

Economic & Market Commentary

Market Update – December 2018

Through December and much of the fourth quarter of 2018 investors had to contend with rising interest rates in the U.S., a sharp slowdown in Eurozone business confidence, weaker Chinese growth and rising trade war concerns. As a result, stocks were hit hard in the month of December, posting their worst monthly losses in years. However, despite the volatile stock market in 2018, strong economic fundamentals were present.

Economy

- Consumer confidence tapered in December but remains near all-time highs.
- Fed Chairman, Jerome Powell, has expressed optimism in the U.S. economy. Powell recently said the central bank will be patient in its approach to monetary policy.

Stocks

- The S&P 500 fell 9.0% in December. This was its worst month since the great financial crisis of 2007-2008.
- U.S. small (-11.9%) and small value (-11.7%) struggled as financial markets flirted with bear market territory.
- International stocks outperformed U.S. stocks in December. International large stocks (-4.9%), international small stocks (-6.6%), and emerging markets (-2.7%) posted smaller losses.

Bonds

- Bond returns were positive in December, with international (hedged) bonds leading the way, up 1.5%.
- Year-to-date, short-term (+1.5%) and international bonds (+3.6%) were the leaders, while inflation bonds were down slightly.
- Intermediate bonds were up 1.3% in December and 0.9% in 2018.

Alternatives

- Alternative asset classes were a mixed bag in December (REITs -5.7%, commodities -6.9%, managed futures +6.0%, and reinsurance -0.6%).

2018 Review: Exceptional Yet Volatile

Looking back at the start of 2018, analysts feared the economic expansion was nearing its end. It was common to hear the expansion was running on borrowed time as the economy grew closer to its longest expansion in history. However, the top of the business cycle proved these misnomers to be just that, misnomers. A tightening labor market, worries of inflation, and geopolitical risks all threatened in 2018. However, the economy ended the year in an exceptional state.

Unemployment remained near all-time lows pushing into territory not seen since the 1960s. Wages finally began to lift, reaching a 3.2% annualized growth rate.

Most surprisingly, fears of an overheated economy fizzled as inflation remained tamed in large part to the Fed raising interest rates. Many analysts questioned whether enacting tax cuts so close to the peak of the business cycle was a fiscally responsible move. Despite the speculation, lower tax burdens have not led to substantially higher prices as the Fed continues to monitor inflation closely.

The U.S. economy continued to expand, with real GDP growing 3.4% over the last year (as of 9/30/2018). Despite rising interest rates, businesses have continued to invest in new equipment and facilities. Tax relief coupled with steady consumer spending allowed the nation's growth rate to accelerate in 2018.

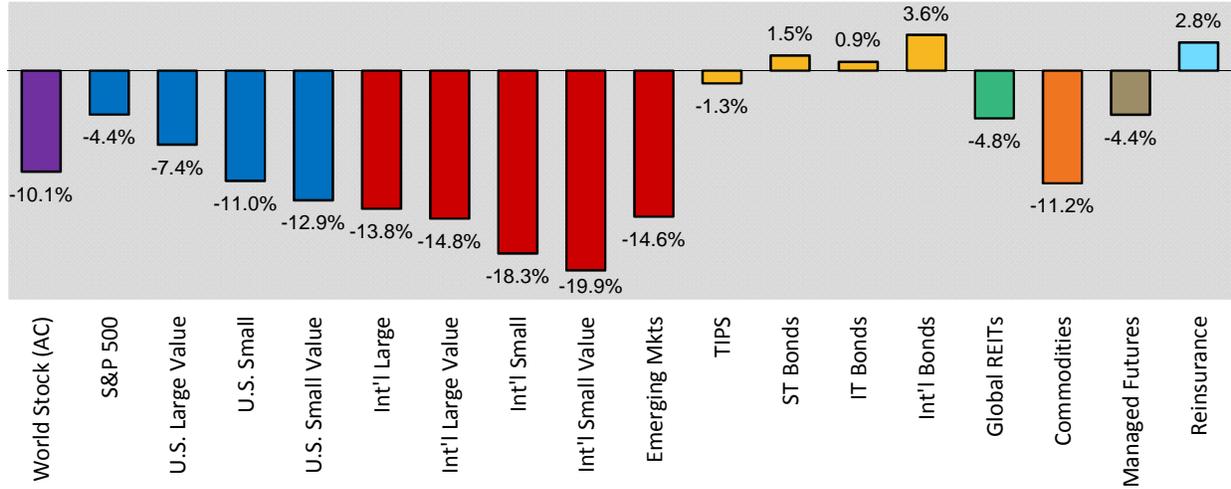
Despite exceptional fundamentals, financial markets saw more volatility in 2018 with two pullbacks greater than 10%. It's important to remember that sticking to your investment plan is critical during volatile markets. We believe investors should not rely on emotions, and should ignore short-term trends and hot tips during volatile markets. Successful long-term investing requires maintaining a comprehensive and strategic investment plan. For more information on how to implement this type of plan contact our office today.

Sources: Bureau of Economic Analysis (BEA), Federal Reserve, Morningstar Direct, Standard and Poor's, MSCI, Wall Street Journal, JPMorgan Chase.

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MARKET RETURNS
Year-To-Date as of 12/31/2018



MARKET RETURNS - Longer Term Annualized as of 12/31/2018

	1 Month	YTD	1 Year	3 Years	5 Years	10 Years	15 Years
STOCKS							
S&P 500	-9.0%	-4.4%	-4.4%	9.3%	8.5%	13.1%	7.8%
U.S. Large Value	-9.4%	-7.4%	-7.4%	8.0%	6.8%	11.4%	7.2%
U.S. Small	-11.9%	-11.0%	-11.0%	7.4%	4.4%	12.0%	7.5%
U.S. Small Value	-11.7%	-12.9%	-12.9%	6.7%	4.3%	11.9%	7.7%
Int'l Large	-4.9%	-13.8%	-13.8%	2.9%	0.5%	6.3%	4.7%
Int'l Large Value	-4.9%	-14.8%	-14.8%	2.8%	-0.6%	5.5%	4.2%
Int'l Small	-6.6%	-18.3%	-18.3%	3.7%	3.3%	10.2%	7.7%
Int'l Small Value	-6.2%	-19.9%	-19.9%	3.4%	2.8%	9.8%	8.0%
Emerging Mkts	-2.7%	-14.6%	-14.6%	9.2%	1.6%	8.0%	7.9%
World Stock (AC)	-7.2%	-10.1%	-10.1%	6.5%	4.2%	9.7%	6.4%
BONDS							
TIPS	0.5%	-1.3%	-1.3%	2.1%	1.7%	3.6%	3.8%
Short-Term Bonds	0.3%	1.5%	1.5%	0.8%	0.4%	0.4%	1.4%
Interm-Term Bonds	1.3%	0.9%	0.9%	1.7%	1.9%	2.9%	3.3%
International Bonds	1.5%	3.6%	3.6%	3.7%	4.5%	3.9%	4.4%
ALTERNATIVES							
Global REITs	-5.7%	-4.8%	-4.8%	3.4%	6.4%	11.3%	7.4%
Commodities	-6.9%	-11.2%	-11.3%	0.3%	-8.8%	-3.8%	-2.5%
Managed Futures	6.0%	-4.4%	-4.4%	-0.9%	3.1%	1.5%	4.9%
Reinsurance	-0.6%	2.8%	2.8%	3.3%	4.0%	6.9%	7.1%

Source: Morningstar Direct. Indices used in above graphs: S&P 500 Index, U.S. Large Value-MSCI U.S. Prime Market Value Index, U.S. Small-Russell 2000 Index, U.S. Small Value-MSCI U.S. Small Value Index, Int'l Large-MSCI EAFE Index, Int'l Large Value-MSCI EAFE Value Index, Int'l Small-S&P EPAC Small Index, Int'l Small Value-S&P EPAC Small Value Index, Emerging Mkts-MSCI Emerging Markets Index, World Stock Index-MSCI All Country World IMI Index, TIPS-Barclays Gbl Infl Linked US TIPS Index, Short-Term Bonds-Ibbotson 1 Yr Treasury Const Mtg Index, Interm-Term Bonds-Barclays Interm-Term Govt/Credit Index, International Bonds-JPM GBI Global Ex US Hdq, Global REITs-S&P Global REIT Index, Commodities-Bloomberg Commodity Index, Managed Futures-Credit Suisse Mgd Futures Liquid Index, Reinsurance-SwissRe Global Cat Bond Index.

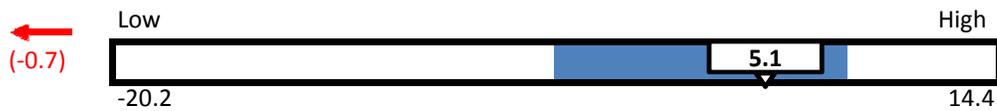
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Economic Indicators

Leading Economic Index Year over Year Change (%)



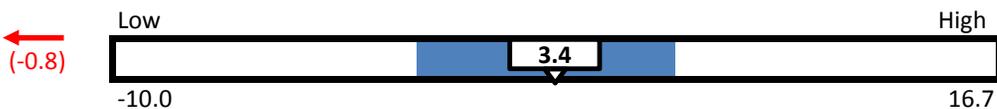
Unemployment (%)



Inflation CPI (YOY %)



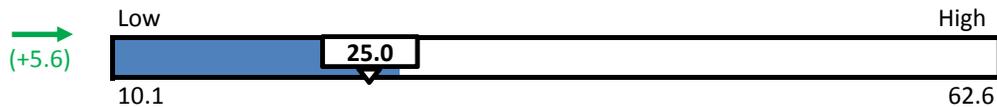
Real GDP Growth (%)



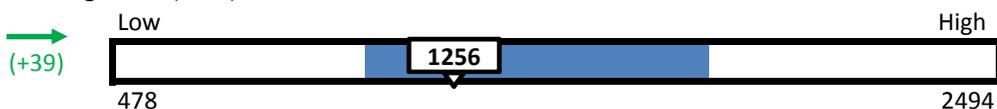
Consumer Confidence



VIX - Market Volatility



Housing Starts (000s)



10-year Treasury Yield (%)



 Typical range (within 1 standard deviation of the median)

 Current Value

 Historical Range

 Change in value since last month

**See appendix for sources and data ranges*

Appendix

Leading Economic Index Year over Year Change (%)

The Leading Economic Index is composed of 10 indicators used to forecast the direction of the economy. A fall in the index over three consecutive months is seen as a sign of a recession. The value shown represents the 12-month change in the index level. *(Data Source: The Conference Board. Monthly data since 1/1/1959)*

Unemployment

The unemployment rate measures the percentage of workers that are out of work in the U.S. labor force. *(Data Source: U.S. Bureau of Labor Statistics. Monthly data since 1/1/1948)*

Inflation CPI (YOY)

The Consumer Price Index (CPI) measures the change in the price level for a broad basket of goods in the U.S. economy. The value shown represents the percent change in the index from a year ago. *(Data Source: U.S. Bureau of Labor Statistics. Monthly data since 1/1/1948)*

Real GDP Growth

Real GDP Growth represents the change in the market value of all output in the U.S. economy. It is an annualized quarterly measure. *(Data Source: U.S. Bureau of Economic Analysis. Quarterly data since 4/1/1947)*

Consumer Confidence

The Consumer Confidence Index measures the level of optimism among U.S. consumers on the economy and their overall financial situation. *(Data Source: The Conference Board. Monthly data since 1/31/1991)*

VIX

The CBOE Volatility Index (VIX) measures the volatility of the S&P 500 index. An increase in the index level represents a spike in market volatility. Conversely, a decrease in the index represents a move towards stability. *(Data Source: Chicago Board Options Exchange. Daily data since 1/2/1990)*

Housing Starts

The number of housing starts (new construction) in the U.S. each year. *(Data Source: U.S. Bureau of the Census. Monthly data since 1/1/1959)*

10-year Treasury

The annualized return that would be realized for holding a 10-year Treasury bond to maturity. The 10-year Treasury yield is the primary benchmark for measuring interest rate movements. *(Data Source: U.S. Board of Governors of the Federal Reserve System. Daily data since 1/2/1962)*

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