# Advisory Notes

March 2019

CELEBRATING 35 YEARS

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## 35 Years of Business and Growing

Wow, it seems like only yesterday that I was writing to you about our 30th anniversary and our accomplishments. Five years pass so seamlessly when you have a great staff, clients and vendors that create such an incredible business environment for success. Our assets under management have grown steadily and have reached $450 million.

Jeffrey Naylor, our Executive Vice President and my business partner, joined the firm 26 years ago, two years after I did and we have been working together to engage our clients' wealth and investment needs ever since. Jeff and I have been leading the company over the past 13 years, as Vince Valicenti, Chairman of the Board, transitioned ownership into our capable hands.

Additional members of our management team are Ralph Roberts, Vice President of Client Services; Tracy Jenkins, Vice President of Operations; Daniel Burchill, Security Analyst; Louis Ruize, Director of Investment Research; Theresa Stewart, Assistant Corporate Secretary; Paul Hornbuckle, Vice President of Tax and Business Services; Liz Zarnoch, Tax and Accounting Manager; and Suzanne Valicenti, President of Valicenti Insurance Services, Inc. Below is a copy of our press release:

Valicenti Advisory Services, Inc., an independent fee only SEC Registered Investment Advisory firm, is pleased to announce that it is celebrating *35 years of cultivating relationships*. Since 1984, it has employed a team approach to give its clients individual in-depth advice through portfolio management, planning and consulting services. The firm also has a professional Tax & Business Services division. Its affiliate, Valicenti Insurance Services, Inc., is a full service premium

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## Market Table

**Valicenti Advisory Services, Inc.**
**Comparative Index Period Returns**
**From 12-31-18 THROUGH 03-31-19**

| | DJIA | S&P 500 | NASDAQ | Russell 2000 Index | BBG Barclays Muni Bond Index | FTSE Corporate Bond Index | U.S. Treasury Bill Index (90 day) |
|---|---|---|---|---|---|---|---|
| 12-31-18 to 01-31-19 | 7.29 | 8.01 | 9.74 | 11.19 | 0.83 | 2.06 | 0.28 |
| 01-31-19 to 02-28-19 | 4.03 | 3.21 | 3.44 | 5.08 | 0.58 | 0.28 | 0.19 |
| 02-28-19 to 03-31-19 | 0.17 | 1.94 | 2.61 | -2.27 | 1.72 | 2.66 | 0.19 |
| **Cumulative Returns:** 12-31-18 to 03-31-19 | 11.81 | 13.65 | 16.49 | 14.18 | 3.16 | 5.07 | 0.66 |

## Director's Chair

Actor Keanu Reeves and Federal Reserve (Fed) Chairman Jerome Powell have things in common, more in a moment. Powell has had a rough six months that began with an October interview, which insinuated the Fed was on a pre-set course of interest rate hikes and balance sheet contraction, both which can slow the economy. At the same time, investors started to worry as economic growth began to slow down from a tax cut stimulated pace commencing a market downturn. Subsequent missteps answering press questions during the December Fed meeting further exacerbated the market slide causing a 13.5% decline in the S&P 500 for the fourth quarter and a 9% decline for the month, the worst December since the Great Depression. Institutional investors and the President were trying to send Powell a message that the economy is slowing and not to make the same policy mistakes as his predecessors have done by tightening interest rates to the point where the economy is choked into recession. There is a long established and true saying on Wall Street, "Bull markets don't die of old age, but rather they are killed by the Fed." On January 4, 2019 at the American Economic Association's annual meeting flanked by predecessors Janet Yellen and Ben Bernanke, Powell firmly and unequivocally signaled the Fed was "prepared to adjust (interest rate) policy quickly," "listen carefully" to the message the market was sending and wouldn't hesitate to change balance sheet policy. Going a step forward, he gave examples of how his predecessor, Yellen, changed policy quickly. The speech could be called a thoughtful reassessment of economic policy as indicated by the most recent economic data or a "hostage speech" from someone who has been beaten into submission by market forces and political pressure. Powell read from and stuck to prepared remarks as if in the hands of captors, sparking a 13.7% rally in the S&P 500 for the first quarter. Just like Keanu Reeves' character of Jack Traven in the movie *Speed*, both he and Powell have played the part of a hostage on TV.

If you remember the movie *Speed*, a bus carrying passengers who become hostages is rigged with explosives. If the bus drives too fast, it risks smashing into objects or crashing, but if it drives below 50 mph, the bomb detonates. The Fed finds itself in a similar situation; keep interest rates too low and the economy could overheat under inflationary pressures or raise rates and risk slowing the economy to the point of stalling and creating a recession.

With his January 4 speech, Powell indicated that the Fed is open to exceeding its 2% inflation target thereby holding off on rate increases that will likely extend the life of our current economic expansion. Subsequent comments have indicated that further contraction of the Fed's balance sheet would cease by year's end. Couple this news with relatively low inflation, moderate economic growth of the Gross Domestic Product (GDP) at a rate above 2% and moderate earnings growth in the S&P 500 in the low-single digits creates a benign environment for stocks. Do not expect, however, the remainder of 2019 to be as robust as the first quarter. Like Sandra Bullock's character that drove the bus around obstacles, the Fed, while keeping an eye on the uncertain U.S. trade policy, will have to watch if tight labor markets finally spark much higher inflation. For now, a rising labor participation rate is holding down wage inflation as long time unemployed individuals are finally coming back into the job market after a decade long hiatus. The bus known as the U.S.A. is currently traveling at 51 mph and it's in Chairman Powell's hands to continue to defuse the situation.

Louis F. Ruize
*Director of Research/Portfolio Manager*

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## Investment Strategy

The first quarter of 2019 saw a recovery in both the U.S. equity and the bond markets. With the Federal Reserve adopting seemingly a more dovish tone over the last 3 months, an improvement in investor optimism, a continued strong employment picture and consumer confidence remaining high have all helped spark the best first quarter in U.S. equities since 1998.

The first quarter had obstacles that came on many fronts, led by but not limited to a government shutdown, challenges in global trade, testy political environments both at home and abroad, a brief yield curve inversion and continued slowing growth in both China and the Eurozone. Despite those headwinds, the U.S. economy continued to show modest growth and signs of near-term inflation seemed to be in check.

With all of that in mind and with first quarter earnings right around the corner, we are staying nimble with our asset allocations. Our asset mix is flexible with 5-20% in money markets, 25-35% in fixed income and 40-65% in equities, which will vary based on client risk levels, income needs and specific directives. We will continue to look for opportunities as they present themselves with a focus on larger U.S. companies that continue to show positive earnings growth and improving balance sheets along with good cash flow.

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Jeffrey S. Naylor
*Executive Vice President/CFO*

## IRA Funds To Purchase a House?

The simple answer is that you can withdraw money from an IRA whenever you want, but if you do so without an IRA allowed exemption, you will have to pay a 10% early withdrawal penalty. For first time homebuyers, there is an exemption which allows the withdrawal of as much as $10,000 penalty free from a traditional IRA, however, it will be taxable income. The IRA definition of a first time homebuyer is someone who has not owned a principal residence within the last two years.

The same applies to the spouse. The purchaser doesn't have to be you - it can be your child, grandchild or parent.

If you have a Roth IRA, you may be able to take out more than $10,000, as you can always withdraw Roth IRA contributions, tax and penalty free. You can withdraw up to $10,000 of your earnings under the first time homebuyer exemption and the withdrawal will be tax free, if your account has been open for more than five years.

We suggest that you check with your financial advisor and your tax preparer before taking funds from your IRA.

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

## 35 Years

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based agency. Valicenti has a staff of 22 professionals and three offices, with two locations in Elmira and one in Corning.

"Our key to success has been living by our core set of values, putting our client's interests first, serving not selling and providing holistic viewpoints to build a customized plan for each client, being stewards of their money and champions of their financial success. Every relationship is a vote of trust and we strive to work hard to earn that trust every day," said Joe Valicenti, President and CEO of the firm.

By listening to its clients' needs and gaining their trust, Valicenti has grown over 35 years. Valicenti is proud of its long history and its ties to our communities. The firm's collective wisdom yields reliable, demonstrable advice that has met the needs of its clients and it remains committed to existing relationships and to cultivating new opportunities long into the future.

The management and staff thank all of their loyal clients and vendors for supporting them for the last 35 years.

We thank you, the clients, for your continued support, trust and confidence in us to continue to meet your financial dreams of today and the future.

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Joseph M. Valicenti
*President/CEO*

## Analyst Corner

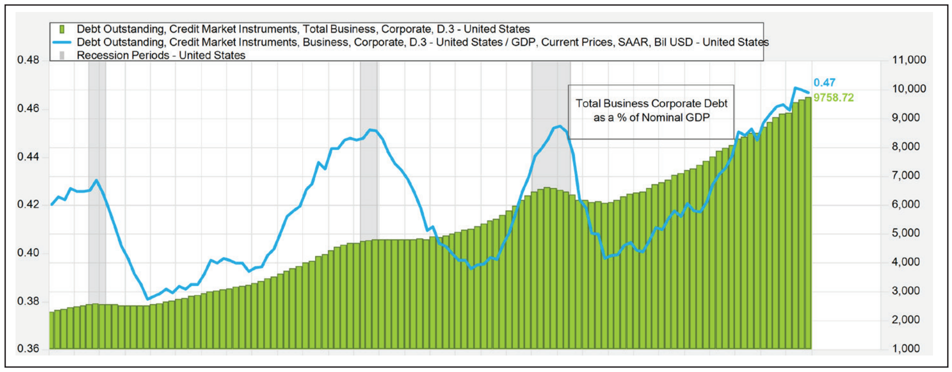
As we concluded 2018 with a major -20% move in the S&P 500 index, we remarked in this piece that markets were just beginning to absorb recent Fed dovishness. While we were reaching a point where an inflection, bounce or pause in the selling was being contemplated more seriously by market participants, it had yet to happen. What transpired in the first quarter of 2019 was a very powerful and quick v-shaped recovery in the S&P 500 index, back to a level above 2800 from a low of around 2350 in late December. The index is up over 20% on a total return basis since 12/24/2018 and is now off less than 4% from the all-time highs. The S&P 500 is up 13.65% for the calendar quarter. Similarly, the Citigroup USBIG Corporate Bond Index performed strongly showing a 5.07% gain quarter-to-date.

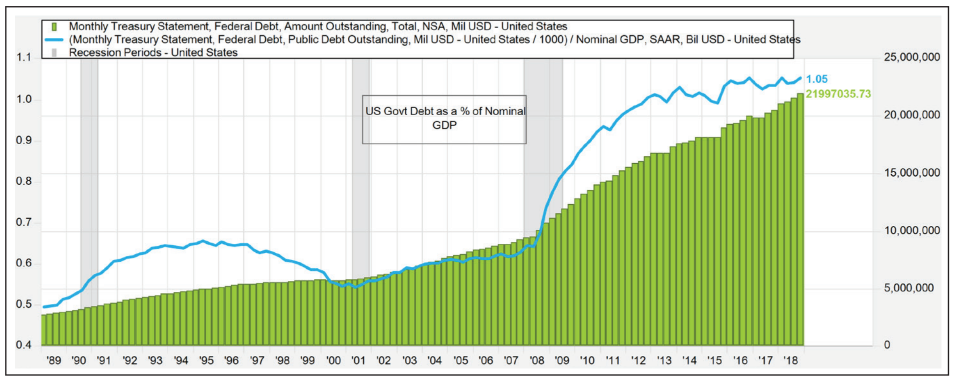
While the softening in the global economy is still playing out, expectations for the first half of this year are more modest for earnings and growth. This market rebound combined with the Fed pausing rate hikes may reduce some of the near term financial stress that had been building late last year. It may not completely eliminate the damage this market volatility has caused in investor psyche, but if the market continues to be resilient from here albeit on softening economic and earnings momentum, it could help extend the consuming and investment patterns and thus the business cycle. Recent softening in consumption and business investment will likely have to trough and see renewed stronger growth to alleviate the worst of the fears about the economy weakening.

The Federal Reserve achieved a lift off from the near zero rate structure of the crisis era. This is attributable in part to the strength of the U.S. economy in 2018 which accommodated higher interest rates. Increasing leverage from this low interest rate era can be seen in the system, mostly in the corporate space as well as the U.S. government debt space relative to GDP levels (See chart). This just means to say that increasing rates were always going to start to impact real outcomes at some point and the Fed appears to have paid attention to the market signals last quarter.

In our view, market symmetry is skewed slightly negative at present until the multitude of catalysts outside the U.S. such as softening global demand, trade issues and Brexit begin to resolve more favorably. What this means is that on balance the immediate fundamental risks to this business cycle are weighing a bit more heavily on market outlooks at the present time and, as a result, some vigilance is required.

| Positive Market Influences | Negative Market Influences |
|---|---|
| • Recent Fed Dovishness<br>• Wages & Employment | • Global Uncertainties<br>• Business Investment<br>• Retail Sales |

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### Positive Market Influences:

- **Recent Fed Dovishness** – The Fed has paused rate hikes and the markets are pricing in very little expectation for further hikes this year. The Fed is also reported to be planning to end its balance sheet tightening in 2019. Amidst reduced inflation expectations, this is positive for risk assets barring a significant further deterioration on real economic outlooks.
- **Wages & Employment** – Average hourly earnings were up about 3.4% YoY in February and the current Labor Force Participation Rate sits at 63.2%, up from its trough of 62.5% in 2015.

### Negative Market Influences:

- **Global Uncertainties** – Trade, waning demand, Brexit negotiations and debt saturation leading to reduced credit growth

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## Analyst Corner

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are all weighing on fundamental outlooks.

- **Business Investment** – Growth in non-defense capital goods, which fuels productivity gains, has slowed since mid-2018 from a run rate north of 8% YoY to something closer to 4% at present.
- **Retail Sales** – Retail Control Group sales grew just 1.1% YoY for the month of December, 3.6% in January and 2.9% in February. This number averages closer to 4% over the longer term, indicating a slowing in consumption growth leading into 2019. Q4 in absolute terms showed a record level of sales and +3.2% growth, but the market meltdown may have negatively impacted growth momentum and confidence overall slowing the data set. Time will tell if consumption strength returns to a stronger footing.

Daniel P. Burchill
*Security Analyst*

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## Don't Get Caught Up in Lifestyle Inflation

April is Financial Literacy Month and is recognized in the United States in an effort to highlight the importance of establishing and maintaining healthy financial habits. No matter what month of the year you begin the path to financial wellness, knowledge and understanding will help you create a more successful overall financial picture.

Successful money management is a process – one we speak of often to help remind us of some of the basics, e.g., budgeting, cutting expenses, obtaining proper insurance coverage and saving for retirement. One of the biggest challenges that people face when it comes to personal financial success is lifestyle inflation.

What is lifestyle inflation? Lifestyle inflation simply refers to an increase in spending in response to an increase in income. That initial response of, "I earned it, so I deserve to spend it," can be tempting – and often the cause of people finding themselves working to just pay the bills. Many people tend to increase their spending upon getting a raise or finding that new job, thinking that a nicer car or a bigger home will surely mean more happiness, and it may for the short-term. But will that purchase truly make you happier if it also brings on higher insurance costs, maintenance and property taxes than you can really afford? Does it support your long-term goals?

To avoid lifestyle inflation, take the time to make conscious, well thought out spending and saving decisions. Calculate the real change an income increase will have on your budget. After taxes and possible additional expenses, such as further travel to the new job, increased child care costs, etc., how much extra money will you truly have to spend? Is it enough to affect your real spending and long-term goals or might you be better off transferring that raise into additional retirement deferrals or to savings?

Often times, curbing that urge to spend does not mean changing your lifestyle. If you are currently living relatively well, more income and more purchases rarely bring on more lasting happiness. Tease them as we may, millennials on average are proving to be more skeptical buyers, often concluding that the fulfillment of an experience or an investment in oneself is more rewarding than ownership of a luxury item. Friendships and activities with people that have similar budgets, interests and philosophies are priceless – and tend to keep us from the throes of lifestyle inflation.

With this month's focus on financial literacy, it's a good time to take control of your financial life. Tomorrows filled by the possibility of achieving financial independence at a younger age, having the financial flexibility to choose a dream job over a higher-paying option and possibly even retiring early, certainly sound more appealing and less stressful than worrying about how you can afford to keep up with the Joneses!

Kelly S. H. Diehr, FPQP™
*Administrative Assistant*

***The highest compliment our clients can give is the referral of their friends and family. Thank you for your trust!***

## Spring Fever Is Calling…How Do You Answer?

The days are finally getting a bit longer, the snowstorms are beginning to subside and I can't help but think about short sleeves and flip flops, drinking lemonade with my kids and riding the blue cruiser bike that I bought for my birthday last year. I will admit, I have a bad case of spring fever and how do I keep it under control for the next few weeks?

We often think of spring as the traditional time of the year for cleaning out closets and drawers and organizing attics and garages, but it is also a great time to review all of your insurance coverages. As important as it is to review your wardrobe, electronics and other personal items to see what needs to be donated, tossed, fixed, updated or stored for the coming months, everyone should be considering a thorough evaluation of their insurance coverage at least once a year.

As the seasons change, so does life and so do your insurance needs. Instead of filing away those policies when they arrive in the mail, take the time to read them over and ask yourself the following questions:

**1. Is my home covered for its full replacement cost?**

Do you have enough coverage to rebuild your home if you suffered a loss? Have you made major improvements to your home, such as adding a new room, enclosing a porch or expanding a kitchen or bathroom? You risk being underinsured if you don't adjust your homeowner's insurance coverage limits.

**2. Do I have enough coverage for expensive items?**

Have you bought or received as a gift any valuable jewelry since you purchased/renewed your policy and when was the last time you had the items you own appraised? Standard homeowners insurance has dollar limits for the theft of certain types of expensive items like jewelry, furs and silverware. This means that the insurer will pay only the amount specified in the policy — generally $1,000 to $2,000. To insure these items to their full dollar value, consider a special personal property endorsement or floater. This coverage includes "accidental disappearance," meaning coverage if you simply lose that item — and there is no deductible.

Remember that items can go up or down in value. Floaters and endorsements are priced on the appraised value of an item or collection, so have periodic reappraisals done to make sure you are purchasing only the amount of coverage you actually need.

The best way to keep track of your belongings and to make sure that they are adequately insured is to create a home inventory.

**3. Do I still need comprehensive/collision on my car?**

If you're driving an older car that is worth less than $1,000 — or less than 10 times the physical damage insurance premium — the optional coverages may no longer be cost effective. Consider saving money on your premium by dropping either comprehensive or collision.

**4. Do I have enough liability insurance to fully protect my assets?**

The liability coverage in standard homeowners and auto policies pay for judgments

*See* **Spring Fever** *on Page 7*

### Spring Fever

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against you and your legal fees, up to a limit set in the policy. However, in our litigious society, you may want to have additional protection — that's what an umbrella liability policy provides. An umbrella policy pays when you reach the limit on the underlying liability coverage in a homeowners, renters, condo or auto policy. If your assets have increased as of late, you'll have more to lose and you may want to consider this extra layer of protection. Many other factors including youthful drivers in your household, pools, watercraft and pets often necessitate the need for increased liability coverage. Be sure you are reviewing this on a regular basis.

**5. What kind of vacation will I be taking this summer?**

If you are taking an expensive, pre-paid vacation or an active vacation such as biking or hiking in an exotic locale, travel insurance can help protect the financial investment in your vacation.

**6. Should I rent out my house during the vacation period?**

Whether you own a second home that you plan to lease or you want to rent out your primary residence through an online service such as Airbnb, your first step should be to call your insurance professional. Depending on the rental scenario, your standard homeowner's policy may not cover losses incurred while your home is rented and you may require a more specialized insurance policy.

Most importantly, whether it's winter, spring, summer or fall, plan an annual review with your agent or contact us at Valicenti Insurance Services, Inc. for a comprehensive review of all of your insurance contracts.

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Suzanne M. Valicenti
*President/CEO*

## First Quarter in Review

On the heels of the Federal Reserve Chairman's reversal on future rate hikes and inflationary fears, equity markets bounced back from the slump in the fourth quarter of 2018. (For further insight of this discussion, see Louis Ruize's article on Page 2.)

The market was led by large capitalized technology stocks, as evidenced by the heavily technology weighted Nasdaq Composite Index (see Market Table). The bond market has recovered as well, as long-term rates for mortgages have retreated and the 10-year Treasury has backed down.

Market prognosticators began forecasting a recession in the near future, as the yield spread on the 10-year and 2-year Treasury notes have come close to zero. This spread reduction has been the result of the Fed going too fast on short-term rates and keeping longer rates also low, while global bonds are at historic lows in developed countries.

Inflation remains low, although wage pressures are starting to pick up. Domestic spending and savings are very healthy in this late cycle economic expansion. Global trade fears have created some uncertainty and volatility in the market. The political landscape will begin to ramp up and create additional volatility when the presidential election "circus" begins.

We are constantly reviewing all the data, both here and afar, to make the best portfolio decisions within your overall goals and objectives. Happy spring from your team at VASI!

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Joseph M. Valicenti
*President/CEO*

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## Taxpayer Reminders

The Internal Revenue Service today reminds taxpayers that the easiest way to check on a tax refund is to use "Where's My Refund?," an online tool available at IRS.gov and through the IRS2Go app. The fastest way to get a refund is to use IRS e-file and direct deposit.

Using the "Where's My Refund?" online tool, taxpayers can start checking on the status of their return within 24 hours after the IRS receives an e-filed return or four weeks after the taxpayer mailed a paper return. The tool has a tracker that displays progress through three phases: (1) Return Received; (2) Refund Approved; and (3) Refund Sent.

All that is needed to use "Where's My Refund?" is the taxpayer's Social Security number, tax filing status (such as single, married, head of household) and exact amount of the refund claimed on the return. The application is updated no more than once every 24 hours, usually overnight, so there's no need to check the status more often.

The IRS issues nine out of ten refunds in less than 21 days. Refunds for those claiming the Earned Income Tax Credit or the Additional Child Tax Credit had to be held, by law, until mid-February. Taxpayers claiming these credits should begin to see their refunds deposited in bank accounts February 27.

Taxpayers should only call the IRS tax help hotline on the status of their refund if it has been:

- 21 days or more since the return was e-filed,
- Six weeks or more since the return was mailed, or when
- "Where's My Refund?" tells the taxpayer to contact the IRS.

Taxpayers who owe should pay as much as possible to minimize interest and penalty charges. Taxpayers should visit IRS.gov/payments to explore their payment options. They can pay online, by phone (telephone numbers available at IRS.gov/payments) or by using their mobile device and the IRS2Go app. Payment options available include electronic funds withdrawal (during e-file), bank account (direct pay), debit or credit card and the Electronic Federal Tax Payment System (EFTPS).

Taxpayers unsure of the amount that they owe can visit IRS.gov/account and, when logged in, they can view their balance, payment history and can make a payment.

It's especially important in 2019 for taxpayers who had an unexpected result when they filed their 2018 tax return to perform a "paycheck checkup" now to determine whether the right amount is being withheld for their 2019 taxes. Taxpayers who do need to adjust their withholding should submit a 2019 Form W-4, Employee's Withholding Allowance Certificate, to their employer as soon as possible.

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