of worry, and as always, there are challenges. Brexit is a mess, there has been no trade deal completed with China, and global economic growth has slowed. However, our base case is that these concerns will likely be resolved, managed, or mitigated in such a way as to not derail this bull market. Time will tell.

Now let's get on to some of your questions.

"In my 32 years of experience in the investment counseling profession, a moderate economic growth and low interest rate environment has provided the strongest returns"

Q: You predicted markets would have a "solid 7-11% or so return in 2019." Well, we are already at 14%...do stocks have more room to run in 2019?

A: I must first remind you that I qualified my 2019 prediction by saying that if risks to the market generally moderated, returns could be higher.

That being said, we make our assessment of the market's forward potential through the lenses of four key drivers of equity performance: interest rates/ liquidity, economic conditions, earnings, and valuations. Currently, three of the four are positive, and I believe the fourth is going to improve.

As I mentioned earlier, the Federal Reserve has changed its tone from a relatively aggressive posture toward raising rates to a more dovish stance. In fact, in October last year the market was pricing in three 2019 rate hikes. Now, it is widely assumed there will be no interest rate hikes at all in 2019!

The economy has slowed somewhat, but most leading economic indicators remain positive and do not indicate a recession on the horizon.

Skipping to valuations, they are still reasonable and certainly not expensive, currently selling at about 16 times 2019 earnings estimates. Furthermore, I do not see any signs of investor euphoria or exuberance, which usually precedes corrections or bear markets.

Earnings are the wildcard. At the beginning of 2019, full-year earnings were expected to grow over 11%. But over the last three months, these full-year estimates have steadily declined to about 5%, which is what I stated would likely be the case for the full year in our January letter. We believe earnings estimates have likely bottomed, and the first quarter earnings season, which we are in now, may show very slight earnings growth for the overall S&P 500 this quarter, maybe 1-2%.

So, if earnings exceed these modest expectations, markets will add to their already impressive run. However, if we come up short, like an earnings recession (defined as two consecutive quarters of negative earnings growth for S&P 500 companies), markets will probably decline somewhat from here, at least in the short run.

We are of the opinion that a reduction in trade tensions, healthy corporate cash flows, and dividend increases/share buybacks will provide an additional buffer for stocks and can drive the market higher. So, yes, I believe we may see additional gains this year.

Q: You are pretty much always bullish. Do you ever get bearish?

"A reduction in trade tensions, healthy corporate cash flows, and dividend increases/ share buybacks can drive markets higher."

A: Well, as we all know, 2018 was a volatile year that ended ugly. In February, October, and December of last year, I wrote three separate communiques sharing our thoughts on the state of the markets. In reviewing them, I felt that all three were measured and sincere with acknowledgement that the market downturn could continue and that clients must embrace a long-term view.

There are times when we are bullish and others less so; when we are more on the offensive with your investments and other periods that we may raise some cash or take more defensive positions, as we did in 2008-2009. Yes, we were hit hard during that period, but from everything I read and saw, we held up quite a bit better than most investors.

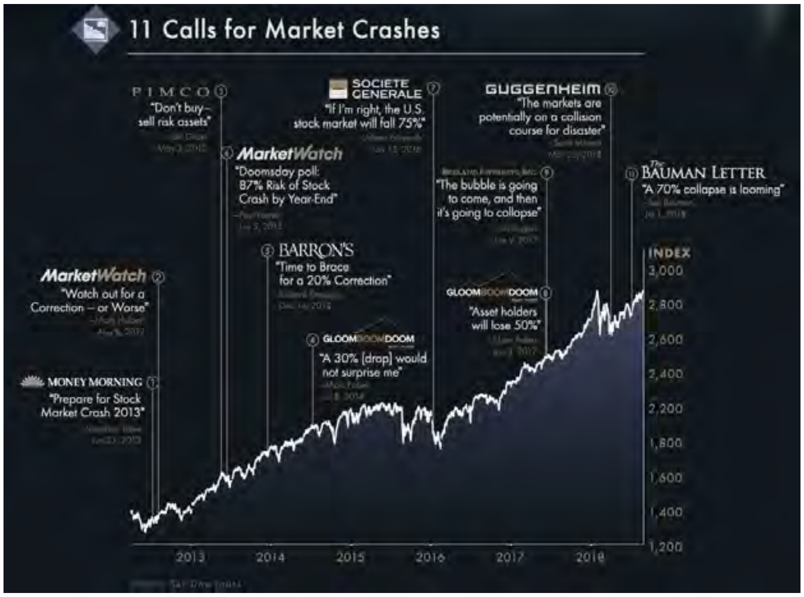
As I stated earlier, timing market swings or attempting to avoid the pain of market declines is a fool's errand. On March 9, 2009, the market hit bottom during the Great Recession. The NY Times had a quote from a trader that morning: "The only hope we have is there is no hope." Simply put, there was nothing whatsoever that could have predicted the sustained, powerful recovery in stock prices that was about to come.

Let me point out some undisputable facts about the importance of being invested in the market for the long term and avoid panic selling. From 1996 to 2015, if an investor was out of the market for the top ten market performance days they would only capture 58.6% of the total market return over that period! For an investor out the top 20 days; they'd only realize 31.1% of the market's gains.[5] The data is clear: to build long-term wealth in the stock market, you must remain invested in the market, which will inevitably include both rallies and corrections.

You own great companies, with great managements, that were bought at attractive prices. Mistakes will be made occasionally, but overall, we are very pleased with the performance and positioning of your portfolio(s). Stocks have been the best wealth creating asset class over the years by a wide margin. Our firm has pressed our equity weighting as high as possible for our individual clients, and this has proved a winning call, to this point.

I truly believe in America and American businesses. So why would I not be bullish? I can't time market swings, and I pretty much know what the end result will be: solid wealth creation. As Warren Buffett said: "For 240 years, it's been a terrible mistake to bet against America, and now is no time to start."

As some of you know, I co-hosted a television show, *Financial Fitness*, for a number of years. I had many really sharp guests that came on and outlined the various reasons why the stock market was overvalued at that time and that a big decline was imminent. No kidding, most of them have had to find new jobs because their bearish stance didn't pan out. Remember the title of last quarter's letter and take it to heart: ***"Bears Sound Smarter, But Bulls Make More Money."*** See the chart below to see just how wrong the bears have been over the last decade.



I know this bull market will end at some point; it will be frightening, and the negative returns will last longer than just three months. This is simply part of the investing process. But as legendary investor, John Templeton, said: "There will always be bull markets followed by bear markets followed by bull markets." Most importantly, over the long term, our disciplined approach of keeping you invested in quality American businesses should continue to win out.

Thank you for your continued confidence. Please contact us with any questions and enjoy the spring!

Best wishes,

Jim

James C. Burns, CFA
President

P.S. In some of our upcoming Client Newsletters I thought I would highlight the senior members of the J.W. Burns & Company team. To kick it off, I wanted to start with a man who for many of you probably needs no introduction: Peter Bunitsky. My first ever hire, Peter joined our firm right after Labor Day in 1990. While I was initially not a fan of his bushy, black (now gray) beard, I didn't let that prevent me from making the hire of a lifetime.

Peter has been with our firm now for almost 30 years and sports unrivaled experience, knowledge, and service to our valued clients. The results of our in-depth personality profile compared him to an Elmer Fudd like figure, describing him as meticulously detailed, precise, and honest as the day is long.

Peter is like a brother to me, and I am grateful for his commitment and work ethic.

This past month a long-time client, Don Kompf, whose permission I have to share this, said the following about Peter:

Jim: I know that you're well aware of this, but I wanted to confirm your opinion. Peter is extremely helpful. He's very knowledgeable and prompt, qualities I appreciate, and I always have the feeling that my best interests are paramount with Peter. Be sure that you never let Peter retire.

Outside of his role as Senior Portfolio Manager, Peter serves his local church and, is in fact, an ordained Eastern Orthodox Priest. And as many of you know, he and his wife Mary spend their summers in their home in Alaska.

But have no concerns, we have installed Peter a "satellite office" for him to work when he is not fishing or wrestling bears. We keep him busy.

Peter with his latest catch and his lovely wife Mary.

J.W. BURNS & COMPANY, INC.

INVESTMENT COUNSEL

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1 T. Rowe Price, "The Case For Staying Invested in Stocks." November 2018

2 Global Financial Data, Fisher Investments, February 2019

3 Global Financial Data, Fisher Investments, February 2019

4 Global Financial Data, Fisher Investments, February 2019

5 Morningstar Direct