QUARTERLY MARKET OUTLOOK: FOURTH QUARTER 2018

Third Quarter in Review

U.S. large-cap stocks outperformed most other asset classes in the third quarter and over the past year. More generally, equity investments performed better than fixed income, as the chart shows, and in line with the usual trade-off between risk and return. As a result, portfolios that included bonds as well as stocks didn’t gain as much as the S&P 500 because they are designed to be less risky and less volatile over time. In addition, international equity investments underperformed the S&P 500 due partly to the stronger dollar and slower-than-expected economic growth in the rest of the world.

Global bull market continues – The outlook for solid U.S. economic growth and strong earnings growth supports rising stock prices over time. And while not as strong, the international equity outlook is also positive, with more attractive equity valuations. In early September, emerging-market stocks were down 20% from their January 2018 high, dipping into bear market territory. Despite the potential disruptions from slower trade and higher tariffs, we think the underlying fundamentals will keep the global bull market on track.

Supportive monetary policy – Inflation has remained near the Federal Reserve’s 2% target, allowing it to continue to increase short-term interest rates slowly and keep U.S. monetary policy accommodative rather than restrictive. In addition, foreign central banks continue to provide stimulus. Supportive monetary policies can help extend the market and economic cycle.

Still-high market volatility – Although daily stock market moves calmed compared to early in the year, volatility has remained high in currencies and commodities, as well as across market sectors. We expect volatility to continue as the Fed continues to raise short-term interest rates, earnings growth slows below 20% and the ongoing impacts of higher tariffs and higher oil prices are felt.

Action for Investors

Set realistic expectations for your investment portfolio’s returns, realizing that well-diversified portfolios aren’t designed to outperform the S&P 500. After several years of above-average performance, we expect lower returns over the next decade. If you haven’t rebalanced recently, you may need to return to the right mix of equities and fixed income for your situation and risk tolerance, with a wide variety of asset classes in each to help improve portfolio resilience and performance over time.

Diversification does not ensure a profit or protect against loss in a declining market.

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