CAPITAL MANAGEMENT GROUP
of Wells Fargo Advisors

HLM Short Take – May 31, 2019

As of Friday morning May 31, the 3 major US stock market indices have dipped below their 200 day moving averages. Technically, if this holds it could signal a further short term pullback. We view this market action as a normal cyclical correction within a secular bull market.

The current market turbulence has been led by presidential tweets, tariffs and trade war concerns, a slowing global economy and an inverted yield curve. While all this is troubling, the fundamental factors of the bull market remain in place. These include low inflation, low interest rates, an accommodating Federal Reserve and overall good earnings of US companies. Furthermore the strong U.S. dollar has benefited US markets and potential negative effects of the trade war could be offset by Fed rate cuts, higher government deficit spending and further growth in the real money supply.

Bull markets don't typically end until there is a high level of optimism, bordering on euphoria. Right now there is renewed pessimism. The put-call ratio which measures the ratio of investors who think the market will go down vs up is at historically high levels. Market sentiment as measured by bears vs bulls also indicates considerable fear and a negative outlook for stocks. To us this is a contrarian indicator and suggests we may not be that far away from, at least, a short term market bottom.

We would generally lighten up more when indices drop below moving averages and there's an inverted yield curve. However with potential sudden tweets and rate cuts, we could be surprised on the upside before we have a chance to buy. So even though indices may drop before they rally, we stay invested with the belief stocks will be higher later this year.

We remain with similar allocations of equities vs fixed income as we had at the start of 2019. Due to our belief that trade wars hurt foreign markets more than the US, we are overweight in US stocks. Our expectation is for 1 or 2 Fed rate cuts before year end and we follow the adage "Don't fight the Fed."

Call or email us if you want to discuss this further.

Hefter, Leshem, Margolis Capital Management Group
of Wells Fargo Advisors
1849 Green Bay Road
Suite 200
Highland Park, IL 60035
847 563-3400 phone
800 247-1541 toll-free
847 563-3420 fax
www.hlmcapital.com

Charlie Margolis, Ben Leshem, Steve Hefter
Managing Directors – Investments
Micah Nathan
Senior Vice President - Investments

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Disclosures

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Stocks are subject to market risk which means their value may fluctuate in response to general economic and market conditions, the prospects of individual companies, and industry sectors. Investments in equity securities are generally more volatile than other types of securities. There is no guarantee that dividend-paying stocks will return more than the overall stock market. Dividends are not guaranteed and are subject to change or elimination.

The prices of small and mid-cap company stocks are generally more volatile than large company stocks. They often involve higher risks because smaller companies may lack the management expertise, financial resources, product diversification and competitive strengths to endure adverse economic conditions.

Investing in foreign securities presents certain risks not associated with domestic investments, such as currency fluctuation, political and economic instability, and different accounting standards. This may result in greater share price volatility. Investing in emerging markets accentuates these risks

Investments that are concentrated in a specific sector or industry may be subject to a higher degree of market risk than investments that are more diversified.

Investments in fixed-income securities are subject to market, interest rate, credit and other risks. Bond prices fluctuate inversely to changes in interest rates. Therefore, a general rise in interest rates can result in the decline in the bond's price. Credit risk is the risk that an issuer will default on payments of interest and/or principal. This risk is heightened in lower rated bonds. If sold prior to maturity, fixed income securities are subject to market risk. All fixed income investments may be worth less than their original cost upon redemption or maturity.

There are special risks associated with an investment in real estate, including credit risk, interest rate fluctuations and the impact of varied economic conditions.

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