ECONOMIC AND MARKET COMMENTARY

1st Quarter 2019

SMITH SHELLNUT WILSON

OUR MISSION

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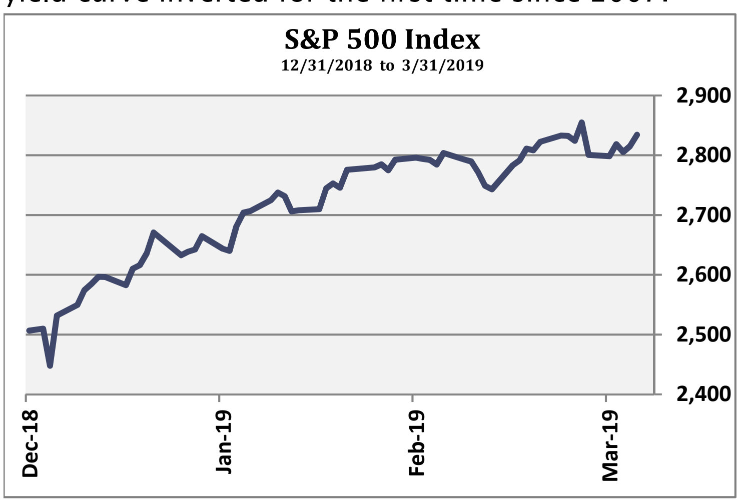
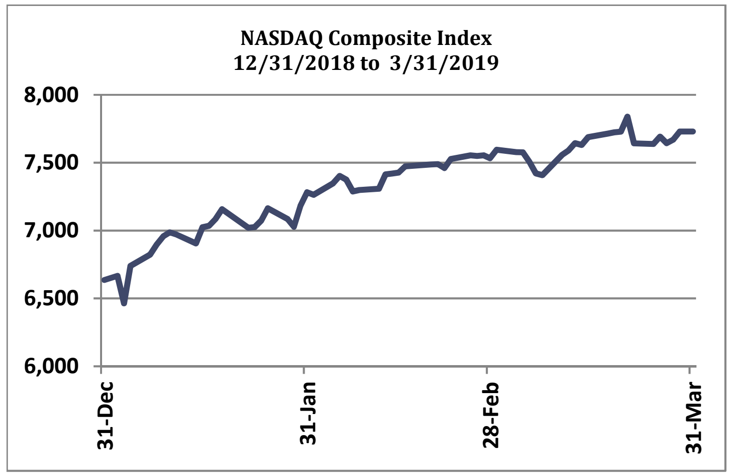
I. First Quarter 2019 Equity Market Recap

Coming off its worst quarterly performance since 2011, the S&P 500 rebounded 13.1% in the first quarter, for its best quarterly performance in ten years. The rebound is being largely attributed to an oversold bounce, improving expectations for a trade deal with China, and, maybe most importantly, a "dovish pivot" by global central banks. While the first two months of 2019 were a virtual straight line higher, a healthy dose of caution surfaced in March as the yield curve inverted for the first time since 2007.



For the quarter, the Nasdaq 100 and Composite indices continued their leadership role with gains of 16.6% and 16.5%, respectively, followed by the small-cap and mid-cap Russell 2000 and S&P 400 indices, with respective gains of 14.2% and 14%. The large-cap S&P 500 and Dow Jones Industrials followed with gains of 13.1% and 11.2%, respectively.



Despite global growth concerns and on again, off again trade discussions with China, the tech sector continued to stage a nice rebound in the first quarter, with March being no exception. So far, the consumer continues to be willing to spend more on goods and services, including technology. Confidence remains elevated, helping to support the sector over the near term.

Technology was not only the top performer for the month of March but was also the strongest sector for the quarter, notching its highest growth rate since 2012. For the month of March, information technology was up by 4.75%, and for the quarter up a whopping 19.37%, retracing a fourth-quarter loss of 17.7%.

*Registration of an Investment Adviser does not imply any certain level of skill or training.

For U.S. stock indexes to move meaningfully higher, technology stocks, as the largest weight in the S&P 500 Index (21%), will have to participate. If not, healthcare and financials (combined 27% weight) will have to take the leadership mantle -- and this seems difficult given the recent weak performance of the financial sector.

Earnings estimates have been falling since the beginning of the year. Fortunately for the stock market, interest-rate expectations have also fallen sharply, supporting equities. When January began, the aggregate estimate for first quarter 2019 S&P 500 earnings growth was 2.9%. However, analysts have been cutting first-quarter estimates and the expectation is now for an earnings decline of 3.9%, which would be the first decline in quarterly earnings since the second quarter of 2016.

Second-quarter estimates have also been falling slightly currently hanging on to positive territory by a thread, at +0.1%. However, market analysts seem to be hoping for an earnings rebound in the third and fourth quarters (+1.7% and +8.3% growth estimates, respectively).

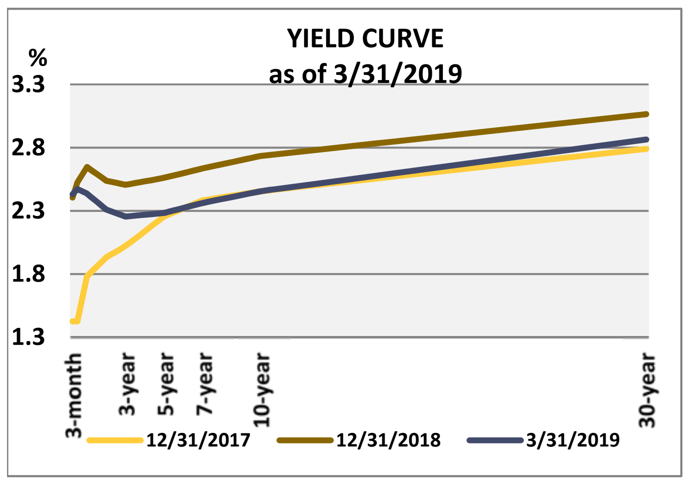
Part of the reason the market is not reacting more negatively to the low earnings growth number is the fact that revenue growth is still looking positive, with estimates ranging between 4.3% and 4.8% for all four quarters in 2019. Wall Street appears more patient with a margin problem than with a broader macro revenue problem. One-year forward price/earnings ratios have recovered from their December lows below 15X and now sit at about 17X expected 2019 earnings. Even still, price/earnings expectations remain below September 2018 levels despite the lowered earnings expectations.

II. First Quarter Bond Market Recap

U.S. Treasury 10-year note yields made 15-month lows in late March, bottoming at 2.34%. At that time, the yield on the 10-year note dipped below 3-month Treasury bills for the first time since 2007. This was a risk which market participants had debated going into the last rate hike at the December 19th FOMC meeting.

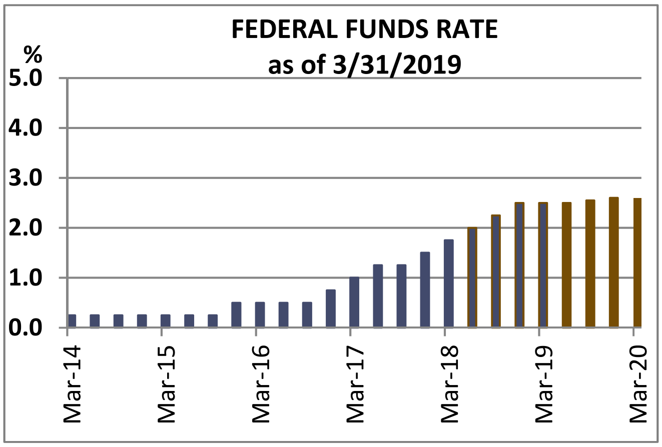
The primary concern is whether the inversion is signaling an upcoming recession, albeit with a lag. While the short end, from 3-month bills out to the 5-year notes, remains inverted, the spread between ten-year notes and 3-month bills has since regained its positive slope, and the longer 30-year bond to 5-year note spread has actually been widening since the summer of 2018.

Yields on intermediate-term Treasury notes fell by 23-28 basis points during the first quarter, leading to a so-called “bull flattening” in the yield curve, with rates on longer maturities declining by more than rates on shorter maturities.



Ironically, the late March inversion was driven by dovish comments made by Fed officials after the March FOMC meeting, following a number of hawkish miscommunications in the fourth quarter. The Fed now expects to end its balance sheet reduction program by September, an about face from December's "autopilot" commentary, and it also reduced its 2019 rate hike expectations from two to zero. Markets seemingly view this less as a "Fed put" to support the stock market and more as a sign that the economic cycle could be nearing its end. While

Fed Chairman Powell said there was no bias about the next direction, hike or cut, markets at the time were pricing in as much as a 75% probability (currently 64%) that the Fed's next move will be a rate cut by December.



Bar chart data in brown indicates projections implied by fed funds futures.

Over the last 35 years, there have been four periods where the Fed held rates steady (1989, 1995, 2000, and 2006), ranging from 3.5 to 15 months in duration. Regardless of whether the yield curve was normal, inverted or flat at the time, rates moved lower in each of those episodes and the yield curve steepend.

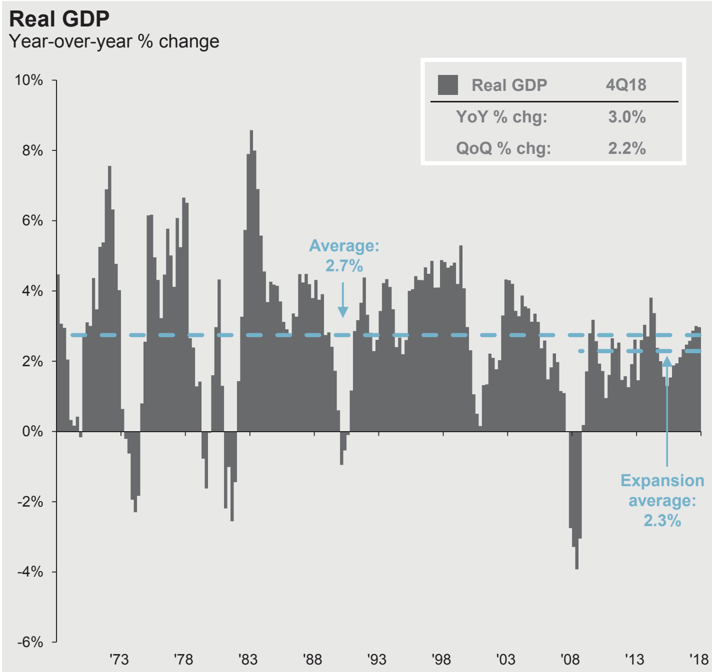
III. Outlook

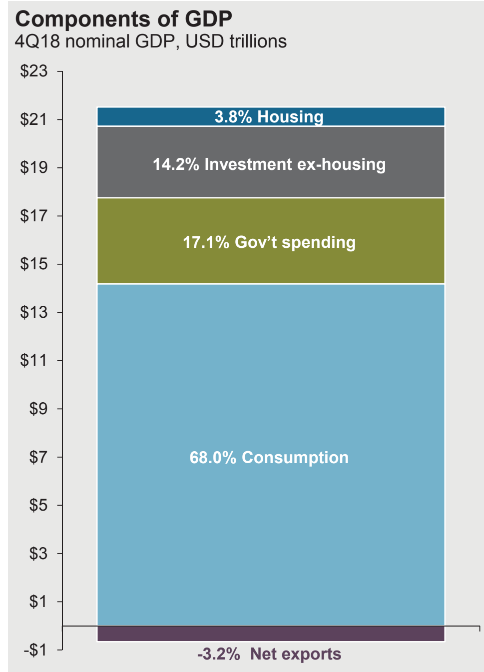
Stocks and bonds are adjusting to a new paradigm of lower growth and a belief that the Fed overshot by raising rates in December. The Fed is now on hold, and markets are pricing in a cut in the federal funds rate by year end. While the "Fed put" is generally seen as a positive for stocks, history shows that the start of rate cuts typically marks a turn in the economic cycle, causing stocks to decline and yield spreads to go from inversion to a positive slope. We have not yet reached this point. Despite slowing economic activity and flat to negative corporate earnings growth, a shift towards accommodative policies coupled with hopes for a U.S.-China trade resolution has stocks remaining at close to all-time highs.

The source of the information in this commentary is SSW and NASDAQ.com unless otherwise noted.

Economy

Economic growth and the composition of GDP

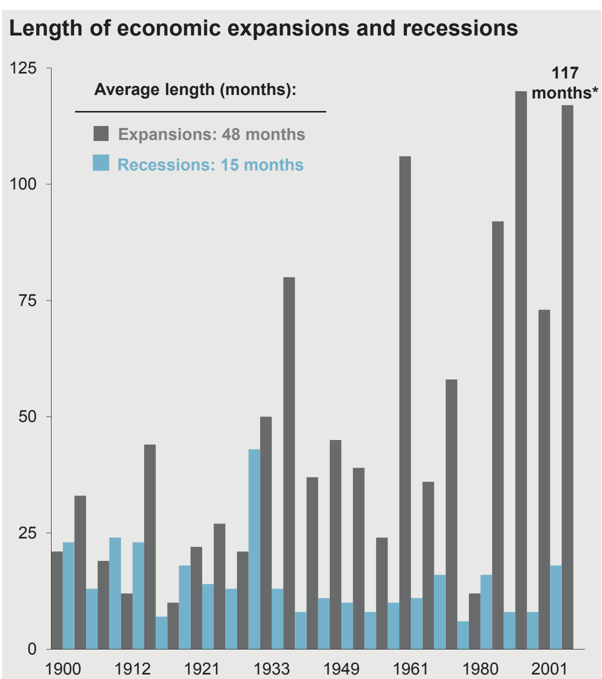


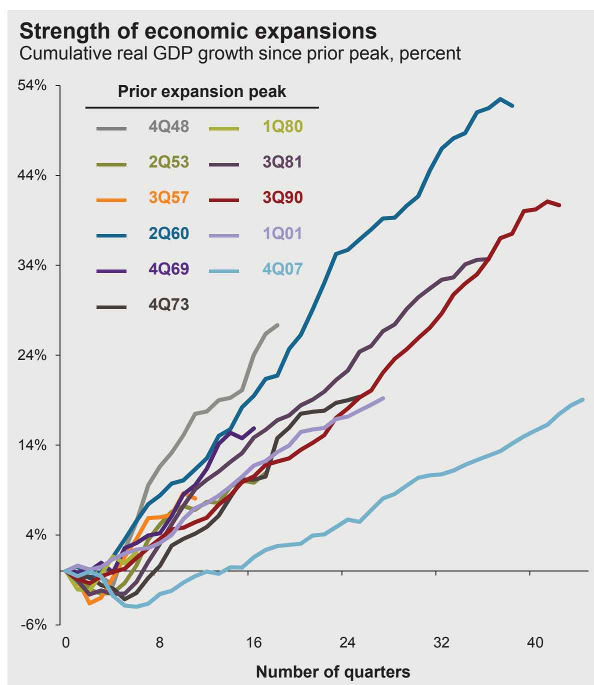


Source: BEA, FactSet, J.P. Morgan Asset Management.
Values may not sum to 100% due to rounding. Quarter-over-quarter percent changes are at an annualized rate. Average represents the annualized growth rate for the full period. Expansion average refers to the period starting in the third quarter of 2009.
Guide to the Markets – U.S. Data are as of March 31, 2019.

Economy

The length and strength of expansions





Source: BEA, NBER, J.P. Morgan Asset Management. *Chart assumes current expansion started in July 2009 and continued through March 2019, lasting 117 months so far. Data for length of economic expansions and recessions obtained from the National Bureau of Economic Research (NBER). These data can be found at www.nber.org/cycles/ and reflect information through March 2019. Past performance is not a reliable indicator of current and future results.
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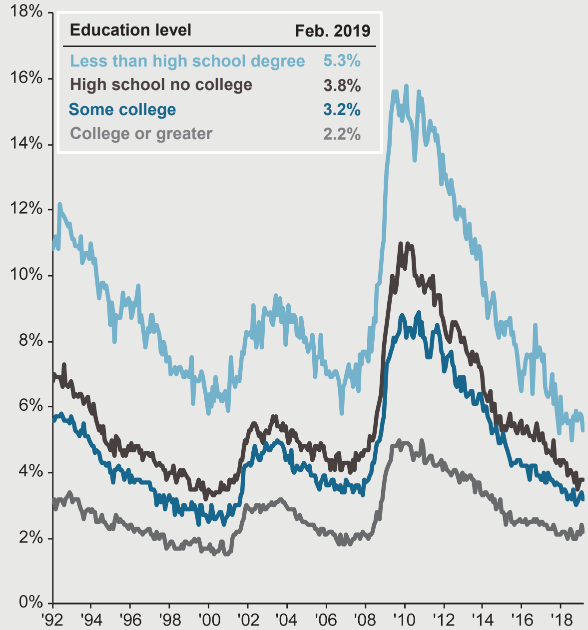
Employment and income by educational attainment

Economy

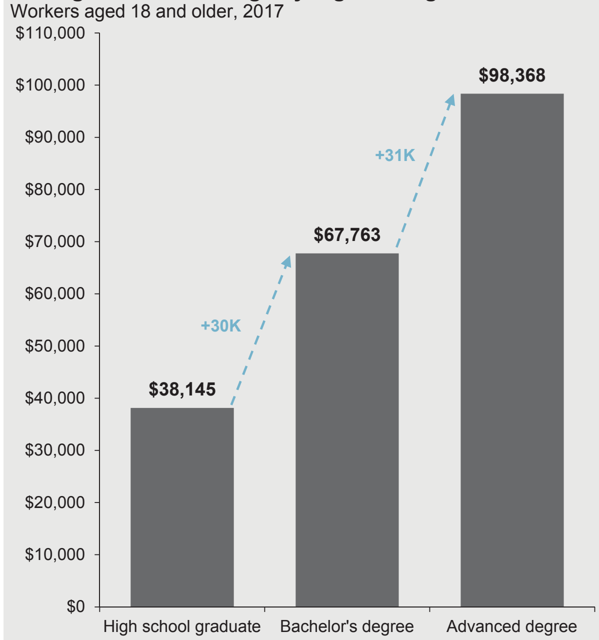
Unemployment rate by education level



Education level	Feb. 2019
Less than high school degree	5.3%
High school no college	3.8%
Some college	3.2%
College or greater	2.2%

Average annual earnings by highest degree earned

Workers aged 18 and older, 2017



Source: J.P. Morgan Asset Management; (Left) BLS, FactSet; (Right) Census Bureau.
Unemployment rates shown are for civilians aged 25 and older. Earnings by educational attainment comes from the Current Population Survey and is published under historical income tables by person by the Census Bureau.
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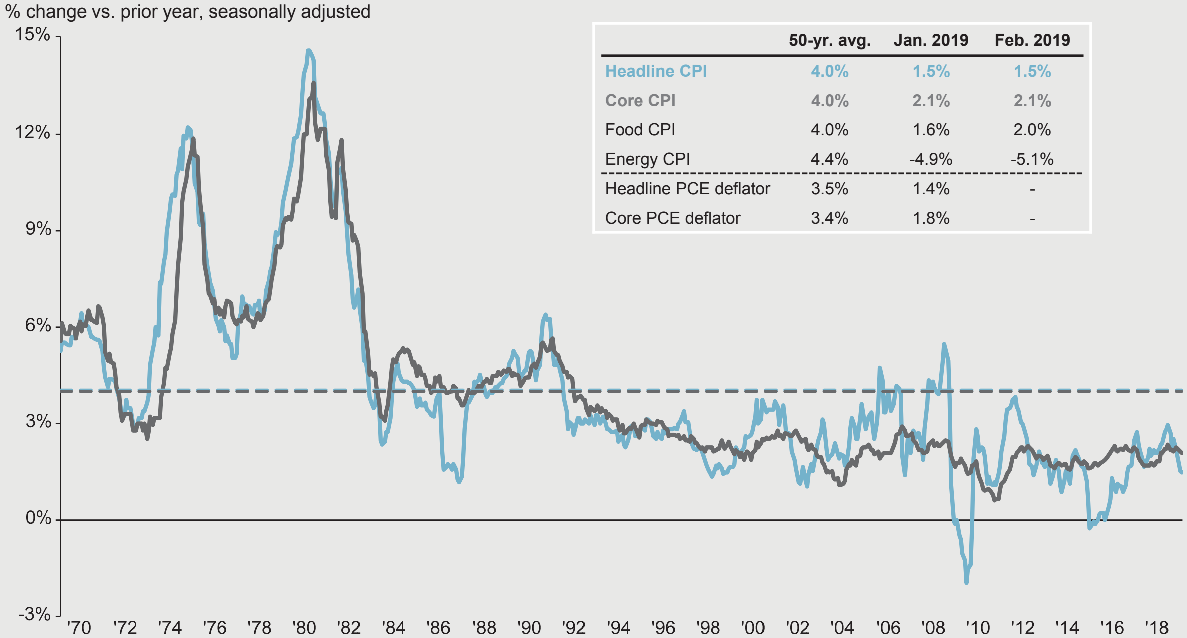
Inflation

Economy

CPI and core CPI

% change vs. prior year, seasonally adjusted



	50-yr. avg.	Jan. 2019	Feb. 2019
Headline CPI	4.0%	1.5%	1.5%
Core CPI	4.0%	2.1%	2.1%
Food CPI	4.0%	1.6%	2.0%
Energy CPI	4.4%	-4.9%	-5.1%
Headline PCE deflator	3.5%	1.4%	-
Core PCE deflator	3.4%	1.8%	-

Source: BLS, FactSet, J.P. Morgan Asset Management.
CPI used is CPI-U and values shown are % change vs. one year ago. Core CPI is defined as CPI excluding food and energy prices. The Personal Consumption Expenditure (PCE) deflator employs an evolving chain-weighted basket of consumer expenditures instead of the fixed-weight basket used in CPI calculations.
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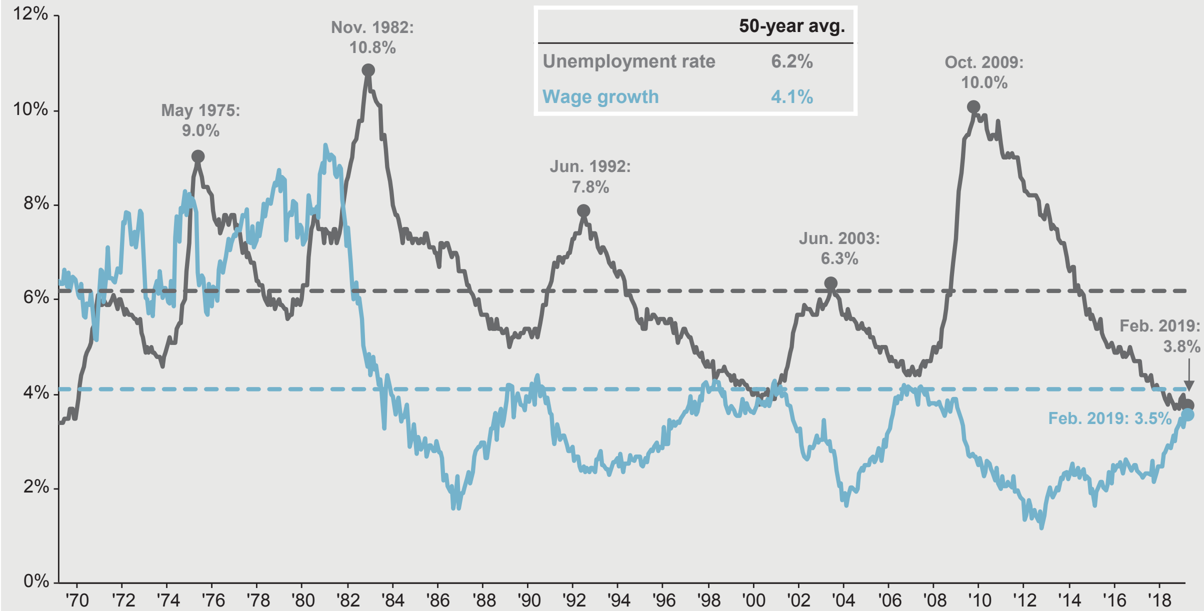
Economy

Unemployment and wages

Civilian unemployment rate and year-over-year wage growth for private production and non-supervisory workers
Seasonally adjusted, percent



Source: BLS, FactSet, J.P. Morgan Asset Management.
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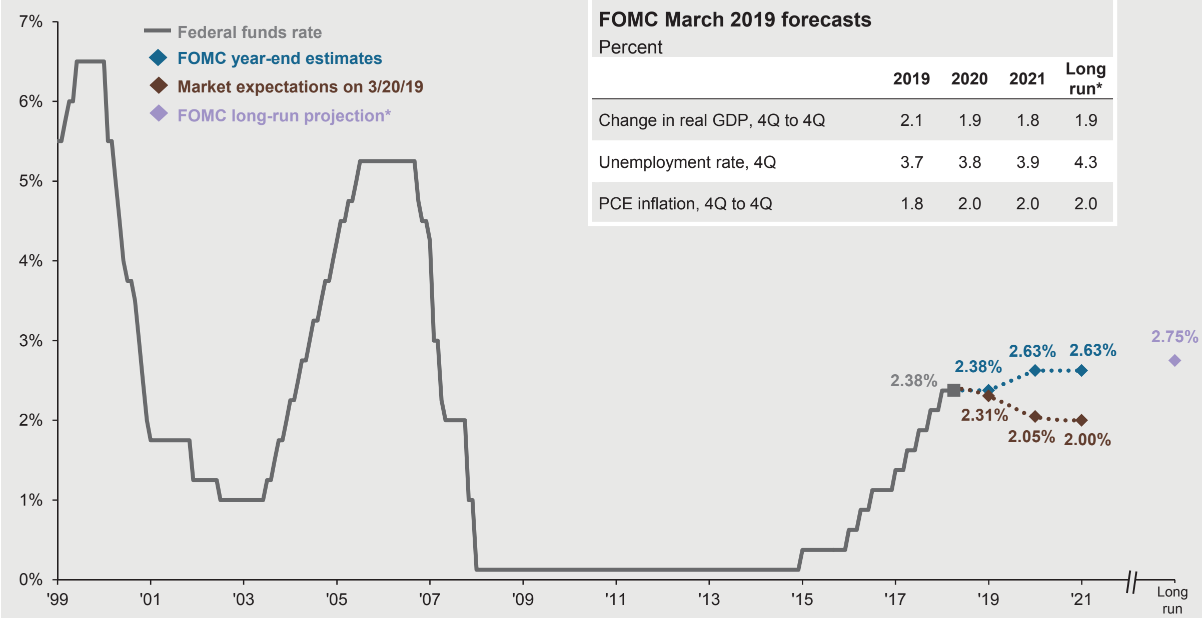
Fixed income

The Fed and interest rates

Federal funds rate expectations
FOMC and market expectations for the federal funds rate



FOMC March 2019 forecasts
Percent

	2019	2020	2021	Long run*
Change in real GDP, 4Q to 4Q	2.1	1.9	1.8	1.9
Unemployment rate, 4Q	3.7	3.8	3.9	4.3
PCE inflation, 4Q to 4Q	1.8	2.0	2.0	2.0

Source: Bloomberg, FactSet, Federal Reserve, J.P. Morgan Asset Management.
Market expectations are the federal funds rates priced into the fed futures market as of the date of the March 2019 FOMC meeting and are through December 2021. *Long-run projections are the rates of growth, unemployment and inflation to which a policymaker expects the economy to converge over the next five to six years in absence of further shocks and under appropriate monetary policy.
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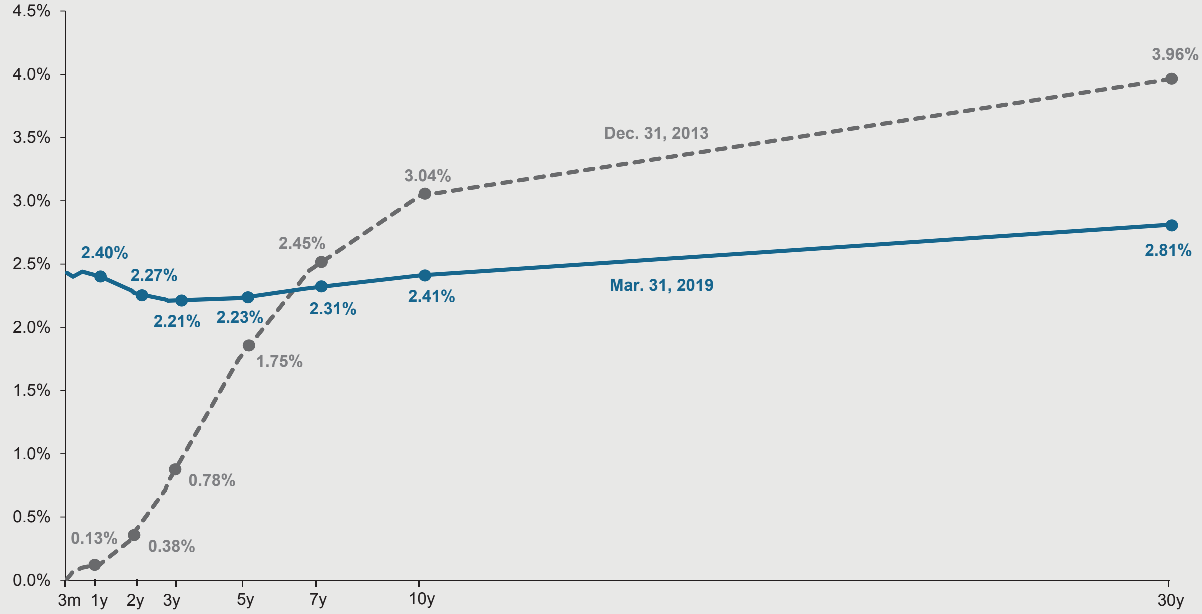
Fixed income

Yield curve

Yield curve

U.S. Treasury yield curve



Source: FactSet, Federal Reserve, J.P. Morgan Asset Management.
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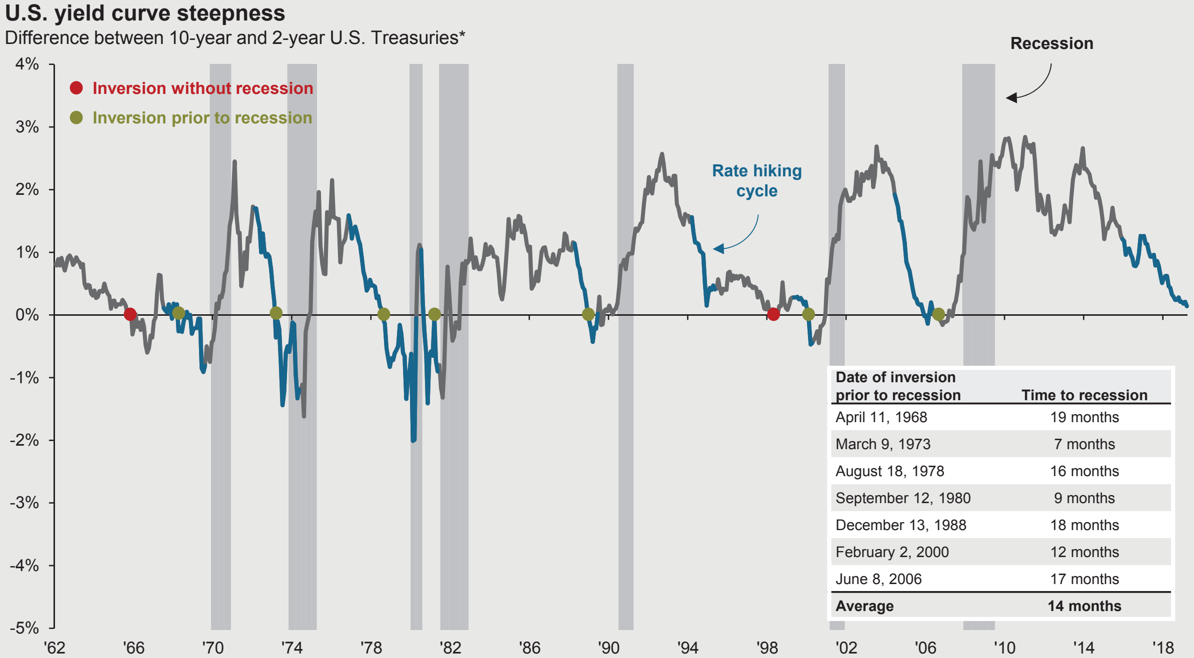
Fixed income

U.S. yield curve inversion and recessions

U.S. yield curve steepness

Difference between 10-year and 2-year U.S. Treasuries*



Date of inversion prior to recession	Time to recession
April 11, 1968	19 months
March 9, 1973	7 months
August 18, 1978	16 months
September 12, 1980	9 months
December 13, 1988	18 months
February 2, 2000	12 months
June 8, 2006	17 months
Average	**14 months**

Source: FactSet, Federal Reserve, J.P. Morgan Asset Management. *From January 1962 to May 1976, short-term bond is U.S. 1-year note, and from June 1976 onwards the short-term bond is the 2-year note due to lack of data availability. Time to recession is calculated as the time between the final sustained inversion of the yield curve prior to recession and the onset of recession.
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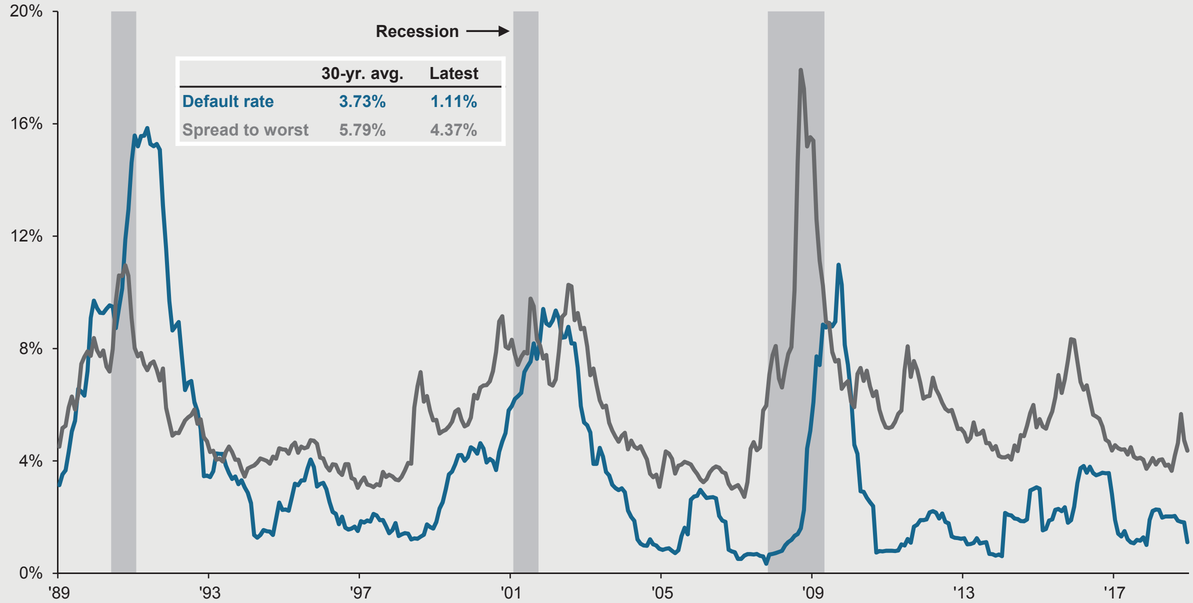
Fixed income

High yield bonds

Default rate and spread to worst

Percent



	30-yr. avg.	Latest
Default rate	3.73%	1.11%
Spread to worst	5.79%	4.37%

Source: J.P. Morgan Global Economic Research, J.P. Morgan Asset Management.
Default rates are defined as the par value percentage of the total market trading at or below 50% of par value and include any Chapter 11 filing, prepackaged filing or missed interest payments. Spread to worst indicated are the difference between the yield-to-worst of a bond and yield-to-worst of a U.S. Treasury security with a similar duration. High yield is represented by the J.P. Morgan Domestic High Yield Index.
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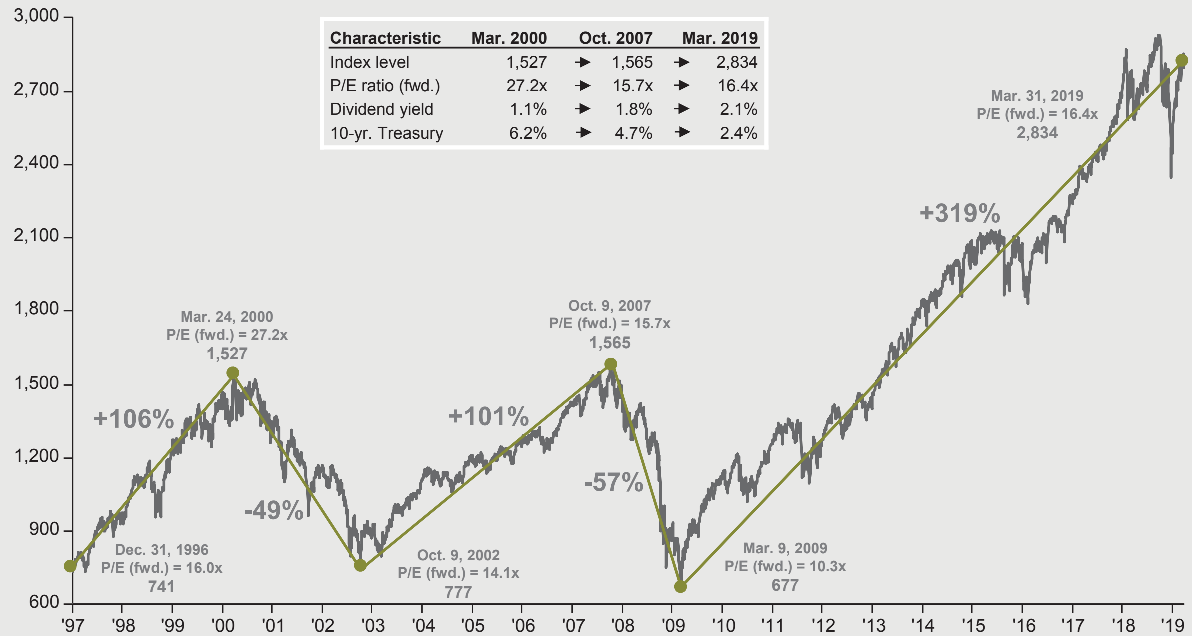
Equities

S&P 500 Index at inflection points

S&P 500 Price Index



Characteristic	Mar. 2000		Oct. 2007		Mar. 2019
Index level	1,527	➔	1,565	➔	2,834
P/E ratio (fwd.)	27.2x	➔	15.7x	➔	16.4x
Dividend yield	1.1%	➔	1.8%	➔	2.1%
10-yr. Treasury	6.2%	➔	4.7%	➔	2.4%

Source: Compustat, FactSet, Federal Reserve, Standard & Poor's, J.P. Morgan Asset Management.
Dividend yield is calculated as consensus estimates of dividends for the next 12 months, divided by most recent price, as provided by Compustat. Forward price to earnings ratio is a bottom-up calculation based on the most recent S&P 500 Index price, divided by consensus estimates for earnings in the next 12 months (NTM), and is provided by FactSet Market Aggregates. Returns are cumulative and based on S&P 500 Index price movement only, and do not include the reinvestment of dividends. Past performance is not indicative of future returns.
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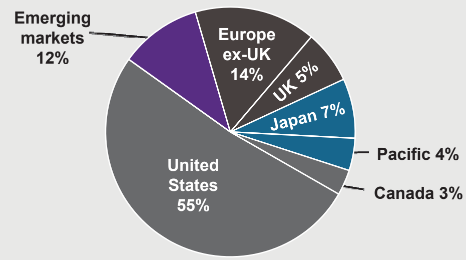
Global equity markets

International

Returns	2019 YTD		2018		15-years	
	Local	USD	Local	USD	Ann.	Beta
Regions						
U.S. (S&P 500)	-	13.6	-	-4.4	7.8	0.86
AC World ex-U.S.	10.7	10.4	-10.2	-13.8	5.7	1.11
EAFE	10.7	10.1	-10.5	-13.4	5.2	1.07
Europe ex-UK	12.6	10.7	-10.6	-14.4	5.7	1.22
Emerging markets	9.9	10.0	-9.7	-14.2	8.3	1.28
Selected Countries						
United Kingdom	9.4	11.9	-8.8	-14.1	4.1	1.01
France	12.8	10.8	-7.5	-11.9	5.4	1.23
Germany	8.9	7.0	-17.7	-21.6	6.1	1.34
Japan	7.8	6.8	-14.9	-12.6	4.0	0.76
China	17.9	17.7	-18.6	-18.7	9.9	1.25
India	6.3	7.2	1.4	-7.3	10.0	1.37
Brazil	8.7	8.2	16.7	-0.1	10.0	1.51
Russia	7.1	12.2	18.1	0.5	4.8	1.54

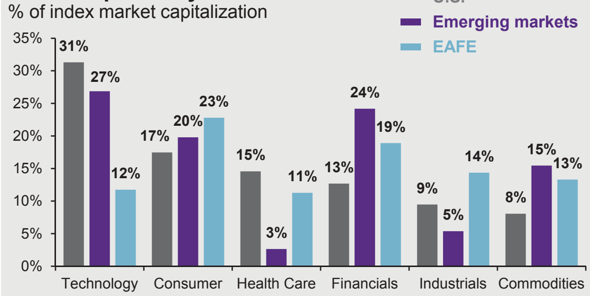
Weights in MSCI All Country World Index

% global market capitalization, float adjusted



Global equities by sector

% of index market capitalization



Source: FactSet, Federal Reserve, MSCI, Standard & Poor's, J.P. Morgan Asset Management.
All return values are MSCI Gross Index (official) data. 15-year history based on U.S. dollar returns. 15-year return and beta figures are calculated for the time period 12/31/03-12/31/18. Beta is for monthly returns relative to the MSCI AC World Index. Annualized volatility is calculated as the standard deviation of quarterly returns multiplied by the square root of 4. Chart is for illustrative purposes only. Please see disclosure page for index definitions. Past performance is not a reliable indicator of current and future results. Sector breakdown includes the following aggregates: Technology (communication services and technology), consumer (consumer discretionary and staples) and commodities (energy and materials). The graph excludes the utilities and real estate sectors for illustrative purposes.
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