Quarterly Newsletter

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DELTA FINANCIAL ADVISORS
Investment Counsel

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2018 Wrap Up

The year's end made many feel that they were back in the dark days of 2008, as financial markets saw their greatest sustained volatility since the Financial Crisis. After modestly recovering in November from September's 7% decline, investors went into full "risk off" mode in December as they pushed the S&P 500 down by more than 9%, and on an intra-day basis, briefly had the market enter into bear territory. After the roller coaster fourth quarter, the broader market closed out 2018 with an almost 4.4% decline. Adding fuel to investors' increasingly jittery nerves was the Federal Reserve, albeit as expected, raising overnight interest rates at its mid-December meeting to 2.5%.

A prime precipitant of the market's recent volatility has been the worsening trade war with China. After starting out relatively small and targeted last January, the battle escalated with new tariffs placed on $200 billion of Chinese goods in late September with Administration threats of tariffs on an additional $250+ billion of Chinese goods in the event of a Chinese retaliation.

Domestic jitters were further raised as the Administration commenced its 3rd partial shutdown of the year on December 22 over demands that Congress provide funding for the U.S.-Mexico border barrier. With the U.S. House of Representatives now controlled by the opposition Democrats, the likelihood of compromise appears increasingly remote. The federal government has been partially shutdown for more than 3 weeks, with no potential resolution in sight.

The modest offset to the market's year-end gloom and doom was December's remarkably robust jobs report with 312,000 new positions being created – sharply stronger than the 177,000 jobs anticipated. Potential job seekers re-started searches in the face of this good news causing unemployment to rise from 3.7% to 3.9% to close out the year. While the U.S.'s 9+ year expansion has lost its early shine, and notwithstanding more recent challenges, there is still some pep left in America's economic engine.

	Close	Month	YTD	1 Year
DJIA	23,327.46	-8.59%	-3.48%	-3.48%
S & P 500	2,506.85	-9.03%	-4.38%	-4.38%
NASDAQ Comp.	6,635.28	-9.48%	-3.88%	-3.88%

	Quarter end yield	Prior Year end yield	Yield 1 year ago
10 yr. U.S. Treasury	2.69%	2.40%	2.40%

Looking Ahead

Four key factors are likely to shape the U.S. market and American economy in coming months - the first being rising interest rates and expectations of rising interest rates. While U.S. rates still remain at historically lower levels, 10-year U.S. Treasury rates, at around 2.72%, are sharply above their record lows of 1.36% of mid-2016. In the face of slowing global growth, expectations for rate increases by the U.S.'s Federal Reserve have diminished with only 1 or 2 rate hikes now expected in calendar 2019. Moreover, in early January, Fed Chair Powell's tone sharply changed. Faced with a series of jaw dropping market swings, combined with some hints that a broader economic slowdown could be arriving, Mr. Powell appears to be rethinking his economic position. At a panel discussion at the American Economic Association, his position became sharply more open with an emphasis on flexibility, adaptability and open-mindedness.

President Trump's unpredictability will remain a big factor. Whether in de-escalating the worsening U.S./China trade war, or re-opening the federal government from its partial shutdown, the Administration's fickleness will keep both markets and foreign leaders guessing as to the president's next step(s). With financial markets finding comfort in predictability, the Administration's ongoing impulsiveness could well result in sustained market volatility.

Slowing global growth is also likely to be a key element. Already facing headwinds associated with rising global interest rates, the recent U.S/China and U.S./European trade battles have created new difficulties. When coupled with increasingly tepid growth from China, and despite substantial Chinese central government support, global growth in 2019 is unlikely to match its recent strength.

Finally, a great deal of economic and market strength has been generated by tech companies over the last 5-10 years. Investors fell in love with these transformative enterprises until the relationship sharply cooled in 2018's second half. Some of the larger firms have their own operational issues.....whether it is Apple with its enormous Chinese operations alongside a vital, but slowing, Chinese consumer or Facebook as it struggles to re-achieve consumer confidence while investing huge sums to protect its network from outside interference. In any scenario, a crushing of this long-time relationship, or conversely a renewal of this love affair, could have broad reaching effects. Although we expect markets to remain volatile, we do not currently forecast a recession in 2019, unless created by bad policy. We feel that the recent market weakness, without an impending recession, will make way for better news for investors in the coming year.

701 Poydras Street
Suite 350
New Orleans, LA 70139

www.deltafinad.com

Office 504-522-9019
Fax 504-522-9676
Toll Free 888-522-9019