

Quarterly Missive

FOURTH QUARTER 2019

BY JAMES H. DRYDEN

Not so very long ago we were writing about some challenging summer months for the financial markets, inverted yield curves, recession fears and gathering storm clouds that threatened the economic recovery and bull market in stocks. Then lo and behold, the economy rebounded and the financial markets recovered. Global equities posted their best November since 2009 and the S&P 500's 3.4% rise occurred while the index notched record highs in more than half of the month's trading days, according to Wells Fargo Investment Institute (WFII). As of this writing (12/12/2019) stocks remain within a percent or so of their all-time highs.

So what happened?

We believe the story behind November's rally was simply one of positive trade developments and better-than-expected economic data and corporate earnings. As we wrote in September, we believed stocks would applaud any real signs of trade progress with China, and that's exactly what we got. President Trump boosted investor sentiment by announcing that negotiations for a "phase one deal" were in the final works and Chinese officials told the U.S. they were working on measures to crack down on intellectual property theft, a key sticking point in past negotiations. The pall cast over the economy and financial markets this year from the trade impasse with China cannot be overstated. In our view, it has been the most noteworthy story we've followed all year, and we've voiced our opinion that the recovery's longevity would depend on better China relations and a roll-back of tariffs. Of course investors have wanted a meaningful de-escalation of the dispute, but even in the absence of real progress appeared willing to embrace equities as long as the rhetoric didn't get any worse.

It's not the *wind*. It's the set of the *sails*.

Beyond the apparent improvement in trade, it's the economy which – more than ten years into recovery – we believe has continued to impress economists and even pessimists alike. According to First Trust Advisors, third quarter Gross Domestic Product (GDP) showed the economy grew at an annualized 2.1% pace, better than the initial reading of 1.9%. Inflation and interest rates remain low. The unemployment rate continues to hover near 50-year lows. Job growth is robust. Wage growth is solid. The consumer is in good financial shape, with household debt-relative-to-assets at the lowest level since 1984. Consumer spending and retail sales remain impressive, and early reports suggest Black Friday sales were up 14% over the year before.

It all makes us at Westlake Private Wealth Management wonder how much stronger the economy could be had there been some clarity throughout the year on trade.

But more importantly, where do we go from here?

Looking forward, we continue to see mixed signals, however we will lean on the still-positive trend as our basis for optimism. We believe the global economic recovery will remain intact, overall economic activity will continue its upward path and corporate profits growth – facing easier comparisons with 2019 – will be positive. Importantly though, our assumptions require consumer confidence to remain healthy and the trade dispute with China to de-escalate, and we're staying cautiously optimistic with this last point. We remember the near-euphoria of October when the President announced an "agreement in principle" with China only to see talks fail once again.



This time around, we're being more cautious and will be looking carefully at the details. We'll also advise our clients to bear in mind the market's fourth quarter advance has priced in such high expectations for a resolution that we shouldn't rule out a rather measurable market response if the details of any agreement disappoint.

Beyond trade, we're also keeping a close eye on the 2020 Presidential election cycle. History tells us that election years are quite good for stocks – since 1928, only four of the 23 Presidential election years have experienced negative returns in the S&P 500, according to WFII. Returns tend to fare even better during years in which there's an incumbent facing re-election, as the sitting President has a propensity for throwing anything and everything at the economy. We're cautious this time around however, as a myriad of policies, including changes to taxes and spending, are being debated by the various candidates. Our single largest long-term concern centers on government spending, which if allowed to remain uncontrolled, may have a substantial impact on the economy. So as we get deeper into 2020 and turn the corner into Convention season, we'll be closely monitoring momentum amongst the candidates because we believe it will play an influential role in investor sentiment and ultimate market returns.

For where stocks stand today, we cannot help but wonder if we're once again on the doorstep of a Santa Claus rally or a January effect, or whatever it may be called this year. With stocks up 24% on the year (WFII) amidst a healthy economic backdrop, the fear of missing out can play a wonderful role in investor behavior, especially at year's end. And remember, according to MarketWatch, the \$3.4 trillion presently sitting idle in U.S. money market funds may need to go somewhere fast. It bears stating however that markets have a tendency to

trade within ranges, and today the S&P 500 is a mere one-percent from the top. We shouldn't be surprised by a stall at some point - not an outright correction, but a stall - within a still-positive trend. Our bottom-line however remains the same – our glass is half-full.

As the year and the decade wind down, we remind our clients that we are here for them always, doing what we do every day so we can impact their lives for the better. We remain grateful for the opportunity to do this, and so very appreciative of the continued trust and confidence our clients and friends have placed in us.

And most importantly, we wish you the very best the Holiday season ahead has to offer.

This Quarterly Missive utilized research from Wells Fargo Investment Institute (Wells Fargo Investment Institute, Inc. is a registered investment adviser and wholly-owned subsidiary of Wells Fargo Bank, N.A., a bank affiliate of Wells Fargo & Company.), First Trust Advisors, BNY Mellon, MarketWatch, and Birinyi & Associates.



The opinions expressed in this e-mail are those of the author(s) and are not necessarily those of Wells Fargo Advisors Financial Network or its affiliates. The e-mail has been prepared for informational purposes only and is not a solicitation or an offer to buy any security or instrument or to participate in any trading strategy. Investing involves risk including the possible loss of principal. Any index referenced is presented to provide you with an understanding of its historic long-term performance and is not presented to illustrate the performance of any security. Investors cannot directly purchase any index. Past performance is not a guarantee of future results and there is no guarantee that any forward looking statements made in this communication will be attained.