

### Equity and Bond Market Update

(as of December 31, 2019)

Index	MTD	YTD
Dow Jones Industrial Average TR	+1.9%	+25.3%
S&P 500 Total Return Index	+3.0%	+31.5%
Russell 2000 Total Return Index	+2.9%	+25.5%
MSCI EAFE Index (net)	+3.3%	+22.0%
MSCI Emerging Markets Index (net)	+7.5%	+18.4%
Barclays US Aggregate Bond TR	-0.1%	+8.7%

### Economic Indicators

	Statistic	Data as of
Unemployment Rate	3.5%	Nov 2019
Gross Domestic Product (GDP)	+2.1%	Q3 2019
Consumer Price Index (CPI)	+0.3%	Nov 2019
Consumer Confidence (1985=100)	126.5	Dec 2019
30-year fixed mortgage rate	3.74%	1/6/2020
Housing Starts (single family)	938,000	Nov 2019
10-Year Treasury Yield	1.92%	12/31/2019

The fourth quarter of 2019 saw equity markets across the globe continue their upward advances, much unlike the fourth quarter of 2018 which was exactly the opposite. Recall we were in bear market territory in most equity markets as we closed out December of 2018; but 2019 was a different story. The fourth quarter of 2019 saw large-cap U.S. stocks advance +9%, small-cap U.S. stocks +10%, foreign developed markets +8%, and emerging markets +12%. This broad-based global rally took place during continued China-U.S. trade tensions, heightened worries in the Middle East, a determined U.S. House of Representatives to impeach President Trump, and a contentious U.S. Democratic Presidential primary season. Also, aggregate bond markets held values from gains attained from earlier in the year.

With markets performing so well in 2019, it is good to look back to see the catalysts that drove markets to new highs in many areas of portfolio allocations.

1. The Federal Reserve cut the Fed Funds rate three times in 2019, reducing from 2.50% at the beginning of the year to 1.75% by year-end. These rate cuts were a quick turnaround from the policy the Fed carried throughout 2018, but market turmoil and pressure changed that stance in early 2019. By mid-year, the Treasury yield curve had become almost completely inverted; by year-end these rate cuts had restored the yield curve to a normal state, which had quite an impact on equity markets in the fourth quarter.
2. The top three performing sectors in 2019 were: Technology (+50.3%), Communications Services (+32.7%), and Financials (+32.1%). The lowest performing three sectors were Energy (+11.8%), Health Care (+20.8%), and Basic Materials (+24.6%). Note the worst performing sector, Energy, was still up over double-digits for the year, returning well over the historical 10-year annualized average for the overall S&P 500 Index during this bull run of just over +11.1%.
3. Low interest rates and a consistently growing economy boosted the Real Estate sector which returned just under +30% for the year.
4. Over 90% of the stocks in the S&P 500 Index saw positive returns in 2019.
5. Even though both stock and bond markets saw positive returns in 2019, these markets continued to be negatively correlated overall. On average, when stocks were up, bonds were either up marginally or down, and vice versa.

For 2020, we are anticipating continued advances in the stock market as the economy continues to experience consistent growth and low unemployment. Recently, there has been a lot of focus on the slowdown in manufacturing in the U.S., with the ISM Manufacturing Index falling below 50 over the last few months. We have seen this index fall below 50 a few times over the last decade-plus during the current bull market, only to advance back over the 50 level signaling growth. Also, the larger, and less "sentiment-based" ISM Non-Manufacturing Index has been advancing well over the 50 level over the last few months, signaling growth in a more prevalent part of the U.S. economy.

As of December 31<sup>st</sup>, The S&P 500 Index was trading slightly overvalued by about +5% based on reported trailing earnings, but at fair value

## Major Market Indices Price Return (YTD as of December 31, 2019)



based on forward projected earnings for 2020. We will be placing a focus at the beginning of 2020 on foreign markets, due to their persistent undervalue status in relation to domestic U.S. equities. Currently, the ACWI ex-US Index (All Country World Index without the U.S. included) is trading at 14.2 times forward earnings, while the S&P 500 Index is trading at 18.2 times forward earnings. A valuation discount, with foreign stocks currently trading at 78% of their U.S. counterparts based on forward expected earnings, is not uncommon, but the average discount over the last 20 years has foreign stocks trading at a higher 88% of their U.S. equivalents. Bottom line is that foreign stocks still look cheap, and with emerging markets showing the strongest uptrend among the major equity classes, we can't overlook the potential opportunity.

All in all, we anticipate returns in 2020 to be closer to the norm, especially after last year's stellar gains. Those recession indicators that were flashing in the first half of 2019 are mostly gone at the current moment, but we are closely watching their return at some point and will make adjustments where required.

Always keep in mind that fear, panic and optimism are not investment strategies, but rather emotions that drive short-term markets.

Please contact Lifestyle Asset Management, Inc. at (281) 612-2035 or by email at [pjackson@lsaminc.com](mailto:pjackson@lsaminc.com) should you have any questions or comments.

### Sources:

S&P Dow Jones Indices website ( <a href="http://us.spindices.com">us.spindices.com</a> )	MSCI Barra website ( <a href="http://www.msclubarra.com">http://www.msclubarra.com</a> )
Bankrate.com ( <a href="http://www.bankrate.com">www.bankrate.com</a> )	The Conference Board ( <a href="http://www.conference-board.org">www.conference-board.org</a> )
Bureau of Labor Statistics ( <a href="http://www.bls.gov">www.bls.gov</a> )	Bureau of Economic Analysis ( <a href="http://www.bea.gov">www.bea.gov</a> )
United States Census Bureau website ( <a href="http://www.census.gov">www.census.gov</a> )	JP Morgan Guide to the Markets

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