

## Outlook

Global markets ended the quarter, the year, and the decade with several pro-risk momentum drivers including a notable move higher in liquidity, a hiatus in global trade conflicts, stabilizing global growth indications, and the beginning of a reconciled Brexit situation in Europe. These developments, particularly global liquidity, lead us to believe that global growth will accelerate in 2020. Our base case is that central banks will remain dovish, Chinese policy will maintain and increase stimulus, the global manufacturing cycle will begin to rebound, the USD will begin to weaken, and that both interest rates and commodities will drift slowly higher.

Political considerations (trade deals, tariffs, elections, armed conflicts) always pose risks and certainly factor into our current outlook but generally are shorter-term in nature and are often overcome by the liquidity backdrop and corporate fundamentals. The Fed's 'It's not QE' QE program has re-expanded the balance sheet by over 50% (\$400b) that the quantitative tightening program accomplished. Chinese credit, fiscal, and monetary impulses are moving higher and data in Europe show fiscal stimulus and beginnings of a manufacturing recovery. Encouraging fiscal, monetary, and economic (housing, jobs, consumer) developments in the U.S. also support a relatively constructive view.

## Economic Overview

The close of the fourth quarter marked the longest economic expansion in U.S. history at 10 ½ years. Since 1854, the average expansion has lasted 17 ½ months, so this most recent period represents 7x the historical average in terms of longevity. It has also been the shallowest recovery of the ten longest expansions on record, suggesting the possibility of continued economic growth going forward. U.S. economic growth for the fourth quarter is projected at 1.8%-2.1%, in line with growth achieved for the

calendar year 2019, while global growth of 2.4%(e) weathered a global manufacturing recession, posting its lowest growth rate since the GFC. A resilient U.S. consumer and global services sectors benefited from significant policy stimulus globally in the fourth quarter, including additional quantitative easing, money supply growth, lower bond yields, and additional fiscal spending. The percentage of countries exceeding their prior year economic growth rates bottomed in August 2019 at 13% and has since risen to 56% in early 2020.

### The U.S. Consumer

The labor market continues to show signs of strength and bolstered the view of a healthy U.S. consumer, as did the 6.1% increase in retail sales during 2019—the highest growth rate since 2012. Consumer confidence and consumer sentiment indices remained at fairly high levels throughout the quarter and business confidence measures began to improve in conjunction with progress on trade negotiations and the reduction in tariffs. Low mortgage rates and modest home price appreciation resulted in strong housing sales through the end of 2019, currently at their highest levels since the GFC.

### Inflation & the Federal Reserve

Inflation readings and inflation expectations both remained benign throughout the quarter with the most recent annualized headline and core PCE registering 1.5% and 1.6% respectively (the Federal Reserve targets an overall annual inflation rate of 2%). Average hourly earnings of 2.9% have remained stable while alternative inflation measures of core PPI (1.1%) and core CPI (2.3%) were also reasonable. The FOMC implemented its third and final rate cut of 2019 in October, moving the rate from 1.75%-2.0% to 1.5%-1.75%. The Fed stated in December that it expects to keep the rate at current levels throughout 2020 barring any material change in inflation data.

## Equity Markets

### U.S. Equity

Domestic equity returns were strong across the board in the fourth quarter, delivering results that would be considered respectable for a full calendar-year return in many cases. Large-cap stocks, as proxied by the S&P 500 Index, were up over +9% in the quarter and small-caps, as proxied by the Russell 2000 Index, delivered almost +10%. Among S&P 500 sectors, three delivered double-digit returns in Q4: Financials (+10.5%), Health Care (+14.4%) and Info. Tech. (+14.4%). The S&P 500 returned over +31% for calendar year 2019, the Russell 2000 returned over +25% and the NASDAQ Composite posted over +36%, a banner year by practically any measure.

### International and Emerging Market Equity

As the U.S. and China made progress on improving the rhetoric and expectations surrounding a “Phase 1” trade deal that would begin the process of normalizing the supply chain disruptions that tariffs have caused, international equity markets moved markedly higher in the fourth quarter. In U.S. dollar terms, the MSCI EAFE Index, a proxy for non-U.S.

developed markets, increased over +8%, returning over +22% for the year. Emerging markets increased almost 12% in dollar terms, finishing 2019 up almost +19%. As clarity began to emerge on the Brexit timeline and process, the U.K. market rose +10%, with over half of that occurring in December after parliamentary elections resulted in an overwhelming victory for Prime Minister Boris Johnson’s Conservative party.

## Fixed Income Markets

The US 10-year treasury yield declined from 2.03% to 1.68% during the quarter, reaching its lowest levels since 2016’s Brexit vote. Although rates in the U.S. have fallen significantly, they remain well above those of most other developed countries; it is estimated that over 25% of all government bonds are yielding below 0%. Corporate credit fundamentals remain solid with reasonable balance sheet leverage, strong interest coverage, and low default rates. As a result, most fixed income sectors produced strong returns in the quarter. The Bloomberg Barclays U.S. Aggregate Bond Index advanced 2.27% in the quarter, bringing the year-to-date return to 8.52%.



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