Matt's Market Update

IN THIS REPORT

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Market Review

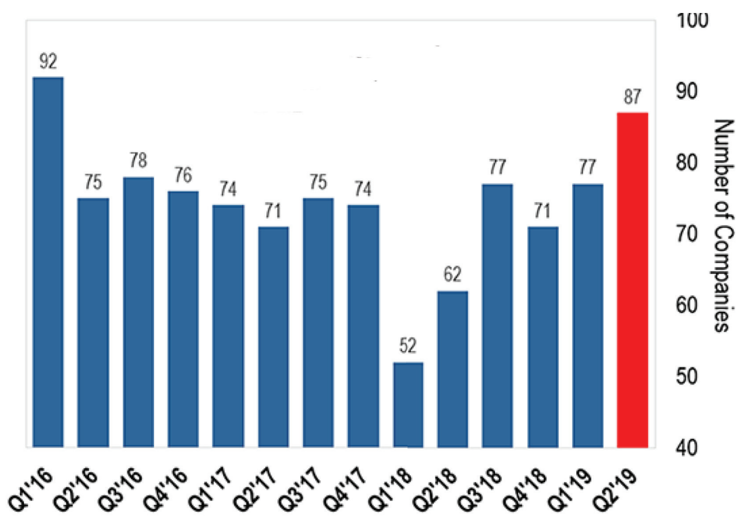
Q2 was another positive quarter for the major global equity benchmarks, but it wasn't without drama in the middle as the month of May saw across the board declines of -6% to -8%. May was the first negative month for the major U.S. equity averages in 2019 and especially hard on the large-cap technology companies. The NASDAQ index was the hardest hit with a loss of -7.93% for May. Profit taking after four strong months to open the year was blamed in part on increasing trade tensions in the U.S. vs. China dispute. In June, equities quickly reversed course higher to salvage a positive quarter. The S&P 500 index has posted a total return of +18.5% YTD through 6/30/19, the index's best performance at the half-way point of the year since 1997, when the stock index was up +20.6% YTD (total return) as of June 30th.

Much of the equity rally seems to have been inspired by the Federal Reserve hinting that interest rate cuts are on the way in the second half of the year. This is a flip-flop from the Fed that as recently as December was forecasting more rate hikes for 2019. The quarter also saw a continuation of the trends that have been in place for quite awhile, namely the U.S. equity markets outperforming foreign competitors. Also, the wide disparity between the Growth and Value equity styles of investing continued, with the former continuing to far outpace the latter in Q2 performance.

Interest rates across the treasury curve continued to decline in June. For Q2, 2-year treasury yields fell by 53 basis points (bp), the 10-year fell 41 bp and the 30-year fell 29 bp. The decline in rates inspired a large rally in bonds with the Bloomberg Barclay's Aggregate index posting a total return of 6.11% YTD. If asked six months ago, this figure is far in excess of the return we would have speculated could be achieved by the index for all of 2019. While the Fed didn't cut interest rates at their June meeting, the market is expecting multiple rate cut announcements in the second half of the year. At quarter-end, the market was pricing in a 100% probability of a cut in rates at the July Fed meeting.

While the Fed, trade wars and politics have dominated the market moving headlines in 2019, there's very little talk about what is typically the market's primary concern: corporate profits. In fact, you could legitimately say we're now in an earnings recession. Consider the following stats from Gluskin Sheff research: At the end of Q1 2019, year over year (YOY) profits for the S&P 500 showed a net decline of -0.3%. This compares to market expectation of +3.5% YOY growth at the beginning of the year. With Q2 earnings season now underway, the expectation is for a -2.6% YOY decline in profits. This is borne out with the chart on the next page highlighting the number of earnings warnings (companies instructing the market to expect less in earnings per share than expected) are at their highest level in two years. Looking at current forecasts for Q3, S&P 500 profits are currently expected to be slightly negative YOY as well at -0.5%. This figure

S&P 500 COMPANIES REDUCING EARNINGS GUIDANCE
87 companies have reduced earnings guidance this quarter... the most since Q1 2016



Source: FactSet

may prove optimistic three months from now if the current trend in the chart continues. Needless to say, it's a fascinating contrast to see the S&P 500 index trading at all-time highs at quarter-end with the strong likelihood of three consecutive quarters of negative YOY earnings growth.

Money Flowing to ESG

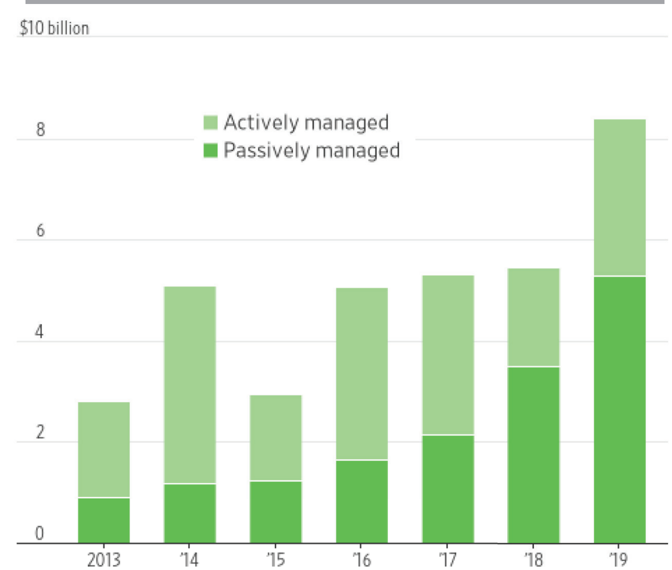
While actively managed funds (strategies based on a manager trying to beat a benchmark through stock picking) have been losing assets in recent years to low cost index funds, the ESG fund segment of the active world is displaying strong growth. The acronym ESG stands for Environmental Social and Governance factors, which are applied by the managers when screening for companies to hold in their portfolios. You may already be familiar with another acronym, SRI, which stands for Socially Responsible Investing. While both are broad in scope, ESG is essentially the next generation of socially responsible funds where managers are willing to consider any company for investment that meets their specific ESG criteria. This is a more nuanced approach compared to SRI funds which would automatically exclude certain companies from potential investment based on the industry classification. As you can see from the chart on this page, recent growth for ESG funds (both active and passively managed) has been impressive. According to Morningstar, ESG funds have already received net flows of $8.4 billion in 2019. This amount is far higher than the just achieved record for annual net flows of $5.4 billion in 2018.

Also according to Morningstar, 37 new U.S. based ESG funds launched in 2018, while an additional 63 funds changed their prospectus to include ESG criteria to their prospectus. This resulted in a 50% increase in the number of available ESG funds. You may wonder are clients of Sentinel using ESG funds? In some cases, yes, typically in response to an investment committee's desire to have an option in the plan related to social or ESG investment criteria. It's important to note that the inclusion of any ESG fund in a retirement plan must be in line with the criteria and guidelines set in the plan's investment policy statement. In other words, these types of funds must be viewed through the same lens as the other plan investments with no special allowances made for the fact that it follows ESG criteria.

DC Trends from Vanguard

Defined Contribution (DC) retirement plans are the main source of savings for most Americans. More than 100 million plan participants are covered by DC plans with assets greater than $7.5 trillion. Vanguard

CHASING GREEN
Net flows into ESG funds



Note: 2019 is through June 30
Source: Morningstar

recently released their 18th annual edition of "How America Saves", a survey focused on retirement savings habits. The data is pulled from the 5 million participants covered by their defined contribution record keeping business. This report is full of interesting stats and trends that plan sponsors may find helpful in making sure their plans are keeping up with the competition. Here are some of the key takeaways from the report:

- 48% of all Vanguard plans used auto-enrollment by the end of 2018. This compares to roughly 16% at year-end 2007.

- Two-thirds of the auto-enrollment plans have also added the auto-escalation feature, which increases the deferral rate for those auto-enrolled participants on an annual basis for a set amount of time. For example, a participant initially enrolled at a 3% deferral rate in year one would see this rate increased to 4% in year two, 5% in year three, etc. until a max deferral rate set by the plan sponsor is met in the future.

- Plans with auto-enrollment have an average participation rate of 91% versus just 60% for those plans with voluntary enrollment.

- The Roth 401(k) feature was included in 71% of Vanguard plans at year-end 2018. Only 11% of participants in these plans signed up for the Roth.

- At year-end 2018, nine out of ten plan sponsors offered target date funds in their plans. This was up from one-third of plans offering them in 2008.

- While 77% of participants use a target date fund, two-thirds of these participants have their entire balance invested in a single target date fund.

These are but a small sample of the findings. The report is easily accessible online for those looking for more in-depth analysis.

Wealth Management Corner

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As people are living longer, the likelihood of a long-term care (LTC) event during their lifetime is pretty high. Most of us are aware that the costs associated with nursing-home stays and assisted living facilities can be quite expensive, yet how many of us have a plan in place to address this? Are you financially prepared to cover the expenses related LTC costs?

According to the American Association for Long-Term Care Insurance, there is over a 50% chance people age 65 and older will need some type of long term care service in their lifetime.[1] The national average for a private room in a nursing home is $97,455 annually and the typical stay is just under 3 years.[2] This cost can be substantially higher in the northeast portion of the United States where such costs are generally closer to $150,000 annually.[2] Manhattan is one of the highest costs, averaging around $215,7702 per year. As you can imagine, even the strongest financial plans can collapse very quickly if long term care is not properly addressed.

The question now becomes "How will I pay for long-term care and what options are available to me?" One option is to 'self-insure.' This option typically is not feasible as most people do not have the resources available to do so. Some people depend on family members to care for them. This "solution," however, can dramatically impact the caregivers quality of life both financially and emotionally while frequently causing great strain on the relationship. Another option would be to review your employer-provided benefits and determine if a group LTC benefit is available at work. With less than 0.5% of businesses offering LTC coverage[2], it is unlikely this benefit will be available.

For those who desire more financial certainty in life, obtaining LTC insurance when you are able to qualify for coverage may be the most effective way to proceed. The two main types of coverages available are standalone LTC policies or hybrid policies. The standalone option may work assuming your life insurance needs are in order and you are comfortable with the use it or lose it approach. If you never require services, there is no benefit to you, similar to the way an auto or homeowners insurance policy operates. The other insured solution is a hybrid policy. Hybrid coverage addresses both the LTC need and also the "use it or lose it" issue. With the hybrid option, you are purchasing a life insurance policy with a LTC rider. Throughout your lifetime if you experience a LTC event, this type of policy should respond and assist you with paying long term care expenses by reducing the face amount of the policy. Any remaining portion not used for LTC in your lifetime will be paid to a beneficiary at your passing.

Consumers tend to prefer this option as the policy will always provide either a LTC benefit or death benefit to their beneficiary. The bottom line is that long-term care costs are both real and expensive and continue to be a major concern for people everyday. We recommend reviewing your situation with your financial planner as early as possible so that you can make the best decision for you once you have all the facts.

Our Portfolio Strategy & Allocation Outlook

We made two small changes within our wealth management portfolios in Q2. First, we removed one of our active equity managers who had recently been underperforming. Specific to this manager, their two main strategies were to be long stocks with cheap valuations while also shorting (or betting against stocks) with excessive valuations. While this strategy had stood test of time, it has been contrary to everything that has been working in the stock market in 2019. So, we decided to redeploy this capital elsewhere in the portfolio. Second, as our conviction that interest rates will go lower from here (or at least stay in this very low range) has grown, we decided to move away from an ETF position that benefits from rising interest rates. We simply see better opportunities elsewhere in the fixed-income landscape as the expectations for rising interest rates have essentially vanished in 2019.

There have been major changes to the market consensus in just the past six months. Consider the following:

- The Fed has completely shifted its stance from favoring future rate hikes to now preparing the market for multiple rate cuts.
- Global trade tensions have never been higher after most thought a U.S. / China trade deal would have been worked out by now. Of course, this still may happen in 2019, but the sides still seem worlds apart.
- Global economic growth risks are on the rise as evidenced by the slowdown in U.S. earnings growth this year and the inability of many foreign nations to kick start growth.
- The dramatic rise in equities this year has been welcomed by investors, but valuations are back to the high levels last seen in September 2018. How much higher can valuations stretch without the support of strong earnings?

Considering the many cross currents in the market right now, it's not the time for making large portfolio bets. Overall, we're satisfied with how our portfolios and underlying managers have performed at the midway point of the year. Our weightings to each asset class are in a neutral range at quarter-end. The second half of the year will no doubt be interesting.

Please let us know if you'd like to discuss your personal investing and financial planning needs.

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Market Scoreboard

Index Returns (%)	Q2 2019	YTD	1 Year	3 Year	5 Year	10 Year
S&P 500	4.30	18.54	10.42	14.20	10.71	14.70
DJIA	3.21	15.40	12.20	16.82	12.29	15.03
NASDAQ	3.58	20.66	6.60	18.26	12.68	15.87
Russell 2000	2.10	16.89	-3.31	12.31	7.06	13.45
MSCI ACWI Ex USA	2.98	13.60	1.29	9.39	2.16	6.54
Barclays Aggregate Bond	3.08	6.11	7.87	2.32	2.95	3.90
Bloomberg Commodity TR	-1.19	5.06	-6.75	-2.18	-9.15	-3.74

Source: Morningstar

Sentinel Benefits
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[1] http://www.aaltci.org/long-term-care-insurance/learning-center/ltcfacts-2019.php
[2] https://www.morningstar.com/articles/879494/75-mustknow-statistics-about-longterm-care-2018-ed.html

S&P 500 TR: A market capitalization-weighted index of 500 widely held stocks often used as a proxy for the large-cap segment of stock market.

Russell 2000 TR: Consists of the smallest 2000 companies in the Russell 3000 Index, representing approximately 7% of the Russell 3000 total market capitalization often used as a proxy for the small-cap segment of the stock market.

Barcap Aggregate Bond TR: The Barclays Capital Aggregate Bond Index is a market capitalization-weighted index, meaning the securities in the index are weighted according to the market size of each bond type. Most U.S. traded investment grade bonds are represented. The index includes Treasury securities, Government agency bonds, Mortgage-backed bonds, Corporate bonds, and a small amount of foreign bonds traded in U.S.

MSCI EAFE NR USD: Widely accepted as a benchmark for international stock performance, the EAFE Index is an aggregate of 21 individual country indexes that collectively represent many of the major markets of the world.

DJ US Industrials TR USD: Computed by summing the prices of the stocks of 30 U.S. companies and then dividing that total by an adjusted value--one which has been adjusted over the years to account for the effects of stock splits on the prices of the 30 companies.

NASDAQ: Measures the performance of all issues listed in the Nasdaq Stock Market and is often used as a proxy for the large-cap technology segment of the U.S. stock market.

DJ/UBS Commodity: The DJ-UBSCI is composed of futures contracts on physical commodities and is often used as a proxy for broad-based exposure to the commodity markets.

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