Mid-Year Update

June 2018

Considering we are coming into the summer months, we thought it would be prudent to reveal what will unfold for the remainder of 2018. First, the S&P 500 will finish the year at 3100, the Dow Jones at 27,500, the Ten Year Treasury will be yielding 3.33%, oil will close the year at 85 dollars a barrel, the Phillies will win the World Series, Tiger Woods will take the US Open, Justify will unfortunately come in 5th at the Belmont Stakes, Republicans will lose the Senate and keep the House, oh and the President will give up his Twitter account.

It's still amazing to us how much time and energy goes into trying to predict the future. Yet, these ten predictions that took us literally 15 seconds to scribe, have just as good a chance of becoming true as the plethora of predictions from many of the famed market, sports, and political strategists that continue to operate under the illusion that education and knowledge equates to super human powers.

Warren Buffet has said, "a prediction about the direction of the stock market tells you nothing about where stocks are headed, but a whole lot about the person doing the predicting."

The fact is, unlike market strategists or economists, Warren Buffet isn't paid to make bold market predictions. He is paid to weigh the current evidence of the market and simply play the cards he is dealt.

In our view, no matter how you slice it, the economic data is very good right now. In fact, the earnings growth rate on the S&P 500 in the first quarter came in at 26.4% year over year which is the best we've seen since 2011! It's now quite clear that the stock market finally transitioned from an interest rate driven market to an earnings driven market in the third quarter of 2016. Historically, this is usually the longest phase of a bull market.*

That said, some of Wall Street's strategists are now predicting that corporate earnings have peaked and the bull market is quite limited. While this may be true, we would argue it's an extremely bold call considering the verdict is still out on the full impact of the tax cuts and other fiscal measures that have been recently rolled out. However, even if earnings have peaked, history would show that's not always indicative of the bull market ending. We could very well go through a period of earnings growth consolidation before another leg higher. **

John Templeton said it best - "Bull markets are born on pessimism, grow on skepticism, mature on optimism, and die on euphoria." Perhaps this crazy political environment is actually good for the market as it is keeping a lid on enthusiasm. Markets like to climb a wall of worry. Given the healthy economic numbers, if we didn't have these negative narratives around trade, North Korea, Italy, etc. this market would probably be heading toward the moon and everyone would have a big happy smile on their face.

But people tend to forget that a certain degree of pessimism is really quite healthy for markets as it creates periods of consolation which allows the market to rest and restore energy for another leg higher. If everyone is happy and fully invested, then there's no one left to keep pushing stocks up.

The biggest risk we see is the potential for inflation and the Federal Reserve being forced to raise interest rates quicker than they anticipate. This would, more than likely, throw cold water on the economy and could end the bull market. Also, the jury is still out on the aftermath of 10 years' worth of unprecedented monetary policy by the Federal Reserve and other central banks around the world. With the Federal Reserve's balance sheet sitting at $4.3 trillion, we are hopeful they are able to unwind this experiment without any hiccups. (For more info on the Federal Reserve, see the piece we wrote last year titled 'Between a Rock and a Hard Place')*** https://fa.morganstanley.com/harboroak/#commentaryfromourgroup

At the end of the day, everyone has their opinions - but what ultimately drives stock prices is simply supply and demand. At the present time, the evidence is still fairly clear that demand remains in control as the market remains in a bullish uptrend. Granted, we had a 10% correction in February and have been consolidating or range bound since; we view this as a healthy development, as it has allowed the market to digest January's parabolic move and start forming a base to work from.

The S&P 500 could certainly break to the downside of this range, which we would view as quite negative. But, in our view, the bias is to the upside as we are seeing a series of higher lows. Also the S&P 500 is trading above its 200 and 50 day moving averages again and most importantly small cap stocks (that tend to lead the way) have already broken to the upside of their range. ****

All of this said, professional money management is not about making predications, but instead weighing the evidence, calculating probabilities, and attempting to skew the odds in your favor. We realize this is perhaps not as sexy as making a bold prognostication, but it's the truth and that is what our clients deserve.

Mike Anderson
Senior Portfolio Manager
Vice President
Financial Advisor
NM*LS# 1418736*

Gray Howard
Senior Portfolio Manager
Vice President
Financial Advisor
NMLS# 1622252

Tony Prudhomme
Portfolio Management Director
Senior Vice President
Financial Advsior

Sources
**http://lipperalpha.financial.thomsonreuters.com/2018/06/sp-500-17q1-earnings-dashboard/*
***https://www.marketwatch.com/story/heres-why-peak-earnings-dont-mean-its-all-downhill-for-the-stock-market-2018-05-07*
****https://www.federalreserve.gov/monetarypolicy/bst_recenttrends.htm*
**** *Thomson Reuters/Charts*

DISCLAIMERS

Technical analysis is the study of past price and volume trends of a security in an attempt to predict the security's future price and volume trends. Its limitations include but are not limited to: the lack of fundamental analysis of a security's financial condition, lack of analysis of macro-economic trend forecasts, the bias of the technician's view and the possibility that past participants were not entirely rational in their past purchases or sales of the security being analyzed. Investors using technical analysis should consider these limitations prior to making an investment decision.

This material does not provide individually tailored investment advice. It has been prepared without regard to the individual financial circumstances and objectives of persons who receive it. The strategies and/or investments discussed in this material may not be suitable for all investors. Morgan Stanley Wealth Management recommends that investors independently evaluate particular investments and strategies, and encourages investors to seek the advice of a Financial Advisor. The appropriateness of a particular investment or strategy will depend on an investor's individual circumstances and objectives.

The individuals mentioned as the Portfolio Management Team are Financial Advisors with Morgan Stanley participating in the Morgan Stanley Portfolio Management program. The Portfolio Management program is an investment advisory program in which the client's Financial Advisor invests the client's assets on a discretionary basis in a range of securities.
The Portfolio Management program is described in the applicable Morgan Stanley ADV Part 2, available at www.morgan stanley.com/ADV or from your Financial Advisor.

Past performance of any security is not a guarantee of future performance.
There is no guarantee that this investment strategy will work under all market conditions.

Holdings are subject to change daily, so any securities discussed in this profile may or may not be included in your account if you invest in this investment strategy. Do not assume that any holdings mentioned were, or will be, profitable.

Morgan Stanley

THE HARBOR OAK GROUP

Providing Sound Guidance in an Uncertain World

704-331-2202 |866-219-3101
6101 Carnegie Blvd Charlotte, NC 28209
http://fa.morganstanley.com/harboroak