Texas Instruments Alumni Assoc.
Market and Tax Update
February 20, 2020

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<u>Agenda:</u>

1. 2019 Review
2. 2020 Outlook
3. What Do We Do Now?
4. Q & A
5. Tax Law Update
6. Q & A

Q4 2019 Economic & Market Review – U.S. Growth Continues, Caution Increases

Advisor Group Product Research

	Beginning of year	31-Oct	30-Nov	31-Dec
10-year Treasury Yield	2.69%	1.69%	1.78%	1.92%
Gold (London pm fixing per ounce in U.S. dollars)	1279	1511	1460	1515
WTI Crude Spot Price (per barrel in U.S. dollars)	45.15	54.02	58.12	61.14
VIX Index	25.42	13.22	12.62	13.78

All economic and market data as of December 31, 2019. Sources: Federal Reserve Economic Data (FRED), U.S. Energy Information Administration (EIA).

Economic Review

In October, the Federal Open Market Committee (FOMC) cut the Fed Funds rate (the rate banks charge each other for overnight lending) by 25 basis points for the third time in the year, to a range of 1.50% to 1.75%. The rate, however, was left unchanged in the FOMC's December meeting – the last of 2019. Most committee members expect rates to remain unchanged in 2020. However, the FOMC indicated that while the current policy supports "sustained expansion of economic activity, strong labor market conditions, and inflation [near 2%]," it would monitor "global developments and muted inflation pressures." Additionally, the Fed's balance sheet grew from $3.8 trillion to $4.2 trillion between August 28 and December 25, 2019, rebounding from the gradual decline seen between October 2017 and August 2019. While not called "quantitative easing," the effect is accommodative.

Trade tensions appeared to ease in the fourth quarter as the U.S. announced in October that it had reached a "phase one" trade deal with China that would reduce some tariffs on Chinese goods, increase Chinese purchases of American (mainly agricultural) goods, and strengthen intellectual property protections in China. The agreement had not yet been signed by the end of the year but neither country proceeded with tariff increases planned for December. Additionally, the U.S. House of Representatives voted 385-41 to approve a revised United States-Mexico-Canada Agreement (USMCA), with a Senate vote expected in 2020. The Mexican Senate has approved the USMCA while a vote is still pending in Canada.

Although overshadowed by U.S.-China developments, trade tensions with European countries rose as the U.S. threatened additional tariffs following a Word Trade Organization (WTO) ruling in its favor regarding European subsidies for Airbus (a case against the U.S. in relation to American subsidies for Boeing is pending), as well as a French digital tax. The U.S. also announced tariffs on Brazil and Argentina.

On the political front, on December 18, 2019, the U.S. House of Representatives voted along party lines to impeach President Trump. Once articles of impeachment are submitted, the trial will take place in the U.S. Senate, where a two-thirds majority vote is required for a conviction and Republicans hold 53 of the 100 seats. U.S. equity market indices, which have increased since impeachment proceedings were announced in September, do not seem to have been negatively impacted. President Trump is the third president in the U.S. to have been impeached, after Richard Nixon and Bill Clinton.

The year ended on a positive note with generally favorable, albeit weakening, economic indicators in the U.S. However, fears of an escalating conflict between the U.S. and Iran grew when, on January 2, 2020, a U.S. drone strike in Iraq targeted and killed a key Iranian military commander. U.S. equities remained positive for the year to January 3, 2020, but global equities pulled back, the 10-year U.S. Treasury yield declined to 1.79%, gold increased to $1,549 per ounce, and WTI oil futures increased to over $63 per barrel.

Below is a look at the key economic indicators that Advisor Group monitors on a regular basis and their most recent level of strength.

Key Economic Indicators:

No current indications of weakness in this economic indicator

Economic indicator is slowing or demonstrating steady-but-slow growth

Economic indicator is flat or contracting

Economic Indicator:	Current Strength Level:	Commentary:
Leading Economic Indicators (Source: Conference Board)		The latest readings point to a potential slowdown in overall economic output. The index declined 0.2% in each of September and October and remained unchanged in November.
U.S. Employment (Source: BLS, FRB of Atlanta)		The unemployment rate remained at a historic low of 3.5% in November. After declining between August and October, non-farm job growth increased to 266,000 in November, the highest since January 2019. Nominal wage growth increased to 3.7% in

		November. Wage growth ranged between 3.4% and 3.7% during 2019.
GDP Growth (Source: BEA)		Slow and steady growth in GDP with third-quarter GDP growing by an estimated 2.1%.
Retail Sales (Source: U.S. Census Bureau)		Monthly retail sales growth slowed from 0.7% in July to 0.2% in November. Retail sales in November were 3.3% higher than a year earlier. This is an area that we are closely watching for signs of a slowdown although thus far figures remain relatively healthy.
Housing (Source: U.S. Census Bureau, National Association of Realtors, S&P)		New home sales saw a 2.7% decline in October and a 1.3% increase in November. In August 2019, existing home sales reached their highest level since March 2018, but declined 2.7% between August and October 2019. The Case-Shiller national home price index showed 3.2% and 3.3% year-over-year growth in home prices in September and October, respectively. The index has been increasing since January 2019.
Inflation (Source: BLS)		Annual inflation increased to 2.1% in November, compared to 1.8% in October and 1.7% in September. That is the highest rate since November 2018. The core inflation rate stood at 2.3% as of November.
Manufacturing (Source: ISM)		Manufacturing has remained in contraction since August 2019 with the Purchasing Managers' Index (PMI) reading dropping to 48.3%, 48.1%, and 47.2% in October, November, and December, respectively. The December reading was a 10-year low. A reading below 50% indicates a contraction.
Consumer Confidence (Source: Conference Board)		The Conference Board Consumer Confidence Index was 126.5 in December and has remained relatively stable since September, when the index declined to 126.3 versus 134.2 in August. The board indicated that

		there is "little to suggest" that consumer spending "will gain momentum in early 2020."
Fixed Income Yield Curve		After briefly going negative in August, the spread between the 10-year and 2-year Treasury rates trended positive for the remainder of the year. After remaining negative since May, the spread between the 10-year and 3-month Treasury rates turned positive in October and trended up for the remainder of the year. An inverted yield curve, particularly a negative spread between the 10-year and 2-year rates, can be a recession indicator.
Equity Markets		The S&P 500 ended the year with a total return of 31%, the highest annual return since 2013. Annual standard deviation also increased to 16%, the highest level since 2009. Analysts also noted that performance was driven by P/E multiple expansion, as opposed to earnings growth, which could be a concern.
Federal Reserve Policy		The Federal Reserve continued its accommodative stance with one more rate cut in the fourth quarter, but has indicated it does not expect further cuts in 2020. Foreign central banks, including China's, also remained accommodative.
Corporate Profits (Source: FactSet)		According to FactSet, the S&P 500 is expected to show a decline in earnings of 1.5% in December, which would make it the fourth consecutive quarterly decline.
Geopolitical Risks		Geopolitical risks are elevated, particularly due to rising tensions between the U.S. and Iran at the start of the year. Trade wars continue but could see a reprieve if the "phase one" deal between the U.S. and China is formalized. An election in the U.K. in December offered some certainty the Brexit

		will happen in January 2020. Protests flared across the globe, including Latin America, Hong Kong, India, and the Middle East.
Google Searches for "Recession" Followed by Year. (Example: "recession 2020.")	🟡	Often, a soft economy can be tipped into a recession by consumers and businesses retracting just a small amount. It's a newer indicator, but Google searches for recession followed by the year was a very good early indicator of the Great Recession that started in late 2007. Interest in "recession 2020" has been elevated since September as compared to earlier in the year, but has declined since it peaked in August.
Advisor Group's Economic View	🟡	We remain cautious in the outlook for the U.S. economy. The U.S. is currently experiencing its longest expansion in history. In recent months, we have seen signs of slowing growth in the U.S. economy while parts of Europe may be entering a recession. The Federal Reserve is preemptively attempting to lessen the chances of a recession; however, we believe there is an elevated chance of an economic slowdown in 2020 and a recession is very possible. It is important that investors hold a highly diversified portfolio to help counter any potential weakness. At the same time, those with intermediate and long-term investment horizons may find very attractive opportunities with any price weakness in financial markets.

	Q3 19	Q4 19	2019
S&P 500	1.19%	8.53%	28.88%
Russell 2000	-2.76%	9.52%	23.72%
NASDAQ	-0.09%	12.17%	35.23%
MSCI EAFE (USD)	-1.71%	7.81%	18.44%

UK (FTSE)	-0.23%	1.81%	12.10%
Germany (DAX)	0.24%	6.61%	25.48%
Japan (NIKKEI)	2.26%	8.74%	18.20%
MSCI Emerging Markets (USD)	-5.11%	11.36%	15.42%
Barclays Aggregate TR	2.27%	0.18%	8.72%

Market data as of December 31, 2019; all Price Return with the exception of Barclays Aggregate TR.

Markets Review

- **Domestic equities** turned decidedly positive during the fourth quarter, extending the longest bull market in U.S. history. According to FactSet, the 12-month forward P/E ratio for the S&P 500 was 18.3 as of the end of December, which is above the five-year average of 16.7 and 10- year average of 14.9. Small-cap stocks, as measured by the Russell 2000 Index, outperformed the broader market for the quarter but slightly underperformed for the year. On a total return basis, the S&P 500 Value and S&P Growth indices were about even for the year at 32% and 31%, respectively, while the Russell 2000 Value index underperformed the Russell 2000 Growth index with returns of 22% and 28%, respectively. Drilling down into S&P sector total returns, technology was the best performer for both the quarter and the year with a gain of 14% and 50%, respectively. Real estate was the worst performing sector for the quarter with a loss of 1%, but closer to the median for the year with a gain 29%. Energy was the worst performing sector for the year with a gain of 12%, but closer to the median for the quarter with a gain of 6%.

- **International equities** were higher across the board during the fourth quarter and for the year despite concerns of slowing economies across the globe. International equities were in part aided by accommodative central banks, including the Fed, which cut its target rate in the fourth quarter and continued asset purchases; the ECB (Europe), which maintained a refi rate of 0% and continued asset purchases; the BOE (England), which maintained an accommodative bank rate; the BOJ (Japan), which maintained a negative base rate; and the PBOC (China), which cut its base rate and lowered reserve requirements. U.K. stocks were helped by the reduction in uncertainty surrounding Brexit, but hurt by fears of the negative impact of Brexit.

- **Fixed income** markets generally underperformed other asset classes for the fourth quarter as interest rates increased, with the yield on the 10-year Treasury note moving up from 1.68% in

September to 1.92% in December. Yields across the globe remained relatively low in response to concerns around global economic growth, heightened geopolitical risks and low inflation in most parts of the world. The benchmark Bloomberg Barclays Aggregate Bond Index rose 0.18% for the quarter. All major fixed-income sectors rose during the quarter with high yield and emerging market bonds outperforming with gains of more than 2%.

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