Year-End Review and Outlook

2019 – Trade Tensions and Falling Interest Rates

This past year generated plenty of news regarding a slowing global economy, ongoing geopolitical concerns, rising global protectionism and the start of impeachment proceedings for the U.S. President. Even with all that, global capital markets shook off the news and marched higher. Reminding us all once again that the markets adjust to economic fundamentals and not the news cycle.

Many of the aforementioned concerns were seemingly defused by the easing of monetary policy by the world's central banks and improving economic conditions. Interest rate cuts combined with improved valuations (following the 4th quarter stock market decline in 2018) provided the backdrop for double digit returns in global markets. Even global returns as robust as they were, stood overshadowed by the strong returns seen in the U.S. stock market. While the calendar year performance has been nothing short of impressive, it's important to keep things in perspective. As of December 31st, the S&P 500 Index was up just over 10% from the previous market highs of September 2018.

Less talked about, but potentially even more impressive was the banner year in fixed income. Not only was there a pause in interest rate increases, but a complete reversal in U.S. central bank policy. The three rate cuts in 2019 helped create a tailwind that contributed to strong bond market returns. (As a reminder, bond prices move opposite to interest rates).

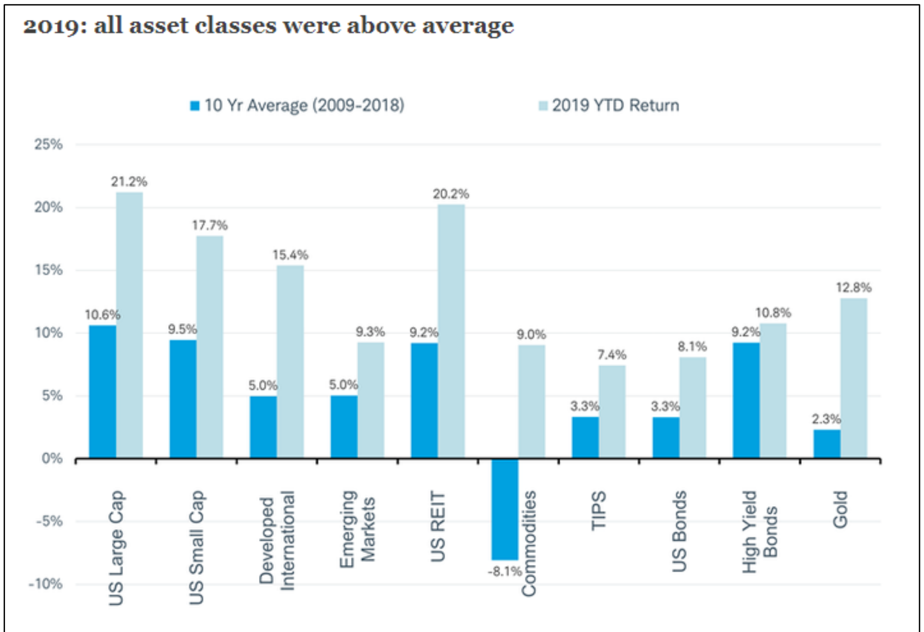
In comparison to 2018, you can see how strong returns were in both stocks and bonds over the past year.[1]

	2019	2018
• U.S. large cap stocks (S&P 500 Index)	31.5%	-4.4%
• Global stocks (MSCI ACWI IN Index)	26.4%	-10%
• Emerging market stocks (MSCI EM Index)	17.6%	-15%
• U.S. corporate bonds (FTSE U.S.BIG CORP. 3-7Y)	10.4%	0%

Overall, it was an impressive year for most investments. That said, it was unusual to have above average returns in so many asset classes in the same year. Typically, within a diversified

[1] Returns calculated by Tamarac Inc. software

portfolio we expect to see more variation with asset class returns. We have included the performance numbers (as of November 2019) as our point of reference.



Source: Charles Schwab, Factset data as of 11/29/2019. Asset class performance in US dollars represented by the following indexes: S&P 500 Index (US Large Cap Stocks), Russell 2000 Index (US Small Cap Stocks), MSCI EAFE Index (International Stocks), MSCI Emerging Market Index (Emerging Market Stocks), MSCI US REIT Index (US REIT), S&P GSCI (Commodities), Bloomberg Barclays US Treasury Inflation-Linked Bond Index (TIPS), Bloomberg Barclays US Aggregate Bond Index (US Bonds), Bloomberg US High Yield Index (High Yield Bonds), NYMEX Gold near term contract close (Gold). Past performance is no guarantee of future results.

<u>The Expected and Unexpected</u>

It might be difficult to remember this time last year, but we had just dealt with a tough 2018 4th quarter (the S&P 500 Index was down close to 20% from the September highs). At the start of 2019 we believed that fundamentals were strong enough to keep us out of a recession. We cited solid GDP growth, low unemployment and strong consumer confidence. Considering these factors, and the improved equity valuations due to the market correction, we were optimistic about the stock market going into 2019. Admittedly, the magnitude of positive returns this past year exceeded our expectations.

While we accurately forecasted that the last of the interest rate hikes were behind us, we did not anticipate the Fed's complete U-turn. Citing global growth concerns and low inflation, the Fed reversed course to an easing of monetary policy. Interestingly enough, the central bankers themselves didn't foresee the rate reductions going into 2019 as they had predicted two additional rate hikes.

Looking Ahead

- **Monetary Policy** – the Fed has made it clear they have no intention of lowering interest rates in 2020 from the current range of 1.5% - 1.75%. In agreement, we expect the positive economic impact of lower interest rates to hold up this year.

- **GDP growth** – although GDP growth for the U.S. slowed in 2019, we believe the easing of monetary policy will continue to support GDP growth of around 2% in 2020.

- **Employment** – unemployment edged up slightly in October, but it turned right back around in November to 50-year lows of 3.5%. This is one of the bright spots in the U.S. economy, and we expect sustained strength this year which will help the consumer.

- **Consumer confidence** – while we have seen some recent declines in consumer confidence, overall confidence remains at elevated levels. Due to the expected low levels of unemployment and modest wage growth we anticipate a resilient consumer in 2020.

Decisive action by the Fed has provided enough momentum to keep the U.S. economy progressing in 2020. Yet, geopolitical risk and political polarity (especially within the U.S.) continue to adversely influence business confidence and spending. We will continue to monitor for escalations in these areas as it has the potential to constrain expected growth, and negatively impact financial markets.

Areas of Opportunity

We continually search the investment landscape for opportunities that will grow and protect your money. While we analyze current economic and market information, we remain disciplined and strategic in managing your portfolios for the long-term. As in the past, we will systematically rebalance the portfolios to take advantage of market volatility.

- **U.S. Equity** – above average returns over the past decade have driven expectations for future returns lower, to single-digit positive returns (on average). We see opportunity to keep investments in companies that are undervalued to provide growth and stability amidst market volatility.

- **Foreign Equity** – globally, more than half of all publicly traded companies are located outside of the U.S. We maintain our view that international stocks, especially emerging markets, provide an opportunity. In addition to having attractive valuations and growth prospects, we have observed the correlations (how much one zigs and the other zags) of U.S. and international stocks decrease. Therefore, we believe there is opportunity for greater diversification and higher future expected returns by maintaining foreign equity in your portfolio.

- **Fixed Income** – while future returns for fixed income are expected to be lower than in the past, their fundamental role in the portfolio has not changed. We continue to invest in high-quality bonds and bond mutual funds that play a key role in providing income, risk reduction and stability.

- **Alternative Investments** – as appropriate (based on your specific situation), we will invest in several mutual funds based on 'alternative' strategies to provide additional diversification and downside protection.

Summing It Up – Staying Focused on What's Important

After an 11-year bull market, stocks are now valued at the upper range of historical price-to-earnings (P/E) ratios. We all know by now it's not a matter of if, but when the stock market will slow down or even decline. Does this mean we should try to time the market, and/or go into all cash? Of course not, we know it's impossible to time markets, and cash is a guaranteed way to consistently lose to inflation. Instead, we want to focus our time and energy on what we can control, and not let the constant noise of the news and market volatility distract us from our long-term objectives.

Ultimately, in this challenging environment investors with an appropriate level of discipline, diversification, and patience will be rewarded over the long-term. Warren Buffet said it best with the following quote:

"The stock market is a device for transferring money from the impatient to the patient."

We manage your money adhering to time-tested investment principles based on a long-term focus, disciplined asset allocation and systematic portfolio rebalancing. This ensures that your portfolio is prepared to take advantage of the inevitable ups and downs in the markets. By sticking to your financial objectives and long-term investment strategy we can help you tune out the noise and provide more time to focus on what's most important to you.