

Company Profile

Farmers Trust Company is licensed by the Ohio Division of Financial Institutions as a bank, authorized to conduct trust business and exercise full fiduciary powers. Our efforts are focused on the administration and management of trust assets. As an independent trust company, Farmers Trust Company offers several investment management options.

We are committed to providing the highest level of service in the areas of investment management, estate settlement, living trusts, testamentary trusts, charitable trusts, charitable endowments and employee benefit plans. Tax and estate planning services are available to our clients as well.

Farmers Trust Company has the unique ability to integrate investment, trust and estate management at a local level. Our clients appreciate the fact that their financial affairs are handled personally and confidentially. They also value our ability to work closely with their attorneys, accountants and insurance professionals to achieve a comprehensive financial strategy.

Market Recap and Outlook Second Quarter 2019

MARKET SCORECARD as of 06/30/2019	TOTAL RETURN IN USD	
	Q2	2019 TR YTD
DOW JONES IND AVG	3.21%	15.40%
S&P 500	4.30%	18.54%
NASDAQ	3.88%	21.34%
MSCI EAFE EQUITY (GROSS)	3.97%	14.49%
RUSSELL 2000 INDEX	2.10%	16.98%
MSCI EMERGING MARKET EQUITY (GROSS)	0.74%	10.76%
BARCLAYS INTERM. TREASURY	2.36%	3.99%
BARCLAYS INTERM. GOVT/CREDIT	2.59%	4.97%
BARCLAYS 5 YEAR MUNI INDEX	1.66%	3.80%
BARCLAYS HIGH YIELD CORP INDEX	2.50%	9.94%
ishares S&P GSCI COMMODITY TR INDEX	-1.42%	13.34%

Note: All returns include invested cash flows expressed in U.S. dollar terms

Market Recap

Domestic equity indices have demonstrated strong performance midway through 2019. The S&P 500 gained 18.54% in the first half of the year and small cap stocks (as measured by the Russell 2000 Index) are up 16.98% over the same time frame. The primary catalyst for equities in 2019 has been a more “dovish” Federal Reserve Bank (the Fed). The Fed has totally changed their stance on raising interest rates, and the market now expects a significant reduction in the Fed Funds rate in the 2nd half of the year. This complete turnaround in monetary policy has also had an effect on bond prices and yields, with the benchmark 10 year U.S. Treasury rate falling dramatically from the 2018 high of 3.24% to 2.0% at the end of June 2019. Lower interest rates have benefitted existing bondholders, as the Barclays Intermediate Government/Corporate Bond index returned 4.97% for the first 6 months of 2019. High yield bonds performed even better, recording a 9.94% gain year-to-date. The U.S. equity markets have generally fared better than the rest of the world, with the developed international MSCI EAFE index up 14.49% year to date. Emerging markets have trailed the other equity indices so far this year, although they still returned a respectable 10.76% for the 1st half of 2019. Real Estate (REITs) continued to perform well, up 19.27% through June end, and Commodities returned 13.34% over the same time frame. Growth stocks have experienced the best gains thus far in 2019; with the Information Technology sector leading the way with a 27.13% gain (Consumer Discretionary came in 2nd place with a 21.84% year-to-date gain). Thus far in 2019, the worst performing sectors in the S&P 500 have been Healthcare (+8.07%) and Energy stocks (+13.13%).

Key Points

- The Federal Reserve is likely to begin cutting the Fed Funds rate in the 2nd half of 2019 which should push bond yields even lower
- 2nd quarter 2019 year-over-year comparisons for both Real GDP and corporate profits will likely fall short of the previous years' data
- Economic growth (as measured by real GDP) and inflation (as measured by the PCE deflator) are likely to both decelerate in unison in the 3rd quarter of 2019
- Given the softer than expected economic and corporate profit data, volatility is likely to accelerate in the 2nd half of 2019

Investment Outlook

Our main investment themes for the remainder of 2019 are slowing growth (in both Real GDP and corporate profits) and slowing inflation, although inflationary pressures are likely to begin rising again by the end of the year. Therefore, we have taken a more conservative approach to the equity markets by overweighting traditionally defensive sectors like Utilities and Real Estate. We have simultaneously underweighted more cyclical areas of the market such as Financials and Materials. Given our view that inflation is likely to wane in the 2nd half of the year, we have eliminated our exposure to Treasury Inflation Protected (TIPS) Bonds. We have also reduced our high yield bond positions as highly levered companies will likely feel the strain of higher wages and further pressure from a simultaneous slowdown in sales and profits. We have added a modest position in Emerging Market equities as a result of their attractiveness from a comparable valuation standpoint. The Fed is likely to lower interest rates in the 2nd half of 2019, and falling U.S. interest rates bodes well for Emerging Market equities. In addition, it is our belief that the U.S. dollar may have reached (or will soon reach) a pinnacle, and any decline in the dollar's value against foreign currencies will also benefit Emerging Markets. Regarding fixed income portfolios, we are still slightly longer in duration than our benchmark (just over 4 years), and favor Treasuries, Government Agencies, and high grade Corporate bonds. We have added slightly to our foreign bond positions, as any reduction in the value of the dollar should benefit these holdings.

Global Macroeconomic Review and Outlook

Economic growth was strong in the 1st Quarter of 2019 with Real GDP expanding at an annualized pace of 3.1% (vs. 2.2% in Q1 of 2018). However, the year-over-year Real GDP comparison will become much more difficult to meet or exceed when the 2nd quarter numbers come out in late July 2019. Economists are estimating that the data will show the economy growing at or just below 2% for the 2nd quarter of 2019, well below the 2nd quarter 2018 reading of 4.2%. Similarly, corporate profits have a nearly impossible task of meeting or exceeding the growth rate they experienced in the 2nd quarter of 2018 when quarterly profit growth was 24.82%. Please note that both economic growth and corporate profits are still growing ... just not at the torrid pace they were last year! The headline U3 unemployment rate is holding steady at 3.6%, but the last Non-Farm Payroll number showed the economy only added 75,000 workers in May 2019, well below the consensus estimate of 175,000. One bad reading should not cause too much alarm, but a miss of that magnitude is definitely something to be monitored closely. Perhaps the low number of jobs added means that the supply of labor is too thin (i.e. we have hired all available workers). Assuming the poor employment reading was caused by a lack of available workers, the tight labor supply may instead further pressure on wages and a further strain on corporate profits. Inflation remains at or near the Fed target rate of 2%, and is likely to decline from that level in the 2nd half of 2019. In conclusion, the deceleration of key variables like corporate profits and Real GDP leads us to be cautious with our near-term outlook.



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