MarketWatch

MARINE BANK
Trust & Investment Management

Conference Call Summary

Joe Terril, Terril & Company, Featured Speaker

Quite a bit has happened since our September and October **Market**Watch calls. Going into Fall of 2018, the markets were facing prospects of rising interest rates, the potential for a trade war, election concerns and a ballooning budget deficit. After ignoring the issues for most of 2018, the markets finally gave way as people began to worry about them. The result, in my opinion, is based on incorrect assumptions.

The number one issue that everyone around the world is now concerned with is the potential trade war between the United States and China. People are jumping to the conclusion that nothing will be resolved and, therefore; the world is going into a severe recession. I vehemently disagree with this conclusion. While there is no way to know whether the United States and China are going to come to some agreement, it is unlikely that China and the United States will jointly commit economic suicide over this issue. We will know more in early December when the president of China meets with President Trump, but I think it is wrong to assume that if they do not agree the world will automatically fall into a severe recession.

The second pillar of what is worrying people concerning the world economy is the interest rate question. Interest rates in the United States which are established by the Federal Reserve Bank on the short end of the market, are 2%. It is not going to kill the world economy if the Fed continues to raise that rate to 2.25% or 2.50%. As a natural result of rising interest rates, mortgage rates are higher, and the housing market is slowing down. However, markets are jumping to the conclusion that housing in the United States is going to fall apart now that interest rates on mortgages are 1.5% higher. It is important to remember that, at the same time, American workers are making more money now than ever before. Husband and wife are both working, getting pay raises, feeling secure in their jobs and paying lower taxes. While their mortgage payments on a new house might be increasing by $200 a month, they are not going to avoid buying the bigger home that they need because their income is up almost $400 or $500 per month.

Additionally, there is a shortage of housing in the United States. It has been ten years since the necessary number of housing units in the country has been built every year to replace depreciation and destruction due to fire and storms, etc. As a result, people look at the number of houses being sold and panic, but part of the issue is that the number of houses on the market is less than four months of inventory. In general, I think the world economy is doing fine right now, and much of people's concern is based on incorrect assumptions.

There have been several corrections in the markets, particularly in stock prices. Bonds are down 4% to 5% on the year. Equities are down sharply, particularly in the S&P 500. Approximately 45% of all the stocks in the S&P 500 are now down 20% to 25%. Value stocks (i.e., companies that are generating cash flow, buying back their stock and raising dividends) have done nothing for the past 18 months and have even gone lower. The value companies are very reasonably priced and are good investments right now. For at least the last year, I have said that the rally in the FAANG stocks (i.e., Facebook, Amazon, Apple, Netflix and Google) was way overdone and made no sense. Yet all year long, people have been buying growth at any price and ignoring value stocks. People are finally beginning to move away from that philosophy and realizing the stocks are not worth an infinite price simply because they have some growth characteristics.

In general, 2018 has not been a good year for investments. Every asset category is down this year. There is not one major stock market index that is still in the positive and some are down 15% or more. Fixed income is down 5%. High yield fixed income is down even more. However, that does not mean this scenario will go on forever. I am actually fairly optimistic about some of our holdings because they are so reasonably priced right now. As we head into the end of the year, I am optimistic about what will happen in 2019.

Year to Date Returns		
INDEX	Returns	Returns w/ Dividends
Bloomberg Barclays US Agg Bond Index	-4.3172%	-2.0717%
Dow Jones Industrial	-1.0258%	1.0085%
S&P 500	-1.1864%	0.5974%
NASDAQ Composite	0.0787%	1.1391%
Dow Transport	-3.7631%	-2.4766%
Dow Utilities	0.5917%	3.6073%
Russell 2000	-4.3309%	-3.2021%
KBW Bank Index	-7.5711%	-5.5800%
XLE, Energy Sector ETF	-10.1000%	-8.0050%
MSCI World ex USA	-13.6171%	-10.7800%
S&P/TSX Composite (Canada)	-8.2184%	-5.6969%
MEXBOL (Mexico)	-15.3118%	-13.5100%
IBOV (Brazil)	15.0500%	15.0500%
IPSA (Chile)	-8.3429%	-8.3429%
COLCAP (Columbia)	-8.2192%	-5.8123%
MERVAL (Argentina)	-0.8669%	-0.8669%
SPBLPGPT (Peru)	-3.9960%	-3.9960%
Euro Stoxx 50 (Europe)	-11.5835%	-8.2741%
FTSE100 (UK)	-8.8544%	-4.9900%
CAC40 (France)	-7.7636%	-4.7800%
DAX (Germany)	-14.7400%	-14.7400%
Nikkei (Japan)	-5.2700%	-3.4745%
Hang Seng (Hong Kong)	-13.6328%	-10.2152%
CSI300 (Shanghai Shenzhen, China)	-20.1557%	-18.1564%
AS51 (Australia)	-6.4853%	-1.0485%

*Return values from Bloomberg Terminal. Year to date as of November 20, 2018

	Portfolio Allocations					
Portfolios	Fixed Income	Equities		International	Total Portfolio Return	Total Portfolio Return w/ Dividends
		S&P500	NASDAQ			
Conservative	75%	25%			-3.5345%	-1.4044%
Moderate Growth	60%	40%			-3.0649%	-1.0041%
Growth	50%	25%	15%	10%	-3.8051%	-1.7936%
Aggressive	30%	30%	25%	15%	-3.6740%	-1.7745%

*Indices used to calculate the actual portfolio returns. Values as of YTD November 20, 2018. Fixed Income - Bloomberg Barclays US Aggregate Bond Index, Equities: S&P 500 and NASDAQ Composite, International - MSCI World ex USA.

ClientQuestions

Why is there so much volatility in the markets?

Response: It is a combination of reasons. First, in the last three years, there has been a big movement towards computer trading. The computer trades based upon algorithms without any knowledge of the fundamentals. Part of the reason for the volatility is the number of people who have taken the human element out and are having computers make their trade decisions.

The second reason for recent volatility is due to a liquidity situation. Those five FAANG stocks made up about 75% of the S&P 500's move all year long. As those stocks have begun to come down and are facing liquidations, investors are not only selling those stocks, but others as well in order to give people their money back. This results in volatility where people are questioning why investors would be selling reasonably priced stocks that are good investments at current prices. They are not selling because they think fundamentals have deteriorated but because they need to give people their money in liquidations.

Although computer trading and liquidity issues create tremendous volatility, there is opportunity within that volatility. Opportunities exist for investors that are still looking at the fundamentals of the companies, like how much cash they are generating, what they are doing with the cash, how much of it is a free cash flow, etc. It is incredible in the last ten years how much stock is now retired due to companies buying their own stock. For example, in the last ten years, Walmart has retired 40% of its outstanding stock. This trend is why investments in companies that are value stocks that generate a lot of cash and have a lot of free cash flow are going to result in good investment returns. As they buy back more and more stock, ultimately the price is going to go higher.

Why have our energy infrastructure trusts been going down in price and why is the price of oil going down?

Response: This is so frustrating to me because the fundamentals of the industry itself (i.e. the pipeline companies that have storage tanks and transport oil, natural gas and gasoline around the country for the producers) are excellent. In the last five years they have retired debt and have paid for all of their capital expenditures out of cash flow. While cash flow and distributions have increased, the price of stocks are down, partly due to the belief that we are preparing for a worldwide recession. People are jumping to the conclusion that energy prices are going to collapse and therefore oil will not be produced to send through the pipelines. Again, I disagree. In fact, the fundamentals of these companies are improving by the day. We hold a big position in Plains Petroleum, who just 30 days ago increased their cash flow position for 2018 and increased their cash flow estimates for 2019. They have paid down debt and are planning on raising the cash distributions to shareholders from the first quarter of next year with all the cash they are generating. Yet, stocks are way down on this morbid fear that energy prices are going to collapse. Year-to-date in 2018, this will be the 3rd year in a row that China, US, India and Brazil, have all four set records for usages of energy. The price of oil is down for no other reason than people who are panicking that the price is going to collapse and are selling oil at any cost. I completely disagree and think the fundamentals of the companies are better than ever. In fact, I am assessing at what price I would want to buy some more of the energy infrastructure trusts and where I have room to buy more. The dividend yields alone on them are more than 9% and in many cases tax deferred.

If the economy is going down, does this mean interest rates are going higher?

Response: Interest rates have begun to move higher in the United States. This increase in interest rates is not consistent with the rest of the world, like Japan and Europe. In the United States, ten-year government bonds got as high as 3.25% and short term interest rates at 2%. The expectation is the United States will continue to gradually increase interest rates until they are more in line with the rate of inflation in the United States, which is 3%, and the rate of growth of the economy which is about 3.5 to 3.75%. Interest rates at 2% when an economy is growing at 3.75% is not being tight. I still believe interest rates will gradually move higher in the United States and that interest rates at current levels are not going to kill the United States economy. What is happening at the moment is that participants all over the world are thinking that the world economy is going to fall apart and, therefore, interest rates cannot and will not go up. The speculation is that the Federal Reserve in the United States will

ClientQuestions *(continued)*

probably do another quarter percent increase in December which will bring us up to 2.25% and then maybe will hold off in 2019 over people's fears that the world economy might be falling apart. I think the rise in interest rates may be briefly interrupted, but ultimately, interest rates will come in line with rate of inflation and growth of economy.

Two other things that are affecting both bond and stock markets are the "General Electric" effect and the Brexit argument. For the last ten years, General Electric has been a terribly managed company and consequently is doing very poorly right now. Because it is such an iconic name, investors are worried that if General Electric could go broke, then other companies could have similar problems. The other issue is the Brexit argument between England and the European Union about how best to separate. The European Union wants a certain number of billions of British pounds from England in order to let them out of the European Union. The British government does want to pay. People are leaping to the conclusion that this somehow will wreck the European economy and England's economy. This is based not on reality but more on fear.

Marine Bank Trust and Investment Management

Holiday Seminar

Market Forecast 2019
featuring Joe Terril

Join Us!

Thursday, December 6 – Panther Creek Country Club
5:30 Cocktails and Hors d'oeuvres
6:30 Forecast with Joe Terril

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MarketWatch

Monthly conference calls with time for your questions about the state of the markets are just one of the many personalized services offered by Marine Bank's Investment Management Team. This **Market**Watch update is a summary of our monthly call.

Our next monthly conference call will be:
January 16th 2019
at **10:30 a.m.**

To participate, dial
1.866.210.1669

When prompted, enter code **8558354#**

Email your questions to Annette in advance:
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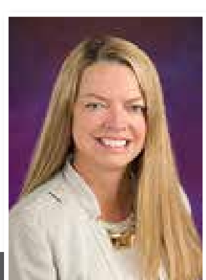

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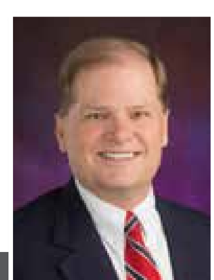

John "Joe" Terril
President of Terril & Company, a St. Louis based, independent wealth management firm. Terril & Company has been overseeing retirement plans, IRAs and individual investment portfolios for over 37 years, an important keystone of Terril & Company's philosophy remains ensuring no conflicts of interest exist between the company and its clients.