TINGEY ADVISORS
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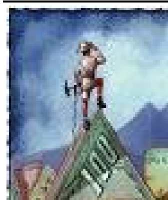
Fall 2019 Newsletter **www.tingeyadvisors.com** **801-352-8166**

Benchmarks

	30 Sept 2019	30 June 2019	30 Sept 2018
S&P 500	2,977	2,942	2,914
DJIA	26,917	26,600	26,458
NASDAQ	7,999	8,006	8,046
6-mo US Treasury Yield	1.83%	2.09%	2.36%
30-yr US Treasury Yield	2.12%	2.52%	3.20%
Prime Rate	5.00%	5.50%	5.25%
Federal Funds Target Rate	2.00%	2.50%	2.25%
30yr Mortgage	3.89%	3.90%	4.75%
Gold – per oz	$1,466	$1.409	$1,192
Oil - WTI / bbl	$54	$58	$75

Sources for Newsletter: WSJ, Barron's, Bloomberg, NBER, Blackrock, Federal Reserve



The Summer of Discontent

If Shakespeare had lived through the stock market of the summer of 2019, he may well have changed the opening line to the play Richard III from the "winter" of our discontent to the "summer" of our discontent. China trade tension; yield curve inversion; slowing economy; political machinations all combined to cause traumatic turmoil in the capital markets. Investors experienced anything but a quiet summer as the stock market cycled from "risk on" to "risk off" but in the end, finished the quarter about where it started. The bond market was the beneficiary of the "risk off" sentiment as investors sought safety.

The economy, for its part, continued its record expansion. Concurrent with the economic expansion is a jobs market that is stronger that any we've seen in 50 years. There is very little to criticize in the labor market with real improvement in jobs and wages. The strongest growth in median wages is coming from the lowest wage earners. Low unemployment, and wages rising faster than inflation is healthy for consumers.

Notes: Figures are 12-month averages of median annual wage growth. Skill levels are based on occupations, not individual workers. | Source: Federal Reserve Bank of Atlanta

While domestic economic growth is continuing, global growth is stalling. Federal Reserve Chairman Jerome Powell was certainly aware of the global economic headwinds as he retreated from the previous path of increasing interest rates. Chairman Powell lowered short term rates by 0.25% and described the change in interest rate policy as "mid-cycle correction". Chairman Powell followed his July rate cut with a similar cut in September.

Stocks:

The S&P 500 eked out a modest gain in the third quarter, helping stocks hold on to their healthy gains for 2019 and prolonging the longest bull market on record according to the Wall Street Journal. Despite the geopolitical uncertainty, investors are finding few solid alternatives to U.S. domestic equities. In a low interest rate environment, the relative healthy dividend yields are attractive compared to the yields of other asset classes.

The current year's stock returns are an impressive rebound from the 2018 stock market swoon in the fourth quarter. However, the stock market is only 2.2% higher than it was twelve months ago. While modest, we'll take it given the trade conflict, federal reserve rate hikes, government shutdown and corporate earnings concerns that were driving the poor stock market returns at the end of 2018.

The S&P 500 Index, Dow Jones Industrial Average and Nasdaq Composite advanced 1.7%, 1.8% and 0.2 % respectively in the quarter, as the market hung on to the impressive gains from the first half of the year. Notably, the small-cap Russell 2000 is up strongly for the year at 14.2%, but has lagged mid-cap and large-cap indices and actually fell -2.4% for the quarter. The strongest U.S. sectors in the quarter were consumer goods, financials, utilities and technology. Global stock indices didn't fare as well as they did in the U.S. In the quarter, the MSCI EAFE index fell 1.1%. The MSCI Europe index fell 1.8% and the MSCI emerging market fell 4.3%.

Bonds / Interest Rates:

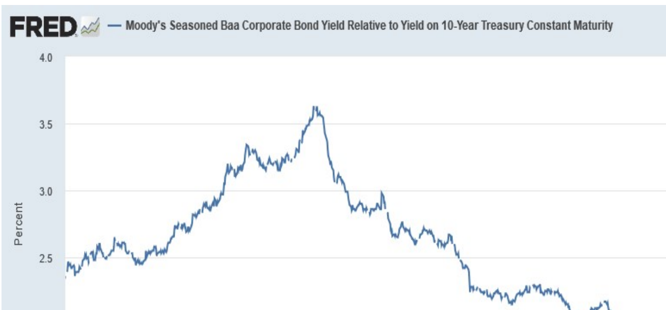
Geopolitical machinations, negative interest rates abroad, and concern for decelerating economic growth, global investors sought safety in the form of purchases of U.S. Treasury bonds. Yields, which fall when bond prices rise moved decisively to the downside during the quarter. The yield on the benchmark 10-year Treasury note settled at 1.675% to end the quarter fully 0.325% lower than where it finished the second quarter. Six-month rates generally followed the federal reserve's interest rate reductions in the quarter and ended the quarter at 1.83% -- down from 2.09% to start the quarter. The long bond yield, fell from 2.52% to 2.12%.

Yields on long-term bonds dropped more than yields on shorter bond maturities. This resulted in a flat to inverted yield curve during the quarter.

Often, an inverted yield curve (where short-term rates are higher than longer term rates) signals possible recession. It is uncommon to have longer maturities yielding less than shorter

maturities because that means that investors are seeking safety more than they are seeking yield. Each of the past seven recessions since 1969 have been preceded by an inverted yield curve. There are times, however, when the yield curve inverts and we don't get recession.

The Baa yield spread is another significant bond market signal that can predict recession. This is a simple calculation of the yield on a Baa 10-year corporate bond compared to the 10-year U.S. Treasury Bond yield. During a recession, corporations have diminished cash flow and therefore have a harder time paying off their debt. The bond market understands this eventuality and will then require higher yields on low credit quality corporate bonds (Baa bonds). Conversely, when the bond market expects recession, money flows into safe government bonds driving yields down. This simultaneous action – rising corporate bond yields and falling government bond yields – results in a larger yield spread and signals when economic growth is faltering. The curious thing today is that this spread, while rising slightly, has been quite muted and, in fact, is sitting at a benign level compared to past recessions.



Certainly, the inverted yield curve bears close watching, and if it were confirmed with a spike in the corporate yield spread it would give strong credence to the prospects of an oncoming recession. As of today, that confirmation has not materialized.

Risks and Opportunities:

It sounds like a broken record from our prior newsletter, but we continue to see the following as the most significant near-term risks: 1) a prolonged U.S. – China trade dispute continues to negatively impact the global economy, 2) a potential increase in inflation due to the effect of tight labor markets on wages, 3) decelerating corporate profit growth, 4) global government and corporate debt and a rising potential for default, and 5) wider government policy swings from a polarized government.

Conversely, we see the following as potential opportunities: 1) continued economic growth, 2) contained inflation, 3) corporate profits potentially better than the market expects, 4) solid labor market, 5) The Federal Reserve continuing a path of a less-restrictive policy, 6) real progress in global trade agreements. While we are cautious, the Federal Reserve's accommodative policy and some signals of the trade conflict de-escalating, tilt us toward opportunities outweighing risks.

Forecast

Continued positive fundamentals with increased market volatility. Trade tension and other global & domestic political uncertainty, U.S. corporate earnings, Federal Reserve interest rate strategy, and inflation are at center stage.

1. ***Market volatility to continue.*** We see volatility continuing as over optimism and over pessimism take hold with respect to risks and uncertainties.
2. ***Trade tensions to affect the markets.*** We see as positive, recently announced steps toward partial agreements. Any sign that we are moving toward agreement rather than escalation is a positive. We believe all-out protectionism will be avoided but carries significant risk.
3. ***Tax reform affects subsiding.*** The economy is experiencing declining positive stimulus from tax reform. However, the benefits of lower taxes should have a long tail both in consumer spending, capital spending and corporate profits. Our concern relates to the risk of higher federal deficits and ultimately higher interest rates if economic growth stalls.
4. ***Corporate earnings to decelerate following record 2018 growth rates.*** Following a year of dramatic corporate profit growth in 2018, we believe corporate earnings will continue to grow at a modest pace when you net out the one-time windfall from the 2018 tax reform law.
5. ***Federal Reserve to drop rates further.***
6. ***Long bond returns pressured.*** With the remarkable drop in yields of the long bond, we believe risks are greater that yields will rise rather than fall over the intermediate term. We will remain "short" with our fixed income strategy.
7. ***Inflation steady.*** Inflation has remained calm and we could see some slight nudging upward due to the tight labor market.
8. ***Business & consumer confidence will remain solid.*** Political infighting and trade tension will restrain confidence. However, the strength of the consumer financial situation and jobs market will buoy confidence.
9. ***Oil prices could surprise on the upside.*** Unpredictable and sometimes violent tension in the mid-east could move oil prices higher.
10. ***U.S. Economic growth continues.*** Economic growth and corporate profits should continue albeit at a slower pace.
11. ***Employment continues strong.*** The labor market will continue to produce historically low levels of unemployment and the labor force participation will increase.
12. ***Stock market will be bumpy but will generate positive returns for 2019.***
13. ***Our long-term forecast remains unchanged.*** We believe the stock market, while still subject to periodic corrections, is in an upward trend.

In Summary

Our investment strategies change with market conditions but our principles do not. Our long-term optimism remains in tact. We recognize that during times of uncertainty, communication is important. **It is a privilege doing business with you.** We appreciate your confidence in us, especially during uncertain times.

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