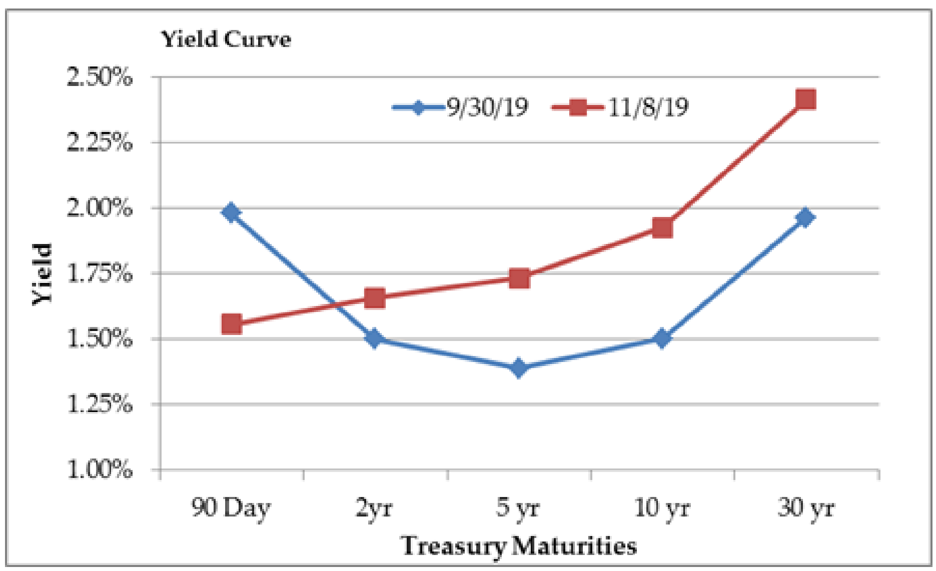
MID-QUARTER UPDATE – NOVEMBER 2019

Beginning in October, hopes for an interim trade deal with China started to move markets, and stocks began to grind higher while bonds headed lower. Large domestic stocks continue to outperform, and the S&P 500 index is up approximately 25% for the year and setting new high water marks. Foreign stocks are still below their highs of early 2018, but globally there is a renewed appetite for risky assets. Germany had been posting recession level economic weakness, but the most recent data is showing a potential bottoming, which has global investors hopeful. Throw in an earnings reporting season that was rife with upside surprises (albeit from low expectations), and the impetus for higher stock prices was there.

Perhaps what has been most astonishing in a year of many surprises was the strength of bonds alongside stocks. A complete reversal in Fed policy at the beginning of the year was the initial fuel for the rally, but now that the Fed has signaled a conclusion to this round of rate cuts, after their third this year on October 30, bond returns have decoupled from stocks, and bonds have not participated in the recent advance. No more rate cuts, green shoots in Europe, and decent earnings mean that bonds are less attractive than stocks to many investors. All areas of the bond market that we follow are off the highs set in August, when trade tensions and global recessionary calls had people talking about what life under zero interest rate policy would look like here in the US, but the mood has changed since then. As an example, intermediate Treasuries are down approximately 4% from the August highs, and the yield curve has un-inverted over the past couple of weeks, as illustrated in Exhibit 1.

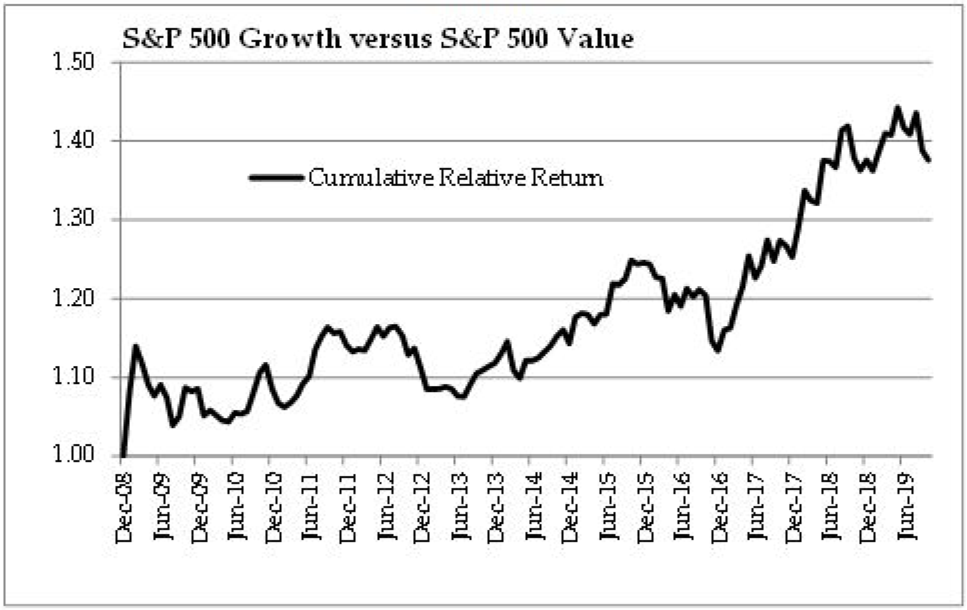
Exhibit 1



The blue curve from September shows how 90 day yields were significantly higher than 2, 5, and 10 year Treasury yields – an inversion. The current yield curve (in red) shows a normal, upward sloping yield curve, where longer dated bonds yield more. We spent plenty of time discussing the yield curve in earlier newsletters, but in short, an inverted yield curve means that longer term rates are actually lower than the shorter term rates, which are set by Fed policy. When the curve is inverted the market thinks that rates will be lower in the future, likely in response to a slowdown or recession. At this point the recession talk has subsided.

The other point worth discussing briefly is that we are seeing a reversal of the multi year period of growth stocks outperforming value, and value stocks are beginning to take the lead. Exhibit 2 looks at the cumulative relative performance of the S&P 500 Growth and Value indices since 12/31/08. When the line is rising, Growth is outperforming Value.

Exhibit 2



From 2008 to 2014 relative performance fluctuated, though with Growth outperforming over more of the period, it built a modest lead. This shifted into overdrive in 2015, with Growth outperforming in four of the last five years and building substantial cumulative outperformance. But you will note that the cumulative performance line has turned down over the past few months. This reign of growth over value has been one of the largest in history, and a reversal has probably been overdue for some time and would benefit many actors in the market, as the broad underperformance of value factors has weighed on value style and factor investors alike.

Things change quickly in the markets. By the time this newsletter reaches your desk, Trump and Xi could be at each others' throats again and the markets could be at a complete about-face. The global economy is not out of the woods yet, and evidence of further weakness abroad would be cause for concern. Impeachment proceedings have thus far not been an issue for markets, and that could possibly change at some point. The real fireworks might be reserved for the election spectacle next year, but that is just too far away for stocks to start considering. In the meantime we will be thankful for the calm in the markets for now and for solid returns this year, but we remain cautious with a healthy dose of skepticism as well.

Planning and Operational Items

We wanted to take a moment to focus on a few important planning items. As everyone knows, life changes, and we encourage you to keep us informed when it does. Triggering events might include:

- Marriage or divorce: This probably means it is time to update your beneficiary designations (here, and with your employer sponsored retirement plan). You should also review your estate planning, as marital status changes can have significant ramifications to existing estate plans.
- Children or grandchildren: We can talk about ways to save for college, gifting strategies, and potential tax ramifications.
- Have you moved? We will update your contact information where appropriate and review whether this results in a change to your state tax withholdings, if applicable.
- Do you have a new job? We can review investment options available in your new retirement plan and give allocation recommendations. It may also make sense to roll over any retirement plans from your previous employer.

As your advisor, the more information you share with us, the better equipped we are to help you and your family with your investment management and financial planning needs.

As we approach year end, we also want to remind you of time sensitive planning strategies to keep in mind. We are happy to discuss any of these topics with you in more detail!

- Roth Conversions – should you consider one?
- Required Minimum Distributions – for those age 70½ or older, these must be taken by December 31st (except for in the first year). For the charitably inclined, a Qualified Charitable Distribution allows you to gift your RMD directly to charity, which could result in tax savings.
- Charitable gift "bunching" – this refers to consolidating tax-deductible charitable contributions that would normally be made over multiple years into a single tax year. This can benefit donors whose non-charitable itemized deductions fall below the new, higher standard deduction.
- Maxing out retirement plan contributions – you can contribute $19,000 plus a $6,000 "catch up" contribution to your employer-sponsored retirement plan if you are age 50 or older. The IRA max is $6,000 plus a $1,000 "catch up" contribution for those age 50 or older.
- Utilize your FSA balance – if you do not use it, you will lose it.
- Annual exclusion gifting – the limit in 2019 is $15,000.

- Quarterly estimated tax payments – check with your CPA to be sure you have paid enough in estimated taxes.
- Filling up tax rate brackets in a lower income year.
- Divest from low basis stock positions – if it is advantageous for your current year tax situation.
- Exercising stock options.

If you think any of these apply to you or you simply want to learn more, please do not hesitate to reach out.

We wish you and your family all the best as we head into the holiday season.

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