HUDSON ADVISOR SERVICES, INC

OUR VIEW OF THE MARKET

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This time last year we were sleeping like babies. The market had ended a banner year in 2017 and was starting 2018 strongly. In contrast, we are now waking up every hour. The market gyrated markedly in 2108 and the fourth quarter was among the most dismal in modern stock market history. Looking ahead to 2019, we are quite uncertain about how events will unfold. We are in anxious times – and that peaceful sleep eludes us.

That said, we are encouraged by positive signs. The U.S. economy is slowing – but will still see healthy growth in 2019. We recognize that recession is inevitable in some future year. But we think it unlikely to happen in 2019. (See article on page 3 regarding the history of recessionary impacts on the stock market.) The recent decline in stock prices has brought equity valuation more in line with historical averages. Unlike 2008, there are few signs of structural risk in the financial system.

From the negative, the market faces what many analysts call "strong headwinds." The policy of the Federal Reserve and other central banks is less accommodative. Trade tensions with China could be prolonged. The economic impact is unpredictable. Corporate earnings will slow considerably in most sectors. Politics in Washington will be conflicted and gridlocked. The federal deficit is expanding at alarming rates.

On balance, we expect the markets to be turbulent in 2019. But we think it can muddle through to be a year of modest gains. We will be talking with each of our clients about objectives and risk tolerance. We expect to advise many clients to reduce their equity exposure and to prepare for volatile periods. At the same time – as always – we will be looking for stocks with future growth potential.

MARKET TRENDS

The accompanying chart summarizes stock and bond market prices for the fourth quarter and full-year 2018. It was a roller coast year in the stock market and relatively more stable in the bond market.

Equity Market: Stocks soared in January, fell back in February and March, recovered well in the second and third quarters, and reached record levels in September. Then anxiety struck in the fourth quarter over rising interest rates and "trade wars" and the potential effect on corporate earnings. It ended being the worse year since 2008.

The Dow Jones Industrial Average was down 12.48% for the fourth quarter and 7.22% for the year. The S&P 500 was down 13.97% for the quarter and 6.24% for the year. Technology stocks were especially slammed. The Nasdaq Composite lost 17.54% for the quarter and 3.88% for the year. Similarly hard hit were the small cap stocks with the Russell 2000 index down 20.51% for the quarter and 12.18 % for the year.

Fixed Income Market: The bond market had been relatively stable in the first half of the year, but bond prices took a strong hit as investors accepted the reality of rising interest rates and potentially steeper inflation. The yield on the 10-year Treasury was 3.05% at the end of September – versus 2.41% at the beginning of the year. (Yields move inversely to prices.) But bond prices gained again in the fourth quarter as the stock market suffered and the yield was 2.68% at year's end.

MAJOR MARKET INDEXES

	2018 Return
Dow Jones Industrials Composite PR	-7.22
S&P 500 Index PR	-6.24
Russell 2000 Index PR	-12.18
NASDAQ Composite PR	-3.88
EAFE Index NR	-13.79
Barclays Aggregate Bond Index TR	0.86

source: Morningstar®

THE OUTLOOK

The Economy: The booming U.S. economy is clearly starting to slow. Annualized growth in the third quarter of 3.4% is expected to fall to 2.6% in fourth quarter. Overall growth for the year is expected to be about 3%.

Much of the recent nervousness in the stock market is based upon fears that the economy could slide quickly into a recession. That is not our view at Hudson Advisors. We are encouraged by the December employment report which showed net gain of 312,000 jobs – almost double the expectation – and one of the strongest in a decade. The tight labor market has generated year-over-year wage growth of 3.2%. Most surveys of consumer and small business confidence are positive.

We accept the viewpoint that the U.S. GDP will grow in the range of 2% to 2.5% in 2019. This slowdown is driven by the fading impact of the Trump tax cut and by economic pauses in China and the actual recession now hitting Europe. But growth over 2% is still healthy by the record of the past decade. That said, we will be watching the news on two key fronts:

The first is Federal Reserve policy. The Fed has articulated a clear intent of restoring interest rates to more normalized levels. They raised rates four times in 2018 and had previously planned three increases in 2019: bringing them to a level of 3.3%. However, Chairman Powell has now modified that objective and signaled flexibility. Inflation is still under 2% -- which removes some pressure for rate increases – and Powell says the Fed will watch economic conditions before acting.

The second is the trade talks with China. Should trade conflicts widen, the resultant slowdown in the global economy could have an impact on the U.S. larger than what the Trump tariffs create. Conversely, some kind of positive agreement would boost economic confidence.

The Market: On the positive side, the recent market correction has made equity valuations look more reasonable. The forward 12-month P/E ratio for the S&P 500 is now 14.2 versus the 5-year average of 16.4 and the 10-year average of 14.6. On the negative side, corporate earnings growth for full-year 2019 is expected to be below 10% versus 20.3% for full-year 2018.

Thus, on balance, we think the market will show modest single digit gains in 2019. But we expect turbulence as the news on Federal Reserve actions and the trade talks unfold. The market will be buoyed if the Fed keeps rates lower and the Trump Administration somehow reaches a trade agreement with China. Conversely, higher rates and failure in the trade talks could sink the market lower. We do not anticipate peaceful sleep in the months ahead.

OUR STRATEGIES

Asset Allocation: Normally, for clients investing new money, we recommend 60% allocation to equities and the remaining portion to cash, bonds with maturities under two years, and alternative investments. But in this environment, we may recommend a lower allocation to equities until the market direction is somewhat clearer.

Preferred Equities: We remain focused on large cap companies with strong balance sheets, sustainable cash flows, and credible business models. Companies that pay attractive dividends are central to our strategy. Some of the sectors getting our attention:

TECHNOLOGY: We are cautious about this sector – especially given the declines in the big tech names – but areas such as bio technology and semi- conductors have our interest.

FINANCIALS: Our focus is upon regional banks. Prices are reasonable for many of these bank stocks.

CONSUMER STAPLES: We are looking at companies in this sector because it has value stocks with good future potential.

ENERGY: This sector has been battered – but the potential for upside movement is good.

Other Investments: Our repeated aversion to bonds with long maturities remains firm. We still believe the risk of a sharp decline in prices is too great a risk for our clients. We prefer to find alternative investments such as real estate limited partnerships, demand notes, and municipal tax liens. We also are investigating Qualified Opportunity Zone Funds, a new investment opportunity to spur economic development in certain designated areas.

Dow Jones U.S. Sectors Total Return
(Percent Change for YTD, Ending December 31, 2018)
Source: Morningstar®

Oil & Gas	**-18.91**	**Consumer Services**	**2.07**
Basic Materials	**-16.17**	**Telecommunications**	**-6.73**
Industrials	**-11.26**	**Utilities**	**4.37**
Consumer Goods	**-13.40**	**Financials**	**-8.98**
Health Care	**6.25**	**Technology**	**-0.63**

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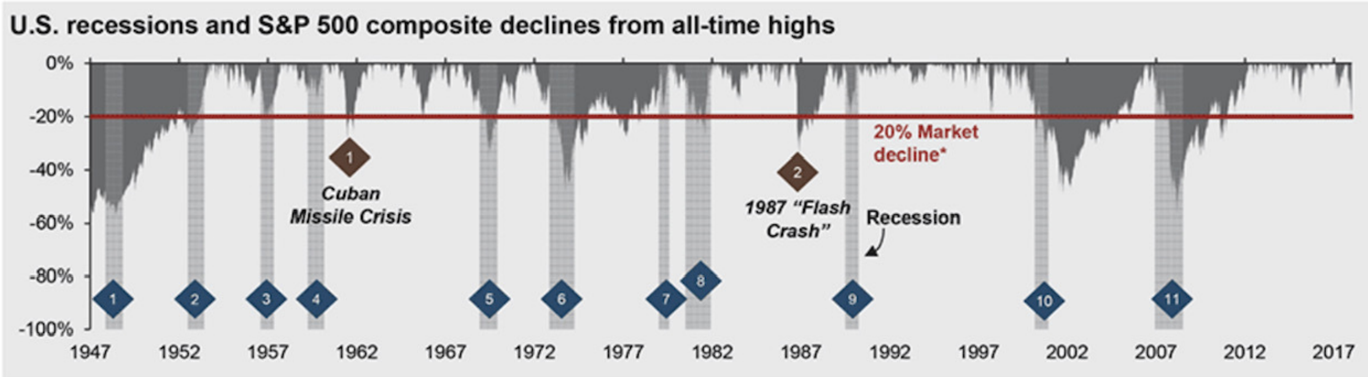
RECESSIONS AND STOCK MARKET CORRECTIONS



Characteristics of recessions and related stock market declines

Recession	Recession: Peak Quarter	Recession: Trough Quarter	Recession: % Decline	Related Market Sell-off: Peak Date	Related Market Sell-off: Trough Date	Related Market Sell-off: % Decline	Macro Environment: Commodity Spike	Macro Environment: Aggressive Fed	Macro Environment: Extreme Valuations
1 Recession of 1949	4Q48	4Q49	-1.5%	6/15/1948	6/13/1949	-21%			◆
2 Recession of 1953	2Q53	2Q54	-2.4%	1/5/1953	9/14/1953	-15%			
3 Recession of 1958	3Q57	2Q58	-3.0%	8/2/1956	10/22/1957	-22%			◆
4 Recession of 1960-61	2Q60	1Q61	-0.1%	8/3/1959	10/25/1960	-14%			◆
5 Recession of 1969-70	4Q69	4Q70	-0.2%	11/29/1968	5/26/1970	-36%		◆	
6 Recession of 1973-75	4Q73	1Q75	-3.1%	1/11/1973	10/3/1974	-48%	◆		
7 Recession of 1980	1Q80	3Q80	-2.2%	2/13/1980	3/27/1980	-17%	◆	◆	
8 Recession of 1981-82	3Q81	4Q82	-2.5%	11/28/1980	8/12/1982	-27%		◆	
9 Early 1990s recession	3Q90	1Q91	-1.4%	7/16/1990	10/11/1990	-20%	◆	◆	
10 Early 2000s recession	1Q01	4Q01	-0.4%	3/24/2000	10/9/2002	-49%	◆		◆
11 Great Recession	4Q07	2Q09	-4.0%	10/9/2007	3/9/2009	-57%	◆	◆	
Non-recession Bear Markets									
1 1962 flash crash, Cuban Missile Crisis	-	-	-	12/12/1961	6/26/1962	-28%			◆
2 1987 flash crash, program trading, overheating markets	-	-	-	8/25/1987	12/4/1987	-34%			◆
Average	-	-	**-1.9%**	-	-	**-30%**			

Source: FactSet, NBER, Robert Shiller, Standard & Poor's, J.P. Morgan Asset Management.
*A bear market is defined as a 20% or more decline from the previous market high. The related market return is the peak to trough return over the cycle. Periods of "Recession" are defined using NBER business cycle dates. "Commodity spikes" are defined as movement in oil prices of over 100% over an 18-month period. Periods of "Extreme Valuations" are those where S&P 500 last 12 months' P/E levels were approximately two standard deviations above long-run averages, or time periods where equity market valuations appeared expensive given the broader macroeconomic environment. "Aggressive Fed Tightening" is defined as Federal Reserve monetary tightening that was unexpected and/or significant in magnitude. Bear and Bull returns are price returns.
Guide to the Markets – U.S. Data are as of December 31, 2018.

J.P.Morgan Asset Management

The chart above shows the 70-year history of the relationship between recessions and corrections in the stock market. There have been 11 such events in that 70-year period. Here are some key learning points:

- Recessions tend to be short-lived events with moderate decline in Gross National Product. The declines have ranged from -0.1% to -4.0% -- with an average of -1.9%.
- The related sell-off in the stock market has ranged from -15% to -57% -- with an average decline of -30%.
- Not shown in this chart is the key point that stock markets have always recovered and surpassed declines brought on by recessions. The most recent example is the so-called "Great Recession" of 2008-09. The stock market started to recover in the second half of 2009 and has grown 302% in the period since.

We always tell our clients at Hudson Advisors that the economy is cyclical and recessions are inevitable. But they are not a reason to panic and to withdraw from equity investments. Stay the course and positive returns will follow.

Top 25 Performing Stocks 2018 - US Listed companies with a market cap above $5 Billion. Source: Telemet ®

Issue	Name	Last	Mkt Cap	Net Pct YTD	Industry Group
TWLO	Twilio Inc	97.88	9,676	278.39	IT Services
DTSRF	Digital Shelf Space Corp	0.27	14,356	190.66	
TTD	Trade Desk, Inc.	125.12	5,410	153.79	IT Services
OKTA	Okta, Inc.	67.5	7,342	149.12	IT Services
WWE	World Wrestling Entertainment	80.39	6,272	145.91	Entertainment
ETSY	Etsy, Inc.	52.03	6,267	132.62	Internet & Catalog Retail
PDD	Pinduoduo Inc. ADR	23.17	21,305	124.85	Diversified Consumer Services
CIG/C	Companhia Energetica de Minas	4.11	5,172	112.81	Electric Utilities
CIGXC	Companhia Energetica de Minas	4.11	5,172	112.81	Electric Utilities
DXCM	DexCom, Inc.	131.47	11,680	108.75	Health Care Equipment & Supplies
SRPT	Sarepta Therapeutics Inc	107.01	7,151	96.14	Biotechnology
TEAM	Atlassian Corporation Plc	94.64	22,348	95.47	Software
AMD	Advanced Micro Devices	20.27	20,260	79.57	Semiconductors and Semiconductor Equipment
REDW	Redwood Financial, Inc.	70.01	33,718	74.44	
HLF	Herbalife Nutrition Ltd.	59.24	9,248	74.1	Personal Products
ABMD	Abiomed Inc.	309.83	13,955	73.44	Health Care Equipment & Supplies
DATA	Tableau Software Inc.	126.46	10,568	73.41	Software
ZEN	Zendesk, Inc.	61.71	6,605	72.49	Software
HAE	Haemonetics Corporation	99.32	5,133	72.26	Health Care Equipment & Supplies
KL	Kirkland Lake Gold Inc.	25.21	5,418	70.45	Metals & Mining
RNG	Ringcentral Inc.	87	6,989	70.33	Wireless Telecommunication Services
LOXO	Loxo Oncology, Inc.	231.54	7,088	66.39	Biotechnology
SWTUY	Swedish Orphan Biovitrum ADR	22.67	6,102	63.02	
IDTI	Integrated Device Technology	48.22	6,221	62.9	Semiconductors and Semiconductor Equipment
CIEN	Ciena Corporation	35.81	5,604	62.02	Communications Equipment

Bottom 25 Performing Stocks 2018 - US Listed companies with a market cap above $5 Billion. Source: Telemet ®

Issue	Name	Last	Mkt Cap	Net Pct YTD	Industry Group
EQT	EQT Corporation	20.01	5,091	-66.6	Oil Gas & Consumable Fuels
COTY	Coty, Inc.	7.49	5,626	-64.5	Personal Products
SNAP	Snap Inc	6.08	7,873	-62.29	Communications Equipment
FNMA	Fannie Mae	1.36	7,793	-60	Thrifts and Mortgage Finance
MHK	Mohawk Industries Inc	125.5	9,312	-57.61	Household Durables
DB	Deutsche Bank AG	8.7	11,996	-56.46	Capital Markets
ECA	Encana Corp	6.4	5,418	-56.19	Oil Gas & Consumable Fuels
IRS	IRSA Inversiones Rep	13.52	7,828	-55.88	Real Estate Management & Development
PRGO	Perrigo Company	44.21	6,006	-54.67	Pharmaceuticals
GE	General Electric Company	8.6	74,804	-54.5	Industrial Conglomerates
LB	L Brands, Inc.	29.11	8,009	-53.39	Specialty Retail
AMG	Affiliated Managers Group	102.32	5,389	-51.94	Capital Markets
LOMA	Loma Negra Compania Industrial	11.44	6,815	-51.69	Construction Materials
WDC	Western Digital Corp.	38.47	11,134	-51	Computers & Peripherals
IVZ	Invesco Ltd.	17.5	7,198	-50.93	Capital Markets
AA	Alcoa Corp	28.63	5,339	-50.66	Metals & Mining
JD	JD.com, Inc. ADS	22.62	32,726	-49.47	Internet & Catalog Retail
PPDF	PPDAI Group Inc	3.84	6,226	-49.37	Thrifts and Mortgage Finance
XEC	Cimarex Energy Co	66.72	6,379	-49	Oil Gas & Consumable Fuels
BTI	British American Tobacco ADR	31.74	59,132	-48.39	Tobacco
DISH	DISH Network Corp cl A	28.57	13,361	-47.71	Media
CTTAY	Continental Ag	14.58	5,832	-47.41	Auto Components
IPGP	IPG Photonics Corporation	117.2	6,258	-47.09	Electronic Equipment & Instruments
PCG	PG&E Corporation	19.07	9,891	-47.02	Electric Utilities
PE	Parsley Energy, Inc. Class A	17.82	5,643	-45.72	Oil Gas & Consumable Fuels