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Q3 2019 – Market Overview Newsletter

Economic Update

During the third quarter volatility continued, driven by the endless stream of negative news. Uncertainty also remains around the globe with continued trade talks, a possible U.S. Presidential impeachment and Brexit. We will likely see continued short term volatility triggered by a variety of events, but the effect of daily headlines is hard to predict.

The biggest obstacle to continued global growth at the moment seems to be trade. President Trump launched the tariffs in March 2018 after the U.S. economy received a boost from the tax cuts. It would have been interesting to see how much stronger the economy might have become if he had waited and allowed the effects of tax cuts to work a little longer. By October of 2018 a formal agreement was negotiated with Canada and Mexico. After that, attention shifted to China where it remains.

The economic tailwind that President Trump had going into the trade negotiations has slowed. The slowdown is representative of weakness in business investment spending, imports, exports, and inventory accumulation. Businesses are not likely going to make long term investment decisions without knowing the outcome of the ongoing trade dispute. Although economic conditions have slowed, we don't currently see anything significant enough to derail the U.S. economy. None of the cyclical sectors of the economy, such as vehicle sales, housing, and business investment spending appear to be overextended. "Without a boom, it's hard to generate a bust", Dr. David Kelly, J.P. Morgan Chief Global Strategist, states.

Despite the economy losing some steam, stocks have strongly bounced back from the end of 2018. The U.S. stock market, as measured by the S&P 500 Index, was up 20.6% year-to-date. We have also seen positive performance in the bond markets. The strong bond performance this year is attributable both to a depressed global interest rate environment and the Federal Reserve's (FED) current posture of lowering interest rates. The FED is now in an "easing" mode that usually occurs during economic downturns, despite a stable economy.

The story doesn't change much when we look at international markets with global manufacturing weakness and the ceaseless Brexit. The trade tensions have led to a slowdown in China as well which has had a ripple effect on the rest of the world. As a result of slow international economic growth, international stocks have continued to lag U.S. stocks in 2019. However, in the long-run, slowing growth in the U.S. and a rising trade deficit could cause the dollar to fall, magnifying returns in international equities. From a valuation perspective, many international stocks are simply cheaper, and valuations tend to be an important guide to long-term returns.

Although investors should be aware of economic and market risk, low interest rates in a growing economic environment generally favor stocks over bonds in the short run. The trade talks could lead markets either way but will hopefully be a positive surprise in the 4th quarter. There are any number of world events with the potential to increase volatility. Despite the headlines there are lots of positives happening too. The important part is to see past the short term situations and focus on long term goals.

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For more market details, see the "IM&R Q3 2019 Market Review" in the commentaries page on our website at www.langdonshaw.com/commentaries

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A recession is a significant decline in activity across the economy, lasting longer than a few months. It is visible in industrial production, employment, real income and wholesale-retail trade. The technical indicator of a recession is two consecutive quarters of negative economic growth as measured by a country's gross domestic product (GDP).

There are some risks associated with investing in the stock markets: 1) Systematic risk - also known as market risk, this is the potential for the entire market to decline; 2) Unsystematic risk - the risk that any one stock may go down in value, independent of the stock market as a whole. This also incorporates business risk and event risk; and 3) Opportunity risk and liquidity risk. The bond market is volatile and carries interest rate, inflation, liquidity and call risks. As interest rates rise, bond prices usually fall, and vice versa. Change in credit quality of the issuer may lead to default or lower security prices. Any bond sold or redeemed prior to maturity may be subject to loss. International investing involves special risks, including, but not limited to, the possibility of substantial volatility due to currency fluctuation and political uncertainties.

The Federal Reserve System (also known as the Federal Reserve, and informally as the Fed) is the central banking system of the United States. The Federal Reserve System is composed of 12 regional Reserve banks which supervise state member banks. The Federal Reserve System controls the Federal Funds Rate (aka Fed Rate), an important benchmark in financial markets used to influence the supply of money in the U.S. economy. Gross Domestic Product (GDP) is the monetary value of all the finished goods and services produced within a country's borders in a specific time period, though GDP is usually calculated on an annual basis. It includes all of private and public consumption, government outlays, investments and exports less imports that occur within a defined territory. MSCI All Country World Index (ACWI) Excluding U.S. is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of developed and emerging markets. Investors cannot invest directly in an index.

Quantitative easing is an unconventional monetary policy in which a central bank purchases government securities or other securities from the market in order to lower interest rates and increase the money supply. Quantitative easing increases the money supply by flooding financial institutions with capital in an effort to promote increased lending and liquidity. Quantitative easing is considered when short-term interest rates are at or approaching zero, and does not involve the printing of new banknotes.

S&P 500 return is from Morningstar.com and is total return. **S&P 500 Index** is an index of 500 of the largest exchange-traded stocks in the US from a broad range of industries whose collective performance mirrors the overall stock market. Investors cannot invest directly in an index.