Johnson Private Client Group | Johnson Trust Company | Johnson Institutional Management

Fourth Quarter 2018

Letter from the President

Nearly a decade into this historic bull market run, the S&P 500 Index posted its first calendar-year loss since 2008, finishing with a total return of -4.4%. This modest decline seems far worse after the fourth-quarter selloff. By late September the market had gained 11% for the year before market sentiment shifted dramatically. In the ensuing months stocks dropped 19% to the Christmas Eve lows before recovering nearly 7% in the final week of trading. Volatility is the norm rather than the exception, but this environment was unusual in a number of ways.

First, it is unusual for so many asset classes to have negative returns in a given year, as typically there are several safe-haven assets that will benefit from a flight to safety. Investment-grade bonds were able to eke out meager positive returns, but nearly 90% of all asset classes posted a negative return in 2018, the largest percentage since 1920. It was also surprising that stocks were weak in a year when corporate earnings growth was greater than 20%. Over the last 50 years, this rare dichotomy has occurred just three times.

The market volatility is primarily a reflection of growing uncertainty about the outlook for the global economy. The U.S. economy has shown signs of modest slowing, but outright recessionary signals are not evident. We expect the volatility to extend into early 2019 as investors monitor the impact of tariffs, ongoing trade talks, the health of foreign economies, and Federal Reserve policy.

While we did take steps throughout the year to position portfolios for the possibility of increased volatility, we continue to manage portfolios with a long-term view. We focus on higher-quality investments that perform well relative to the market at this stage in the economic cycle. We are finding good value today as many quality stocks are as attractively-priced as they have been in a number of years.

In addition to our efforts related to investment management, we continue to invest in an enhanced client-service experience. Ultimately, it is our people that make the difference. We added more talented professionals to our team in 2018 and now have over 130 dedicated people at your service. Our goal is to surround clients with a team that can deliver investment expertise and integrated wealth management services.

Our firm has always placed a high value on continuous improvement and innovation. To that end we have continued to invest in technology. In January, we will be unveiling a newly-branded website and client portal. In addition to a better look and enhanced functionality, the new client portal will include enhanced security measures. Keeping client information confidential is one of our highest priorities. We have also been upgrading our technological infrastructure behind the scenes. We have adopted several new software packages and tools, all of which will enhance the quality of our service to you.

Featuring

TOTAL RETURNS

	4Q2018	2018
S&P 500	-13.5%	-4.4%
Dow Jones Industrial Average	-11.3%	-3.5%
NASDAQ	-17.3%	-2.8%
Russell 2000	-20.2%	-11.0%
MSCI EAFE (International)	-12.5%	-13.4%
Barclays Aggregate Bond Index	1.6%	0.0%

Thank you for the opportunity to be of service and for your continued confidence in us. We are honored to serve you and look forward to partnering with you in the years ahead.

Thank you,

Jason O. Jackman, CFA, President

JOHNSON INVESTMENT COUNSEL

Market Update

Fourth-Quarter Selloff Erases 2018 Gains

Stocks ended 2018 with a resounding thud, dragging returns from peaks of double-digit gains into negative territory for the first time since 2008. The S&P 500 fell nearly 7% in October, and November's 2% gain was followed by the worst December since 1946, with a loss of 9%. The full-year losses for the S&P 500 and the Dow Jones Industrial Average were still in the low-single digits thanks to gains in the first nine months. The numbers would have been worse were it not for a record day on December 26th. The Dow notched its first-ever 1,000-point gain, boosting the index over 5% in a single day. The final week of the year added more than 7% to the index.

The fourth-quarter weakness was broad. Stocks fell around the globe, especially those of tech companies. Tech experienced a massive reversal after leading the market higher through September. Earlier gains helped it finish third among sectors for the full year, behind health care and utilities stocks. Cyclical stocks like energy and materials were also big losers.

Mid cap and small cap stocks were hit even harder than large cap. The Russell 2000 Index of small-cap U.S. stocks fell into bear market territory, losing more than 20% from the peak. International stocks fared even worse than the U.S., especially those of emerging markets.

Unusual Weakness across Asset Classes

Stocks weren't the only losers. Rising oil output and fears of slowing demand pummeled oil prices. After rising earlier in the year, the price of a barrel of crude fell 38% from October through December, leading to a full-year decline of 25%. Prices of other commodities also fell as a result of fears of a global slowdown. With so many asset classes in the red, 2018 will go down as a year in which "cash was king."

For the full year, bonds were generally flat. Typically bonds would provide positive returns in a year when stocks are negative. The first nine months brought rising interest rates, which left most indices in negative territory coming into the fourth quarter. The stock market selloff led to positive returns for bonds in the fourth quarter, bringing the full-year total returns roughly to even. Municipal bonds finished with slightly positive gains for the full year.

Markets at Odds with Fundamentals

2018 will be remembered as a year when market behavior was out of step with the underlying fundamentals. The volatility spike in the fourth quarter was largely a function of a shift in investor sentiment as opposed to declines in the actual data. While the global economy is showing some signs of slowing, there is little evidence that a global recession is imminent. This is particularly true in the U.S. economy. GDP rose at the fastest pace since 2011, and economic readings are still healthy for the most part. Corporate earnings per share also grew at the fastest pace since 2011, with revenues and margins both exceeding expectations throughout the year. The divergence of market prices from earnings led to a steep drop in valuation. The price-to-earnings (PE) ratio based on next-twelve-months earnings forecasts finished 2017 at 20.0, but fell to 15.4 by the end of 2018. This divergence between prices and fundamentals is a sign of weakening investor optimism about the outlook for 2019. Investors fear the best may be behind us for the economy and stocks. At the same time, this steep drop in valuations creates room for additional gains in 2019 should fundamentals stabilize or resume their upward trend.

Investors Focused on Shifts in Policy

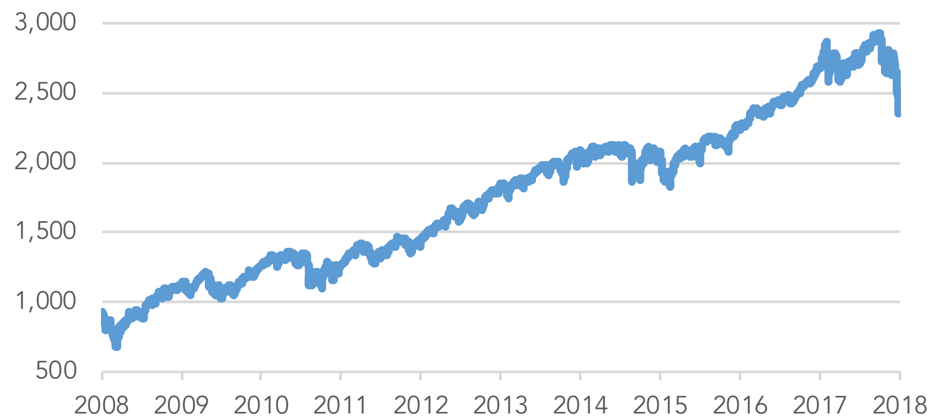
Adding to the concern are several shifts in the policy backdrop. The passage of tax reform in late 2017 gave a one-time boost to corporate earnings growth numbers heading into 2018. With a full year behind us, the bar will be higher for corporations to grow their earnings in the year ahead. Analysts are still predicting growth, but the rate of expansion is expected to be lower than 2018.

Fed commentary exacerbated the volatility in late 2018, as investors were on edge regarding monetary policy. Central banks worldwide have been withdrawing stimulus, and attempting to do so without causing a hard landing for the economy. The Fed raised its benchmark rate several times in 2018, but late in the year backed off some of its earlier hawkish commentary regarding 2019. This was a main reason the market leapt higher in the final week of trading.

Meanwhile, the ongoing trade negotiations continue. They have produced little in the way of landmark agreements, but the concern around this issue has decreased as both sides have shown more willingness to bend. U.S. and Chinese leaders resumed talks in the first weeks of the New Year.

The U.S. political drama has also picked up. The Democrats won back the House in November, and since then have locked horns with President Trump. The federal government partially shut down after a dispute over funding a border wall prevented passage of a budget bill to fund the government. With Congress split, 2019 is unlikely to produce significant policy

S&P 500 Index - Last 10 Years



Source: Factset

shifts, and attention is turning to the 2020 presidential election. Divided government has often proved beneficial to stocks, but political forces are unlikely to be a major driver of returns in 2019 relative to economic and earnings growth.

New Year, Same Disciplined Strategy

The fourth quarter of 2018 was unnerving for many investors. Sharp spikes in volatility and broad weakness in asset prices are always uncomfortable, especially when it comes on the heels of nearly a decade with very little of it. This is why it is crucial to remember that volatility is the norm and not the exception. The years of calm, upward-trending markets that we have seen in the past decade are unusual. Over the long term we continue to believe stocks are the best way to increase purchasing power, but those gains are unlikely to come without the typical volatility associated with investing in the stock market. This is precisely why appropriate diversification is necessary, particularly for those with near-term cash-flow needs from the portfolio. Adequate exposure to conservative assets like high-quality bonds is the antidote to volatile markets, and a key aspect of protecting client portfolios during times of stress. As we enter the later innings of the economic and market cycle, we remain disciplined in our strategic approach to managing portfolios.

JIC News: We're Looking Forward With a New Look

As we begin the New Year, you will see some changes to our firm's look as we unveil a refreshed brand and revised service offerings.

We see these exciting changes as a culmination of several years of growth and innovation. We've added people, expanded our service offerings and grown our presence to become the leading investment advisor in the region. We want our brand to reflect what we've become, while giving us an updated, contemporary appearance.

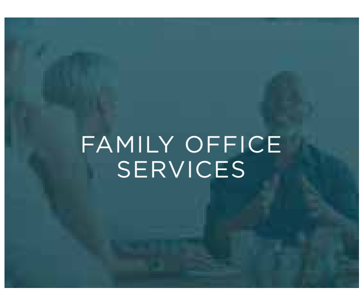
The most visible change is an updated logo – the new design reflects the JIC mission of putting clients at the center of everything we do. You'll see this new logo roll out on a variety of materials this year. The refreshed brand also includes an enhanced online experience. Clients will see a new client portal and a new, easier-to-navigate website in January.

You will also see new ads from us in 2019, which will highlight JIC and our divisions. These division names have been adjusted slightly to better communicate the ways we serve individuals, families, and organizations. You'll note our new logo has a variety of colors to represent each division. Here's a revised list of our divisions:

Divisions:
- > Johnson Wealth Management
- > Johnson Family Office Services
- > Johnson Trust Company
- > Johnson Asset Management
  (formerly known as Institutional Management)

While the look and feel of the firm will be updated, we remain true to our core values. For more than 50 years we have followed our founder's client-centered, service-oriented approach. We look forward to doing so for many decades to come.

JOHNSON
INVESTMENT COUNSEL



Promotions

We are pleased to announce these individuals have been promoted to new positions.

> Trinity Garrett
Senior Trust Associate

> Dom Robles, CTFA
Senior Trust Associate


Garrett


Robles

New Additions to the Team

We are pleased to announce that the following individuals have joined our team over the last several months:

> Skye Barry, CFA
Portfolio Manager, *Cincinnati*

> Rebecca Desch
Marketing Associate, *Cincinnati*

> Megan Eberhart, CFA
Associate Portfolio Manager, *Columbus*

> Michele Kaye
Client Support Assistant, *Cleveland-Akron*

> Lindsay Keith
Trust Officer, *Cleveland-Akron*

> Susan Koenig
Receptionist, *Cincinnati*

> Patti Kohlmorgen
Trust Compliance & Operations Associate, *Cincinnati*

> Kathleen Mahdasian
Client Support Assistant, *Columbus*

> Laura Mattern, CFA
Portfolio Manager Assistant, *Cincinnati*

> Joe White
Portfolio Manager Assistant, *Dayton*


Barry


Desch

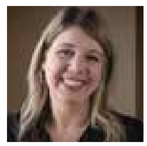

Eberhart


Kaye

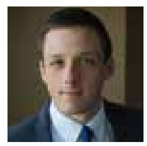

Keith


Koenig


Kohlmorgen


Mahdasian


Mattern


White

New Board Appointments in 2018

We are pleased to announce that the following individuals have been appointed to new boards in 2018.

> Tara Adams, CTFA
The Children's Theatre of Cincinnati, Board of Trustees

> Holli Alexander
Ensemble Theatre of Cincinnnati, Board of Directors, Executive Committee, Secretary

> Brian Butt, CFA
Cincinnati Zoo, YP Advisory Board

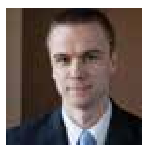
> Dan Gusty, CPA, CFP®
Columbus Zoo and Aquarium, Association Board

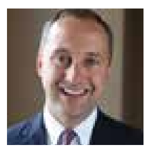
> Jason Jackman, CFA
Cincinnati Regional Business Committee (CRBC), St. Elizabeth Healthcare Foundation, Board of Trustees

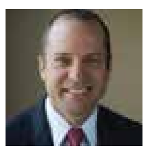
> Jamie Ritter
SPCA Cincinnnati, Board of Trustees, Executive Committee, Secretary


Adams


Alexander


Butt


Gusty


Jackman


Ritter

About Us

Johnson Investment Counsel, Inc. is Ohio's largest independent wealth management firm, managing over $10 billion in assets. Johnson Investment Counsel is an employee-owned firm, offering a full range of fee-based, integrated wealth management services, including: investment portfolios, education and retirement planning, cash management, estate planning, trust services, charitable giving, mutual funds, 401(k) plans, IRAs and more. Johnson Investment Counsel has built strong, long-term relationships with individuals and families, charitable organizations, foundations and corporations through three divisions: Johnson Private Client Group, Johnson Trust Company, and Johnson Institutional Management.

Divisions

- Johnson Private Client Group
- Johnson Trust Company
- Johnson Institutional Management

Services

- Stock Portfolios
- Bond Portfolios
- Balanced Portfolios
- Integrated Wealth Management
- Trust Accounts
- Pension & Profit Sharing Plans
- Individual Retirement Accounts
- 401(k) Plans
- Foundations
- Endowments
- Johnson Mutual Funds
- Johnson Charitable Gift Fund

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