April 10, 2019

"Life is a long lesson in humility"
-J.M. Barrie

Whiplash. This is exactly what investors who panicked during the fourth quarter and sold stocks experienced when the market rebounded in the first quarter. The S&P 500 peaked in September at 2,940.91 and fell 20.2% to a low of 2,346.58 on December 26. Since then the market has recovered and is back near its high. As stocks declined the media presented a continuous stream of strategists explaining why the next bear market was upon us. Not one of them has a consistent record of predicting market declines or rallies. Over our years of investing we've learned making market calls is a sure path to looking foolish. Instead, we focus on identifying solid businesses that can weather the ever-changing market conditions. In this quarterly update we'll highlight some key factors that contributed to the challenging environment in the last two quarters and provide some insight on our thinking for the remainder of the year.

We believe the global trade war has been the most significant factor behind the decelerating economy and corresponding market swoon in the fourth quarter. The threat of tariffs, which disrupt global supply chains, was occurring at the same time corporate managements were budgeting for the new year. The Institute for Supply Management (ISM) Manufacturer's Index, which is a leading indicator of manufacturing activity, declined from 61.3 in August to 54.1 in December. The softening in the ISM correlated with deteriorating trade talks between the US and China, the two largest global economies. More recently, the ISM has rebounded to 55.3, coinciding with the improving tone of the tariff talks with China. We expect an agreement to be reached between the US and China as a trade war is in neither nation's best interest.

The Federal Reserve, which had been slowly raising interest rates, reacted to the weakening economic data by pausing rate hikes. As a result, the yield curve has flattened and the 10-year treasury yield has fallen from 3.1% in September to 2.5% now. We believe the Fed has done an excellent job fulfilling its dual mandate of low inflation and full employment. Unemployment is at 3.8%, a historically low figure, and core inflation remains subdued at 2.0%.

Brexit is still an unknown and the UK parliament is struggling to agree on a path to leave the EU partnership. Interestingly, Europe is the main source of global weakness and we suspect the uncertainty surrounding trade between the UK and its EU partners is a contributing factor. Economic activity in the European Union, outside of Germany, has been subdued for years and any resolution to trade issues would be good for the economy.

Looking forward, corporate earnings in 2019 are estimated to expand 10% after growing 23% in 2018, a year in which the corporate tax cut had a one-time favorable impact on results. The market multiple of 17x is lower than it was at the beginning of 2018 and appears reasonable assuming the economy continues to expand. In the first quarter, S&P 500 earnings are projected to be flat to slightly lower, but we believe this reflects the lingering impact of the tariff battle. Results later in the year should improve assuming a trade deal is reached with China and Brexit can be constructively resolved.   We continue to believe that identifying businesses run by adept management teams capable of navigating dynamic conditions is a superior strategy to market timing.

Thank you for entrusting Ayrshire Capital Management LLC with your money. We are always available should you wish to discuss your portfolio or the markets in greater depth.

Sincerely,

JM Sam Nevin, Jr	W. Joseph Ryan III
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