Clear Point
ADVISORS INC

Quarterly Commentary

Fourth Quarter 2019

Investment Commentary

Stocks and bonds completed a bountiful decade in the final quarter of 2019. The 2010 decade was the first in U.S. history to avoid an economic recession, with accelerated growth in various sectors, including technology, healthcare, and industrials. According to Wilshire Associates' estimates, total stock market value increased $7.5 trillion for the past year alone.

The equity market's rebound from its topple in December 2018 was unexpected by many investors, as 2019 began with concerns of a recession and a further market downturn. The S&P 500, the Dow Jones Industrial Average, and NASDAQ Composite all reached levels that most investors considered unreachable in 2020. The Dow approached 29,000, while the technology-heavy NASDAQ rode the rally overtaking Nasdaq 9,000 in the last quarter. For the full year, the Dow increased 25.3%, the S&P 500 Index rose 31.2%, and Nasdaq was up 36.7%. International markets also advanced broadly in 2019, with gains seen in the developed markets and, to a lesser extent, in emerging markets. The EAFE International stock Index rose 22% for the year.

Inflation has been surprisingly contained even with the unemployment rate at a 50-year low, together with a gradual economic expansion. Fed Chair Jerome Powell announced, "as long as incoming information about the economy remains broadly consistent with our outlook, the current stance of monetary policy will likely remain appropriate." Many believe that since it is an election year, the Fed will stay out of the way.

During the fourth quarter, the Fed injected billions of dollars into the repurchase-agreement market, also known as the "repo market," and also bought roughly $400 billion of bonds. The Fed added these funds to the marketplace to shore up liquidity to avert a market disruption, such as the one that occurred in the fourth quarter, 2018. The strategy strikes similar notes to the Fed's quantitative easing program ("QE") enacted during the financial crisis. Many analysts believe that the Fed's recent actions helped dampened volatility that followed the recent upheaval in the Middle East.

The price/earnings ratio for the S&P 500 Index ended 2019 at 18.3, up from 15.6 at the end of 2018. Analysts view this ratio as a gauge of fair value of the equity markets. Wall Street analysts' expectations were not enthusiastic about 2019 corporate earnings. They were on point, with earnings running flat last year. For 2020, most analysists expect a low single-digit rise in earnings. Some growth in earnings would be most helpful in supporting the market's upward momentum from the somewhat lofty current price-earnings multiple.

Geopolitical Catalysts

A proposed phase-one trade deal between the U.S. and China helped elevate market indices during the last quarter, though some believe that a more substantive agreement may not materialize as soon as is hoped. The 94-page phase one deal was just signed into effect on January 15th of 2020.

With a view towards the phase-one deal, the U.S. canceled new tariffs slated to go into effect last December 15. Also, the deal rolls back the 15% tariffs imposed on $110 billion of Chinese goods back in September, down to 7.5%. In return, China has committed to the purchase of more than $200 billion of U.S. products over the next two years. Many believe this should mark the end of the trade war escalation and put the economy on a sturdier footing in 2020.

With the Fed seemingly on the sidelines and trade less uncertain, 2020 economic growth could tick up toward 2.5%. Federal tax revenues and the federal budget deficit should also benefit from the rise in the equity markets and the continued low rate environment.

Fixed Income Markets

By all accounts, most investors expected the Fed to increase interest rates in 2019 but instead ended up with three rate cuts, dropping rates below 2%. This illustrates how perilous it can be to make investment decisions based on assumptions about the direction of rates.

Bond Investors realized exceptionally strong results attributable to the decline in short-to intermediate-term interest rates. With rates being so low, the interest received from bonds made only a small contribution to total returns from bonds for the year. Declines in interest rates cause bond prices to rise, and most of 2019's bond market gains came from a rise in bond prices. The

sharp decline in yields delivered a sugar rush for investors who held longer-term bonds for the year, with the Barclays Aggregate Bond Index gaining 8.7%.

The Secure Act

Retirement plan legislation passed by Congress effective 2020 includes changes affecting millions of American retirees. The setting Every Community Up for Retirement Enhancement Act was signed into law by the President on December 20th. The Law includes provisions to facilitate retirement savings for small company workers, offers additional distribution options for 401(k) participants, and redrafts inherited IRA rules.

The Act also increases the required minimum distribution (RMD) age for IRAs to 72 from 70 ½. The new RMD age applies only to those who turn 70 ½ after December 31, 2019.

The rules surrounding the distribution of funds from an Inherited ("Stretch") IRA have changed by accelerating the distribution and taxation of Inherited IRA funds going to non-spouses. Those most affected by the new rules are retirees with generous IRA balances intending to leave funds to their children and grandchildren. Inherited IRAs have allowed IRA beneficiaries to stretch distributions and taxes over an extended period of time.

On another front, the IRS is providing annual inflation adjustments for over 60 tax provisions, including tax rate schedules, exemptions, and standard deductions. Notable increases affecting many taxpayers include the standard deduction (married filing jointly increased to $24,800) and basic 401k contribution limits (up to $19,500) for 2020. The tax code provision that provides for a $3,000 write off for capital losses, such as on investments, is an unindexed provision that isn't changing and hasn't had an increase since 1977!

2020 Outlook

Our outlook for 2020 is for the U.S economy to remain stable, led by a strong consumer, full employment, and low-interest rates. U.S. stocks aren't cheap, but the 18x forward price-earnings multiple may hold, especially with rates so low. We continue to prefer the U.S. stock market over International stocks, but emerging markets appear poised for better relative performance in 2020.

After big years in the markets like 2019, or after a big market meltdown as in 2008, our investors often ask, "what should we do now?" As fiduciary advisors, we believe that the best response is to revisit and reassess your risk tolerance and current financial situation:

- Unless market conditions have changed, try to rebalance your portfolio back to your targeted asset stock/bond mix.
- Seriously consider your investment time horizon and act accordingly.
- If your time horizon is over five years, think and invest for the long-term, not the next trading days.
- Stay invested and be true to your plan, as "going to cash" is usually not fruitful.

One final thought. Markets tend to run in bullish and bearish cycles; some markets are secular (long-term) and some cyclical (shorter-term). History illustrates that secular markets have tended to last for about 20 years. Time will tell, but perhaps we remain amid a 20-year secular bull market in stocks. So, we'll keep your portfolio diversified and invested at an appropriate risk level for your circumstances.

Best Regards,

Steven

Clear Point Advisors