Advisory Notes

DECEMBER 2018

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A Year in Review

The year of volatility (see Market Table) – While most of 2018 saw markets moving forward with optimism driven by fiscal stimulus and growth of earnings, there was also divergence in signals between the Fed rate hike decisions, based on hard economic data and soft economic data such as consumer confidence readings and economic surveys.

The Fed continued the policy of raising rates (four times in 2018) and by the final December hike some believed the additional tightening was unwarranted. The Fed is now worried about being perceived as not having independence from the White House, so we expect it to be more hard data dependent and to increase rates another two times in 2019 in order to get to a normalized target rate.

Volatility increased dramatically into the fourth quarter, due to fears of rising interest rates, government shutdowns and trade war implications across the globe. These uncertainties fueled the ups and downs in the markets recently and have reset the market multiples into what we believe is a fair value with modest earnings growth expectations "baked in" to start the New Year.

The fear of the yield curve inversion, which is when the short-term rates are higher than long-term rates, may signal a slowdown in economic growth and ultimately a mild or deeper recession. In the first week of December, we started to witness a time where the yield on the 2-year Treasury note was higher than the 5-year Treasury note and the belly of the interest rate curve started to invert. A true inversion is between the 10-year Treasury note and the 3-month Treasury yield. So is this a handshake or will long-term rates stay lower? Interest rates remain relatively high given the market pullback, while the Fed continues

See **A Year** *on Page 3*

Market Table

Valicenti Advisory Services, Inc.
Comparative Index Period Returns
From 12-31-17 THROUGH 12-31-18

	DJIA	S&P 500	NASDAQ	Russell 2000 Index	Bloomberg Barclays Muni Bond Index	FTSE Corporate Bond Index	U.S. Treasury Bill Index (90 day)
12-31-17 to 03-31-18	-1.96	-0.76	2.32	-0.40	-1.21	-2.26	0.38
03-31-18 to 06-30-18	1.26	3.43	6.33	7.43	0.95	-1.00	0.41
06-30-18 to 09-30-18	9.63	7.71	7.14	3.26	-0.16	0.87	0.57
09-30-18 to 12-31-18	-11.31	-13.52	-17.54	-20.51	1.85	0.00	0.66
YTD Returns 12-31-17 to 12-31-18	-3.48	-4.38	-3.88	-12.18	1.40	-2.41	2.03

Director's Chair

Blue Wave Turned Purple Stream

The so-called "blue wave" of Democrats that was supposed to take over the Congress in this year's mid-term elections ran into a "red tide" of Republican victories in the Senate. In December 2017, the generic ballot, a poll by eleven different media outlets that measures the preference of voter desire of one party versus the other, favored Democrats by thirteen points, a clear sign of a sweep. As late as September 4, 2018, the poll signaled a nine and a half point preference for the Democrats to still sweep territory that should have flipped sixty seats in the House of Representatives and two in the Senate. What happened to the tsunami? Nomination hearings for a Supreme Court justice turned into a spectacle that rivaled what occurred before the same committee in 1991, coupled with continued improving numbers for jobless claims and Gross Domestic Product. This awakened the Republican base, which turned out in greater numbers than most models predicted. Approximately forty House seats flipped into Democrat hands, impressive, but it could have been more. What was more of a stunner and not predicted in the polls was a three seat net gain by Republicans in the Senate. An average of polls by over 10 media outlets toward the end of September predicted the Democrats would have a net gain of at least a seat in the Senate.

Now that both sides have spent a projected $5 billion dollars, which is approximately $10.7 million dollars per seat, running for Federal office for jobs that pay $174,000 per year (does something not smell fishy here?), how do we take advantage of the new political landscape as investors? For the most part, a split Congress will produce a lot of nothing; I know you are asking how is that different from any other Congress? The budget process should produce new winners particularly within healthcare. Democratic House members will undoubtedly move to increase spending on medical research as done at the National Institute of Health (NIH). The NIH is such a popular organization, researching cures for cancer for instance, that approximately half of the Republican delegation supports NIH funding and, with the new makeup of the Congress, such spending will increase. Companies that are suppliers to such organizations will be beneficiaries. Democrats gaining governorships of a few states that did not expand Medicaid under the Obamacare law will be another positive for the sector as these states are very likely to expand Medicaid, increasing the insured population and thereby increasing demand for healthcare services. Another segment that may benefit, although is more tenuous, under the coming makeup of the Congress, is infrastructure suppliers. Politicians love spending taxpayer money in their own districts to show what they have done for the voters. A Republican Senate and Democrat House might be able to find common ground on spending that will make them look good in the 2020 elections, thereby benefitting construction or material stocks. This is how we believe investors can benefit from the "purple stream."

How the newly staffed Congress will take care of America can best be summed up by Groucho Marx's character of Rufus T. Firefly, as the newly placed political leader in *Duck Soup*, when he said, "The last man nearly ruined this place he didn't know what to do with it. If you think this country's bad off now, just wait till I get through with it!"

Louis F. Ruize
Director of Research/Portfolio Manager

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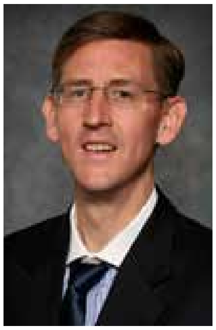
Investment Strategy



We would like to wish you all a very Happy New Year and a prosperous 2019! There was a move to higher volatility in 2018 which hasn't been seen in several years. Some of the reasons for the volatility are as follows:

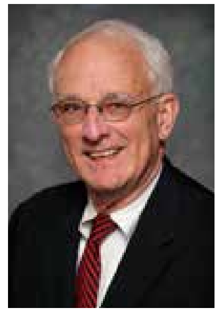
1. The Federal Reserve continues to raise interest rates in an effort to keep the economy from overheating. This impacts lending and liquidity.
2. Concerns over trade weigh on global markets, while world leaders try to come to some common ground.
3. The change in leadership in the House of Representatives with the mid-term elections brings up concerns with how this may impact Washington D.C. getting things accomplished.
4. Slowing growth in the Eurozone, Japan and China.

On the positive side, the economy is growing at a strong pace, the employment picture remains strong, wages are gradually moving higher and consumer confidence remains high. Some companies have outlined the effect of global trade as a potential impact on earnings.

In this environment, we are staying focused on companies with strong balance sheets, forward growth in potential earnings and attractive valuations. Asset allocation, which will vary based on client risk levels, income needs and specific directives, will remain between 5% - 15% for money markets (to be used for opportunities as they present themselves), 25% - 35% for fixed income and 40% - 65% for equities.

Jeffrey S. Naylor
Executive Vice President/CFO

Referrals



Do you remember how you became a client of our firm? Perhaps, you were referred by an existing client.

Referrals are the "life blood" of our business. When a client refers someone to us, they are not only reflecting confidence in us, but are also comfortable that the person being referred most likely needs the services that we provide.

Whether its help with managing an existing investment account, retirement planning, tax planning, estate planning, an inheritance, etc., we have an educated, experienced group of professionals with expertise ranging from portfolio management to tax preparation and everything in between.

If you have someone who may benefit from financial guidance, a disciplined approach and specialized expertise, please have them contact us at (607)734-2665 or, if out of the area (866)734-2665. We'll be happy to call them to discuss our services further. The highest compliment our clients can give us is the referral of their friends and family. Thank you for your trust!

Ralph H. Roberts, Jr.
Vice President of Client Services

A Year in Review

(Continued from page 1)

to tap the brakes on economic growth. The Fed should be more cautious as we believe inflationary factors are low while low unemployment has not yet produced a major cost push. Oil prices, which are an inflationary gauge, are at the bottom of their trading range and are extremely low.

The U.S. economy is coming off its second longest tenured expansion in recent history, which has helped bring up global economies. At this point, it seems that the monetary tightening in the U.S. may be stalling other economies such as Japan, Europe and China.

So, as the Federal Reserve tries to get U.S. interest rates back to normal, to manage the U.S. balance sheet and to keep the economy moving forward, we do have some tailwinds such as the fiscal stimulus of the tax cuts that could help. Deregulation in the financial sector, which is barely one year old, and lower overall inflation pressures may help eliminate overburdening costs while sustaining this period of economic growth and low unemployment. Consumers seem to have confidence which showed during this holiday season as shoppers exceeded expectations.

We are in the camp that this fourth quarter correction has repriced the market going forward. Adding 7% to 8% earnings growth at a reasonable multiple will provide some opportunities in both the fixed income and equity markets.

We wish you a happy and prosperous New Year in 2019.

Joseph M. Valicenti
President/CEO

Analyst Corner

Over the last six months, we have commented in this piece about two 2018 market performance results. First, stock market returns were extremely strong to the upside throughout the middle months of the calendar year. The S&P 500 was up over 11.4% (over 20%+ when annualized) in the April through September period. Second, as longer term interest rates gradually moved higher, corporate bond prices which usually price lower as a result of the higher rates, remained buoyant as the credit or risky component to fixed income prices compensated for the adverse rate move. In short, a positive credit price move canceled out a negative interest rate move in investors' corporate bond allocations.

I believe that the easiest way to describe how the market movements changed in Q4 is to note that these two things reversed course very quickly. Credit concerns began to creep into weaker segments of corporate bond pricing. Risk-free government rates faded from their recent highs and markets in general very quickly priced in slower growth and lower expected inflation heading into 2019 sending the major equity indices sharply down. With the current Atlanta Fed GDPNow forecasting for Q4 real GDP at 2.7%, an imminent contraction in the U.S. economy over the next few quarters does not appear likely, barring an unexpected significant negative shock. Conversely, the strong growth momentum combined with weaker energy cost inputs and lower expectations for future funding rate hikes may in time provide the basis for a bull trend continuation should the worst of fears disappear via fundamental corporate earnings resilience and status quo consumption patterns. Going into the end of the year that type of meaningful bounce has yet to appear. Forecasts for a slowing economic growth trend appear to be reasonable, as we have been moving at perhaps an above trend pace the last twelve months. Further, various situations globally around trade, fiscal and monetary policies are providing uncertainty.

Positive Market Influences	Negative Market Influences
• U.S. Real Q4 GDP Outlook	• Tightening Dollar Liquidity
• Reduced Inflation Expectations	• Credit Concerns
• Consumer Resilience	• Slowing Growth
• Industrial Production	• Trade Uncertainty
	• Fed Tightening

The S&P 500 was down -13.5% on a quarter to date total return basis which as stated earlier reversed out Q2 and Q3's strong upward move. Illustrating the defensiveness and fear typical of an abrupt move, Utilities were the only sector with a positive 0.5% return while other defensive areas such as Real Estate and Consumer Staples held up better than the overall market and were down only -4.6% and -5.9% respectively. The pro-cyclical sectors such as Energy, Technology, Consumer Discretionary, Industrials, Materials and Financials were each down between -10% and -25% in the quarter. The FTSE USBIG Corporate Credit Index was down - 0.24% which offered some stability. Notable is the fact that the credit weakness prevented corporate bond allocations from mitigating equity portfolio results even more as the positive interest rate move supported bond prices.

Technically speaking, the market has experienced enough of a pullback in Q4 to concern market trend followers. A quick movement down of this size, peak to trough, is not a frequent occurrence yet neither is transitioning from the last decade's accumulated policy accommodation. The most recent December Fed hike followed by slightly more dovish messaging regarding the pace of hikes next year is just now being absorbed by market participants. The overall effect on economic and liquidity conditions and investor risk behavior will be watched closely as the market looks towards fundamental earnings outcomes for Q4 '18 and Q1 '19. Clearly, negative influences eventually overpowered the positives, though with that pressure build up and then release the current symmetry at this point in time is most probably neutral to slightly negative as valuations have been reduced but we have yet to see a near-term inflection higher.

Positive Market Influences:

- **U.S. Real Q4 GDP Outlook** – Real GDP which measures growth after the impact of inflation ran at a seasonally adjusted annualized quarterly rate of 4.2% in Q2 and Q3 growth came in at 3.5%. The Q4 GDP estimate as per the Atlanta Fed GDPNow is currently at 2.7%.
- **Reduced Inflation Expectations** – Forward market expectations for inflation have fallen from around 2% to 1.5% as oil prices have concurrently significantly softened.
- **Consumer Resilience** – The Retail Sales Control Group, which ties into GDP, has shown solid and increasing month over month rates of growth in spending for October and November.
- **Industrial Production** – After dipping slightly in October, industrial production has shown a strong 0.6% month over month rebound in November alleviating near-term concerns. There are expectations that the very strong readings may soften from the high levels, but for now there does appear to be underlying strength.

See **Analyst** *on Page 5*

Analyst Corner

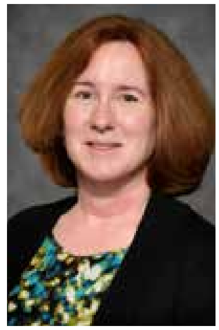
(Continued from page 4)

Negative Market Influences:

- **Tightening Dollar Liquidity** – The Fed's balance sheet is shrinking and at the same time foreign countries are creating fewer USD reserves. The supply of high powered money denominated in dollars globally is on the decline, which tightens overall liquidity conditions.
- **Credit Concerns** – In the lower interest rate environment, non-financial corporate indebtedness grew to around 46% of GDP, which is historically high. Calling recent credit softness a systemic risk may be a bit of an overshoot at this point, though it is observed everywhere along the quality spectrum that credit instruments are pricing risk higher.
- **Slowing Growth** – Growth internationally and in the U.S. is expected to soften a bit in 2019 from higher levels in 2018.
- **Trade Uncertainty** – Movement on the trade dispute with China and the United States is expected next year though outcomes are uncertain, which then creates an unknown regarding inflation and growth effects.
- **Fed Tightening** – The Fed has raised short-term rates nine times since December of 2015 from extremely low levels. Subsequently, longer term rates have also risen. They have done this because positive growth and inflation dynamics warranted the moves though given the slight adjustment in expectations for further raises next year and subsequent market price reactions, we may have reached a point where the higher funding and borrowing cost levels are becoming headwinds.

Daniel P. Burchill
Security Analyst

Wants vs. Needs



Now that the holidays are over and we are staring down the credit card bills, it is time to take stock of needs vs. wants. There are many people who cannot distinguish between wanting something and needing something. Understanding the difference is the first step in becoming financially savvy and taking control of your money.

Let's start with needs, which by definition, are things that are necessary or required because they are essential to survival. Some examples of needs are shelter, food, water and clothing which are necessary to survive – in other words, a person could die without these needs being met. The first rule of budgeting is to make sure your income will cover your needs. If you don't have a roof over your head, not much else will matter in your life.

After making sure you are putting funds into savings, the need for shelter is met – an affordable (for your budget) place to live, taxes and utilities are easily paid, the need for basic food and water would come next, then clothing, transportation and communication (phone, internet). Then other bills such as student loans and credit cards must be paid.

Wants are things that make life more enjoyable and comfortable, but which we could live without. The latest smartphone, designer fashions and the 2019 Lamborghini Aventador Coupe are all examples of wants. We would all like to have these, but we don't need them to survive. Our old phone still works and the Ford Focus is running well, so why go into debt for the newest gadgets?

Credit card debt is one way we get into trouble when confusing needs and wants. Once we put a want on a credit card (the newest Coach handbag or the Hermes scarf), it now becomes a needs, as it is debt that needs to be paid. After the holidays, this becomes apparent when many people who used their credit cards to fund the wants of family and friends wake up with a "credit card hangover" in January.

We get into trouble with our money when we perceive wants as needs. Everyone needs shelter, but not everyone needs the biggest house in the best neighborhood, no matter what HGTV tells you. Being in control of your money will allow you to meet your needs and to fund some, if not all, of your wants.

Ann S. Nolan, FPQP™
Administrative Assistant

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New Year's Resolutions

Now that the holidays are over and we embark on a New Year, you may be contemplating resolutions for the New Year, which might include saving money, home organization and home projects, etc. While you are making that list, may I make a few suggestions from an insurance perspective that can perhaps help you save money and protect your investments?

Making Smart Savings Choices

In today's unsettled economy, many people are looking for ways to stretch their money — but sometimes this includes altering insurance coverages to dangerously low levels or eliminating coverage entirely. If you're thinking about changing your coverage to save money, consider the key issues below:

- **Make sure you're receiving the appropriate discounts and credits:** Most insurers offer a variety of policy credits and account discounts that can translate into significant savings — without endangering the level of protection you need for your home, autos and other valuable property. Often, if you purchase multiple policies through the same insurance company, you'll receive further discounts. People who own motorcycles or boats and who complete approved safety courses can qualify for discounts and families with teen drivers who earn good grades in school may qualify for auto policy discounts.
- **Increase deductibles for cost savings:** Only a small percentage of homeowners have claims in any given year, so you might consider increasing your deductibles.
- **Specialty lines coverage options:** Own a classic car or RV? If their use is seasonal, you can typically reduce your coverage to liability only during the off-season, then add full coverage only when you are actually using the vehicle.
- **Full payment on policy:** Depending on your financial circumstances, you may be able to make lump-sum payments instead of partial premium payments, such as monthly or quarterly. Partial payments often include small transaction fees, so paying the full amount can eliminate those extra costs.

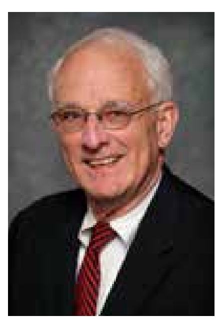
Some Decisions to Avoid

It is just as important to understand what not to do as you look for cost savings. Here are some scenarios you should avoid:

- **It may be unwise to carry only the minimum state-required amount of uninsured/underinsured motorist coverage on auto policies or to cancel it entirely if it is not required in your state:** According to the Insurance Research Council (IRC), the correlation between the percentage of uninsured motorists and the unemployment rate is high — when the economy is struggling, more people go without insurance. You want to make sure you're protected in this instance.
- **Ignoring renters insurance:** This coverage is often overlooked no matter the shape of the economy. Landlords' policies generally only cover the structure,

See **New Year's** *on Page 7*

Thank You!



Thirty four years! Wow! Where has the time gone?

It is hard to believe that we are completing our 34th year and that the 35th is just around the corner. We have much for which to be thankful, not the least of which are our diverse and loyal clients who have given us the opportunity to know them, to work with them and to help them along their "financial journey." At the same time, a thank you to our wonderful staff for dedication and hard work. We continue to use a teamwork approach to our business and we continue to "Cultivate Relationships" while always adhering to our moto *"Our Clients Come First."*

As this is being written on December 18, 2018, our various departments are focused on the usual year-end duties and planning for 2019.

From all of us to all of you, we wish you a prosperous and healthy New Year.

Ralph H. Roberts, Jr.
Vice President of Client Services

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New Year's Resolutions

(Continued from page 6)

not the individual renters' contents. Imagine having to replace furniture, clothing and other personal property out of pocket because you excluded this essential, affordable coverage and then suffered a devastating loss from a burglary or other covered event.

Much of Your Home's Value is What's Inside

There's a popular saying that goes like this: "Home is where the heart is." That saying rings true for many who find "home" a safe haven and a place to cherish, convene with family and friends, raise children, cook meals, rest, retire and celebrate. Most will agree a home is not just a pile of bricks and mortar. Rather, a true "home" comprises much more, including everything inside it.

Some of the things inside your house that help make it your home include your furniture and appliances, clothing, sports equipment and electronic goods. These items are considered personal property – and it's really important to protect it all.

How Do I Protect What Really Makes My House a Home?

Protecting the important stuff inside your home begins with an understanding of what you have. If you're like many people, you may find your home contains much more personal property than you realize.

To understand how much stuff you have, develop a careful inventory of your personal property following these tips:

- Use a video camera to record and audibly describe items as you move through your home. If you don't have access to a video camera, use a standard camera or phone camera.
- Whether you use still photos or video to develop your inventory, include brand names and descriptions where possible, especially on high-cost items.
- Keep any and all receipts on high-dollar purchases. Keep these receipts filed together with any instruction booklets, warranties, etc. that accompany the items.
- Store your video or photo inventory offsite or back it up with an additional drive.
- When you make new purchases, be sure to add them to your inventory.

If you have high-value items, be sure to check with us so we can review your homeowner's coverage to make sure you're properly protected. We understand that your home is not just a house and we are here to help ensure that everything important to you is protected — both outside and inside your home.

Contact Us!

At Valicenti Insurance Services, Inc., we can work with you to make sure you've got the coverage you need, while at the same time using all possible credits and discounts to make that coverage affordable. Saving money is important, but so is making sure that what you've got is protected. Just give us a call at (607)215-0242 or send us a note at info@valicentiins.com. We want to help you meet your goals and to make sure what's important to you is protected!

Suzanne M. Valicenti
President/CEO

The 2018 Child Tax Credit

Raising children costs quite a bit of money these days. Food and clothing alone can make up a major part of the expense of such an endeavor. This is why there is just as much interest as there ever has been in the child tax credit.

One very notable change to the child tax credit has been the increase made to the tax credit brought about by the Tax Cut and Jobs Act of 2017. Under the old law, the child tax credit was $1,000 per child under 17 years of age. Under the new tax law, the child tax credit is $2,000. It should be noted that under the new law, there are no longer personal exemptions that can be claimed by a taxpayer, their spouse or for their dependents. Under prior law, the personal exemption was $4,050 per personal exemption. At a marginal tax rate of 15%, that would be worth $607.50 per personal exemption. If you are filing in the 25% tax bracket, the personal exemption is worth $1,012.50. As a result, you might actually be losing $12.50 of tax benefit with the tax change.

Additionally, there are income phase-outs for qualifying to be able to take the child tax credit. Under prior law, the child tax credit started to phase-out for single filers with modified adjusted gross income (MAGI) over $75,000 and for joint filers with MAGIs over $110,000. For 2018, the phase-out does not start until single filers have MAGI of $200,000 and joint filers have MAGI of $400,000. That can make a big difference in who can qualify and be able to take the child tax credit in 2018. You could possibly qualify for a refund of the child tax credit even if the child tax credit reduces your income tax to zero. The refund of the additional child tax credit could be as high as $1,400.

There is a new tax credit for people that fall under the definition of qualifying dependents other than your qualifying children. The tax credit amounts to $500 per qualifying dependent. A qualifying dependent must meet certain criteria to be determined as such - the taxpayer must provide more than half of the support for the qualifying dependent, the qualifying dependent must earn less than $4,150 and must be part of the household for an entire year. The $500 does not make up for the loss of the dependency exemption amount, but it can help defray some of the costs.

There have been quite a number of changes made in the tax law and, as a result, taxpayers could have some surprises both on the upside and on the downside when they file their taxes for 2018.

Paul E. Hornbuckle, CPA
Vice President of Tax and Business Services

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