Market Review with Ted Halpern

The Best Year for Domestic Equities Since 1997

The third quarter of 2019 illustrated the resiliency of U.S. markets. For the first time so far this year, markets faced significant volatility, but showed wonderful resolve and finished the quarter with decent gains. The S&P500 gained 1.7% and the Dow Jones Industrial Average (DJIA) gained 1.8% despite storms brewing in the markets.

Did you know 2019 has been the best year for domestic equities since 1997…that’s more than two decades! The year-to-date numbers are simply outstanding, but as usual, good news is rarely well publicized. The YTD and quarter-to-date numbers tell a story.

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<th>S&amp;P 500</th>
<th>DJIA</th>
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<td>Q3</td>
<td>1.7%</td>
<td>1.8%</td>
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<tr>
<td>YTD</td>
<td>20.6%</td>
<td>17.5%</td>
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The story involves a healthy and stable economy with an employed consumer. We likely are late in the business cycle and earnings are slowing, but markets have produced thus far in 2019 in a huge way!

As we enter October, many investors are fearful—and not just because of Halloween. Part of it is superstition and October’s reputation for market mayhem. Strangely, the crash of 1929, Black Monday in 1987, and the significant problems of 2008’s financial crisis all occurred in October. These were very serious events, but if you look at the data, it’s clear that October is not haunted. In fact, over the past 20 years, October has been the second-best month of the year for the S&P 500 and DJIA over the past 20 years (source: Stock Trader’s Almanac).

*Remember, the S&P 500 and DJIA are a proxy for the performance of broad equity markets. It’s a way to take the temperature of markets in general, and is not a benchmark for your individual portfolio, which is a diversified mix of asset types.*
Looking Ahead

To be fair, there are a few events upcoming in October likely to shape the rest of the year—and any of them could create volatility to the upside or downside.

- U.S./China have scheduled talks this month.
- Earnings season is expected to give us a third straight quarter of slowing profits.
- The U.K. faces an October 31 deadline to exit the E.U.

Historically, markets are susceptible to pullbacks in October after a year with a big bullish run, where the S&P 500 has set a record close and where the general expectation is for slowing growth ahead. Well, the YTD numbers certainly indicate a bullish run. We have had 3 record closing milestones for the S&P so far this year. And, if you’ve been reading these commentaries regularly, you’re aware we have been expecting slower growth for some time now. All of these factors are on the table…so should investors be fearful this October?

To give you some insight—recently, I went to an Economic Forum where an economist from JPMorgan was speaking. He said the U.S. economy is made up of the “3 S’s: Strong, Steady, and Slow—and while the risk factors right now do not merit great concern, it could be a good time to put your portfolio in bubble wrap.

Control what is within your control, and remain an optimistic investor!

Rest assured, Halpern Financial portfolios are designed to weather challenges like a potential market downturn. Your portfolio benefits from our strategy based on long-term and well-tested investment methodologies. Over the past few quarters, we have taken further steps to mitigate this late business cycle we find ourselves in. These steps will help your portfolio continue to prosper during uncertainty while protecting the strong returns we have experienced. A consistent process of portfolio rebalancing, security monitoring and a focus on real value will serve you well during this final quarter in 2019 and beyond.

As always, we focus on the elements we that are within our control. This helps us to be prepared for those market events out of our control. Always remember you must remain an optimistic investor.

As we look to the quarter ahead, we wish you a joyous holiday season with plenty of health, wealth, and happiness.
Quarterly Commentary

Investment Commentary with Kirsty Peev, CFP®

Summary:

A phenomenal year-to-date, and strength amid volatility in the third quarter.

Continued gains in U.S. markets. The third quarter of the year provided markets with far greater challenges to overcome than at the start of the year, and resulted in significant levels of volatility. However, positive returns remained and large-cap U.S. markets delivered additional healthy returns during Q3. U.S. markets have shown strong levels of resiliency!

Cautious investors led higher risk-level assets to lag. Stocks of smaller companies, and stocks from emerging market countries struggled to overcome headwinds during Q3 and delivered negative returns. Still very healthy year-to-date numbers.

Bond markets delivered stellar, equity-like returns over the past 9 months, giving us very strong gains for the quarter and year-to-date! This is a good sign of strength, given the TWO Federal Funds rate cuts during the quarter.

U.S. Equities:

Resilient markets prevailed. The trade war has been going on for more than a year now. During this time there have been repeated calls for the next recession, intense focus on slowing economic growth, sensational headlines around an inverted yield curve, a history-making separation of a key member country of the E.U. in the works and a variety of other headwinds. In the face of all these challenging factors, the S&P500 is up 4.3% during the last 12 months, and a staggering 20% for the YTD. Markets tend to fall back on the fundamental economic data once the noise around headlines and specific events recedes—and fundamentals are strong.

U.S. equities held up incredibly well in the face of extreme Q3 volatility and market-moving headlines. The third quarter may have felt more muted than the first two of the year. However, given the headwinds facing markets and the broader economy, the positive returns are especially impressive.

During volatile times, our low-volatility strategy shows its worth. Both YTD and for the quarter, the minimum volatility fund we selected has performed very well. The fund determines the risk profile of the stocks it can hold, and how the holdings interact with each other to create an overall portfolio that shares some characteristics with broad equity markets, but with less volatility. It also places constraints on individual holdings and sectors to avoid overweighting in any one area. We continue to favor this approach given the expectations of volatility ahead, though we maintain exposure to higher risk-reward holdings as well, in proportion to each portfolio’s individual needs.
International Equities:

Developed international equities have lagged the U.S. due to the looming specter of Brexit plus trade issues with other countries. Brexit itself is an ever-changing situation. The current PM hung his hat on taking Britain out of the E.U. regardless of any deal. Despite efforts to come to a deal, no workable solution has been presented yet. This is a great unknown for both the U.K. and the E.U. A few months ago a ‘hard Brexit’ appeared unthinkable….now we are just 1 month away from it! An extension of the deadline appears to be the most likely course of action. The dividend yield on indices from the European region remains attractive. This could help prop up investor interest in the asset class as a whole.

International countries are easing monetary policy alongside the U.S. The central banks of many countries around the globe have cut rates, as the Fed has done in the U.S. These moves are an effort to create an easier money environment to continue to stimulate economic growth. The rate cuts have been prompted by concern about the potential impact of the trade war on global growth and corporate profits.

China faces headwinds from massive anti-government protests in Hong Kong, the ongoing trade war and a potential credit bubble. China and other emerging markets countries have experienced a huge debt boom in recent years and there is potential for a bubble. We specifically keep allocations to emerging markets limited as the risk-return profile is very high.

Bonds:

All bond asset classes delivered healthy positive returns. The third quarter added to the gains from earlier in the year and most bond categories have now delivered equity-like returns in just 9 months of the year. This is especially impressive when you consider the rapidly changing interest rate environment.

The Fed cut interest rates twice during the third quarter to help stimulate continued economic expansion. Longer term bonds thus delivered even more outsized positive returns, as the short end of the curve was most affected by changes to the Fed funds rate.

The Yield curve inverted. This means the 2 year Treasury note yield traded above that of the 10 year note, for the first time in more than a decade. The inversion increased recession fears since an inverted yield curve can serve as an early warning of a potential recession. This is because it suggests monetary policy and financial conditions may be constraining the economy. We believe the Fed is firmly committed to adjusting monetary policy as necessary to avoid a recession and the 2 recent rate cuts demonstrate this.

Foreign demand for U.S. Treasuries is high as some international sovereign bonds are delivering negative yields. European demand for U.S. Treasuries particularly high. This contributed to a price rise / yield drop seesaw effect as prices and yields are negatively correlated.

Expectations are now very mixed about potential Fed movements ongoing. Fed members were divided even about the September cut. Some members wanted to keep rates unchanged, citing the strong job market, and a couple of members wanted to do a 0.5% rate cut. Demonstrates uncertainty about how the trade tensions will affect an otherwise strong economy.
Expectations and Perceptions for the Future:

EQUITIES

Trade issues will provide market momentum.
Most of the headlines focus on the trade situation with China. Talks appear to be going well and we believe it is in both countries’ best interest to avoid an all-out trade war. Steps are being discussed to soften the impact and provide relief to companies harmed by the tariffs.

The U.S. and E.U. also have been quietly exchanging trade barbs. E.U. tariffs went into place on American steel, aluminum, and large aircraft. The U.S. responded by placing tariffs on popular goods like Scotch Whisky, Italian cheese and other European food products. We will continue to monitor this situation and potential impact on the global economy.

The U.S. and Japan reached a limited trade deal in Q3 that is likely a positive for both sides.

Economic growth is strong and the unemployment rate is at just 3.5% – a 50 year low! Any slowdown in economic growth will keep recession speculations alive for investors who have become nervous after sustained market gains.

Major central banks appear committed to taking steps to sustain economic expansion.
Central banks have cut rates or implemented easier monetary policies in recent months. These stimulative monetary conditions are likely to operate with a time lag, so we may see the positive effects globally going forward.

Volatility will likely remain elevated around headlines related to trade negotiations, recession predictions and Brexit.

EQUITIES

BONDS

Bonds have 3 key purposes:
- Equity diversification
- Stability
- Income

The bond holdings within your portfolio have demonstrated these functions incredibly well this year. We are very confident in the diversified, laddered approach we have implemented to navigate changing interest and economic environments going forward.

Opinions are dividend on the Fed’s path with interest rate going forward. Fed members were not unanimous on the recent cut. There was also language from Powell suggesting the cuts were not a new normal. As the Fed always says, future moves will be data dependent.

Municipal bonds continue to be very attractive – high demand and low supply. These continue to serve an important and attractive role within taxable accounts.

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