American National Bank & Trust™

TRUST AND INVESTMENT SERVICES

Third Quarter 2018 Review

Although 2018 started a bit rough, the market has generally moved higher since the end of the 1st quarter. The S&P 500 has had a total return of 10.56% through the end of the 3rd quarter. The first few days of October have brought greater volatility as interest rates have increased. Judge Kavanaugh's confirmation has highlighted the country's ideology split right down the middle and midterm elections are just around the corner. To be sure November is going to be very interesting.

While we have been concerned about elevated valuations for much of the year, we remained bullish, as there were few reasons to reverse course. Do not be mistaken, we have had many reasons to be concerned this year. North Korea remains a mystery, Congress, (especially the US Senate of late) has showed us how the sausage is made in Washington, DC, and still no one has been able to lock down President Trump's Twitter account. Fortunately, the yield curve remains positive, corporate profits continue to improve and trade agreements are being renegotiated. We did well to follow the trend, lean into our equity allocations, and ignore our nagging doubts. Growth has led value for some time.

Notwithstanding the recent sell off of stocks the first week of October and the rise in interest rates, there is no reason not to see this upward trend continuing into the 4th quarter of 2018. All of the economic indicators are flashing green. GDP, industrial production, and housing are expected to be higher than they have been in years. The unemployment rate is at levels not seen since the Nixon Administration at 3.7%. Rising investment, productivity and valuation multiples have been largely ignored and underappreciated by many of the market pundits. The only thing giving the market pause presently is the recent increase in interest rates and the threat of higher inflation. Just this week the 10-year yield has increased from 3.05% to 3.23%, which is the highest rate since 2010.

As we stated before, we continue to believe that many investors and analysts have not fully comprehended H.R. 1, better known as the *Tax Cuts and Jobs Act,* which was signed into law on December 22, 2017, and went into effect January 1, 2018. While much has been written about individual taxpayers and the benefits they will receive depending where they live, the most significant impact will be on corporations. Warren Buffett described it best when he was interviewed on Squawk Box January 10 and said the following;

> *"You had this major change in the silent stock holder in American business who has been content with 35 percent ... and now instead of getting 35 percent interest in the earnings they get 21 percent and that makes the remaining stock more valuable."*

We think the market has failed to appreciate this gift from Congress and President Trump. We expect the markets to continue to improve as this change becomes more apparent, notwithstanding rising interest rates. We do expect the midterm elections to cause some heartburn for the markets in the next few weeks. Midterm elections are normally positive for the equity market in the long run but can cause volatility in the short run. We will continue to lean into equities until the momentum really turns down in this market.

Thank you for the confidence you place with us as your financial partner. We appreciate the opportunity to serve you!