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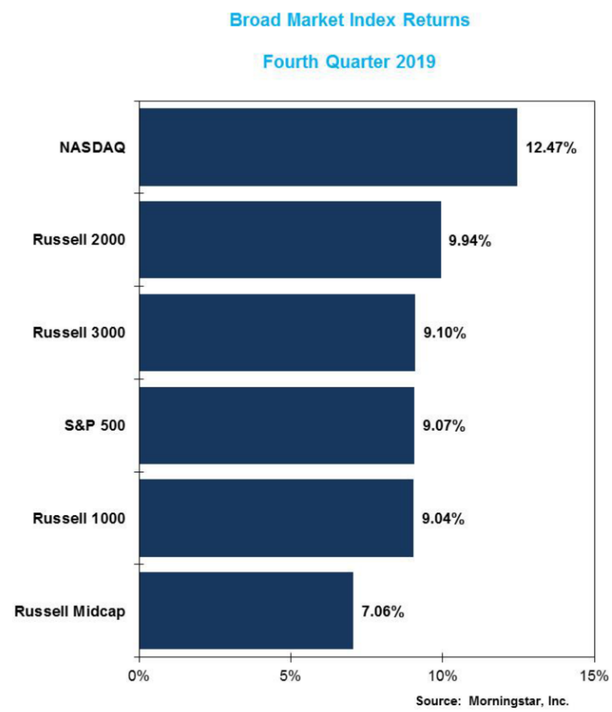
What a difference a year makes. In 2018 basically all areas of the market were down, and concern abounded regarding the economy, trade wars and the market. 2019 has been a good lesson in reminding us that the world, the economy and the markets are uncertain and as a result generally unpredictable. The 2019 market was a complete reversal of 2018. Simply put, virtually all areas of the market were up and up significantly this past quarter and throughout 2019.

THE ECONOMY

The US economy's growth continued to slow modestly in the quarter. The Bureau of Economic Analysis reported its third estimate of third quarter 2019 gross domestic product (GDP) of 2.1%, in line with the prior estimate, and slightly higher than the second quarter's 2.0% reading. The employment situation surged in the latest month, with an average of approximately 205,000 jobs added each month of the quarter. The unemployment rate dipped to 3.5%. The Federal Open Market Committee (FOMC) modified its interest rate policy by lowering the federal funds rate target once during the quarter, to a range of 1.50% to 1.75%. Economists currently expect the FOMC to maintain the fed funds rate at current levels through 2020.



The global economic environment continued to lose momentum, driven by ongoing trade uncertainty and developed markets economies experiencing the slowdown phase of the business cycle. Eurozone economic growth was resilient, with consumers again serving as the primary positive driver. Employment in the region remains robust, but further gains may be difficult to attain at this point in the cycle. China's economy continues to suffer, with both imports and exports declining. Exports to the US alone plunged 20% in recent months due to increased tariffs.

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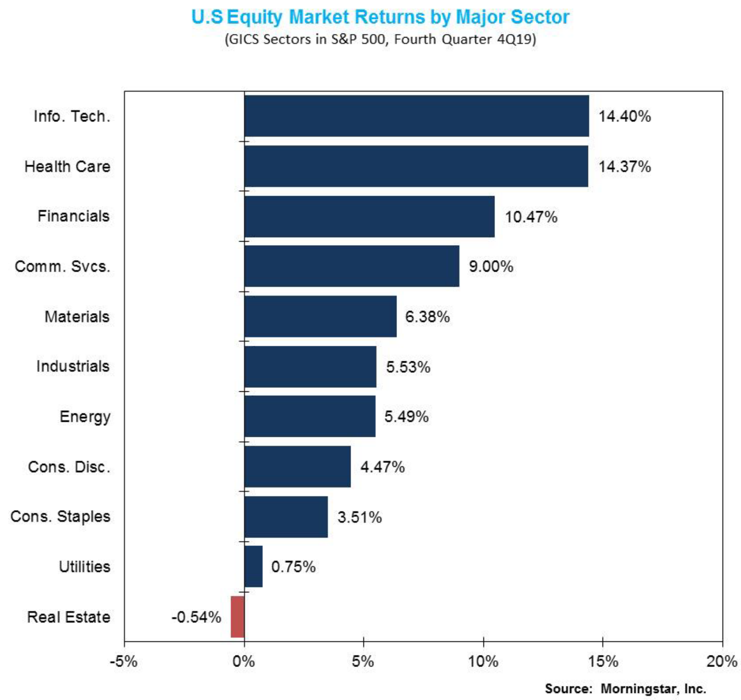
Highlights and Perspectives

GROSS DOMESTIC PRODUCT (GDP)



The Bureau of Economic Analysis released the third estimate of the third quarter 2019 real GDP, a seasonally adjusted annualized rate of 2.1%, slightly higher than the second quarter's 2.0% annualized growth, and in line with the prior estimate. Growth slowed for much of the year, and employment gains also moderated commensurately. Consumers are currently serving as the engine for growth, and home sales and residential construction were also positive factors with the decline in mortgage rates. Business investment remains sluggish due to trade uncertainty and geopolitical risks. Corporate profits fell by 0.2% (not annualized) during the quarter. The Trump administration's trade war with China and other trading partners remains the primary drag on growth, although economists believe the FOMC's interest rate reductions in 2019 should begin to offset some of the negative impacts of tariffs. Analysts also expect President Trump to soften his trade stance heading into an election year.

HOUSING

The housing segment leveled off during the quarter after having posted solid gains throughout the first three quarters of the year. Analysts point to low inventories as being a reason for the recent dip. Mortgage rates are back near the 2016 lows after the FOMC's interest rate reductions. Existing-home sales for November (the latest monthly data available) fell to an annualized rate of 5.4 million units, 1.7% lower than the results from October, but up about 2.7% from year-ago levels. The inventory of existing homes was less than four months of supply, lower than levels of the prior year. Existing-home prices in November increased 5.4% from November 2018. In the new-home segment, the National Association of Home Builders (NAHB) Housing Market Index (HMI), a measure of homebuilding activity, ended the quarter at 76, sharply higher than both

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the prior month's and year-ago levels. The data indicate that homebuilders are very positive on the outlook for the housing market.

EMPLOYMENT

The employment situation improved markedly in November, reversing the trend of lackluster results for the past couple of quarters. Employers added 266,000 jobs during the month, above the consensus expectations of 182,000 new jobs, and higher than the prior month's gain of 156,000. In addition, gains for September and October were adjusted higher by a combined 41,000. Resolution in the auto workers strike boosted gains, and gains in the health care sector were also strong. The three-month moving average rose in November to its highest level since January, coming in at 205,000. The unemployment rate in November declined to 3.5%, and the labor force participation rate remained at 63.2%, its highest level of the year. Average hourly earnings increased by 3.1% from the year-ago level.

FED POLICY

The FOMC ended its recent December meeting by announcing that there would be no change in the federal funds rate target range of 1.50% to 1.75%. The committee had lowered the target once during the quarter, following two reductions in the third quarter. There were no dissenters to the decision to leaving the target rate unchanged. The consensus among analysts is that there will likely be no change in interest rate policy in 2020 absent a significant change in economic growth.

INTEREST RATE

Fixed income securities' prices and yields were impacted by several important factors during the quarter, including an acceleration in job growth and expectations for an easing in the trade tensions with China. In addition, Boris Johnson's decisive re-election as UK Prime Minister is expected to bring greater clarity to the Brexit situation that has cast a cloud over the region for more than three years. For its part, the FOMC lowered interest rates once during the quarter, bringing the target federal funds rate range to 1.50%-1.75%. The combination of these factors resulted in a more normal yield curve shape, with generally higher yields. Economists expect yields to closely track the economy going forward, as the FOMC committee members anticipate no additional rate reductions (or increases) in 2020.

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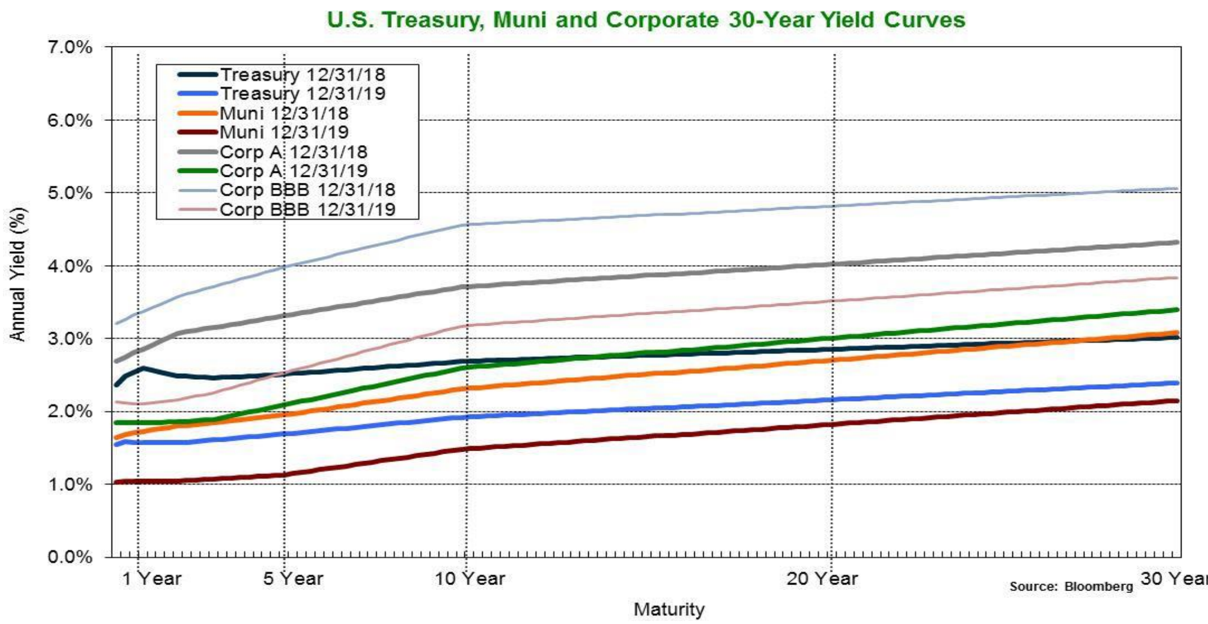

The yield on the 10-year Treasury generally trended higher during the quarter, as US employment data showed robust gains, signs emerged that trade tensions would ease, and that the UK elections would finally bring some clarity to the Brexit situation. The path of interest rates during the quarter reflected the general resilience of the US economy. Inflation expectations were somewhat higher, with the Fed's gauge of five-year forward inflation expectations increasing slightly from 1.58% on September 30.

Total returns on fixed income securities were generally positive across most of the market segments. The Bloomberg Barclays Treasury 5-7 Yr. Index declined by -0.4% for the quarter. The Bloomberg Barclays US Corporate 5-10 Yr. Index gained +1.3% during the three months. High yield securities, which often follow the performance of equities, climbed, posting a return of +2.6%. Municipals also rose, as the Bloomberg Barclays Municipal Bond Index gained +0.7% during the quarter. Prices of non-US fixed income securities were modestly higher in the quarter, as the Bloomberg Barclays Global Aggregate ex-US Index advanced +0.7%. Emerging markets bonds continued their positive trend, with the JPM EMBI Global Index gaining +2.1%.

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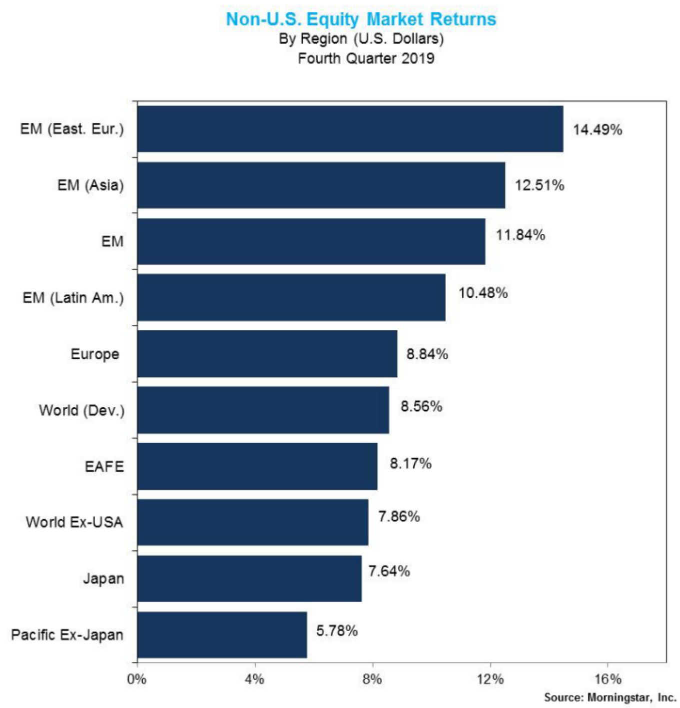
EQUITY MARKETS

After battling through the adverse seasonal headwinds at the beginning of the quarter, equity markets provided consistent and steady gains throughout the quarter. September and October are often difficult months for stocks, and 2019 was not an exception, as broad-based indices declined roughly 3.5% in the first week of October. However, as economic data remained solid, and as the trade situation continued to thaw, markets recovered and established new all-time highs. Within that context, the S&P 500 Index finished the quarter with a gain of +9.1%. For the year, the S&P 500 delivered a total return of +31.5%.



Performance of the eleven primary economic sectors was positive during the quarter, with ten sectors delivering positive gains and only one producing a negative return. Health Care, Information Technology and Financials were the strongest performers on a relative basis, generating returns of +14.4%, +14.4%, and +10.5%, respectively. The Real Estate, Utilities and Consumer Staples sectors were the poorest relative performers, posting returns of -0.5%, +0.8%, and +3.5%, respectively.

The Russell 1000 Index of large capitalization stocks generated a +9.0% total return. Within the large cap segment, growth stocks outperformed value stocks. Small cap stocks, as represented by the Russell 2000 Index, slightly outperformed large caps, and finished the quarter with a total return of +9.9%. Small cap growth outperformed small cap value. The NASDAQ Composite, dominated by information technology stocks, finished the quarter with a gain of +12.5%. The Dow Jones Industrial Average of 30 large industrial companies advanced +6.7%.

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Real Estate Investment Trusts (REITs) gave up ground during the quarter, with the DJ US Select REIT Index down -1.2%. Commodities were higher, with the Bloomberg Commodity Index gaining +4.4% for the quarter.

International stocks delivered strong gains during the quarter, and generally performed in line with US equities. As in the US, global growth has slowed in recent quarters, but has remained positive. The MSCI ACWI Ex-USA Index, which measures performance of world markets outside the US, rallied by +8.9%. The MSCI EAFE Index of developed markets stocks rose by +8.2%. Regional performance was positive across the board for the quarter. China was the strongest performer on a relative basis, with a return of +14.7%. The Pacific region ex-Japan was the poorest relative performer, gaining +5.8%. Emerging markets performance was quite strong, as the MSCI Emerging Markets Index was higher by +11.8%.

LOOKING FORWARD

The US economy is in the midst of the longest expansion on record at 126 months, and at this point in the cycle the slowing growth that has been experienced should be expected. But the economy is nothing if not resilient, continuing to deliver gains in the face of the continuing trade war with China and other significant trading partners, geopolitical tensions, and deep political fissures that have resulted in the impeachment of President Trump. By most accounts the FOMC has seemed to have reversed the damage done by its decision in 2018 to raise interest rates too much and too quickly. The committee's three rate reductions in 2019 seem to have been enough for the economy to remain on track for continued modest growth. Expectations among economists are that President Trump and China's President Xi Jinping will continue to de-escalate the trade war, both because of the damage it has already inflicted on the Chinese economy and the fact that 2020 is a Presidential election year in the US. The consumer has been the linchpin of growth not only in the US but across world economies. Many analysts believe the outlook for consumers remains bright as a result of the combination of household deleveraging that has occurred over the past decade and growth in personal income. Economists warn that one risk to the US economy in 2020 may be that because there are stark differences in the economic policies of President Trump and his Democratic rivals, uncertainty about the election's outcome may alter consumer behavior such that it adversely impacts the economy. Elections have historically had little impact on the economy, but some economists believe that with the prevailing deep political divide 2020 may be an exception.

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We all enjoyed 2019 return wise, but it is important to remember that the market generally reverts over time to the mean. As a result, it is anticipated that returns for 2020 will be significantly different from 2019 and we think it is important to temper expectations.

Please be sure to contact us if you have any concerns regarding your portfolio or allocation or if you have any upcoming cash needs that we are not aware of.

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