Q1 2020 NEWSLETTER

IMPACT

FINANCIAL STRATEGIES

January 4th, 2020

Wow, another decade has passed. This week, as in most 1st weeks of January, I find that putting dates on signature lines take more effort; in particular, because we've been in the 20-teens for the last 10 years. And while we have to remember to put 20**20** in for dates, can you think back to January 2010, and imagine that a decade later we would will still be in the midst of the longest US expansion since the Civil War? When you consider that we were just 9 months off the market bottom in the Great Recession, it might make a little more sense, but who knew that the last 10 years would be so good from a market standpoint, yet feel so scary and negative the whole time? I've been through it with you.

Having traveled to 6 different states in Q4 to meet with over 1/3rd of you, I know what is on your minds. I know that you are feeling trepidatious of the markets and wondering if this expansion and rally can continue. And with the professional prognosticators coming in all over the board for 2020 expectations (from down 7%, to up almost 13%*) how do you look past the noise and the negativity? Well, that's what I do for you; I will tell you what I am watching and where I believe we are headed in 2020. I'm here to free up your time, give you the confidence to know you are on track, and be your "boots on the ground." Our goal is for you to spend time with those you love doing what gives you meaning.

If the first two trading days of 2020 are any indicator of what we should expect for the full year, one thing stands out; continued volatility and short term, concentrated volatility spikes due to headline risk. The year opened with all three US Indexes notching record highs on the first trading day, only to see a potentially major flare up in the Middle East gave it almost all back the next day. Another expectation I want to prepare you for is more negativity and uncertainty. From the recent uptick in hostilities, the impeachment trial, the 24/7 news feed and the upcoming election, (who else is looking forward to those upbeat messages of inspiration? *wink*wink) it might be a good year to take a long vacation!

What does all this mean? Remember, I believe in fundamentals and having a long-term perspective. The last decade gave us higher than average returns, so a reversion to the mean is normal. Does this mean I expect a negative decade ahead? No, I have confidence in a positive decade ahead, albeit, with lower averages than we have recently experienced. Additionally, even in the face of several uncertainties, (more on that below) **I believe that 2020 will be a positive year in the markets**, and barring some major event, that our chances of a recession during this year are less than 25%. The economy is on sound footing; with low unemployment, low interest rates, rising wages, strong profits, and an expectation of some global growth this year. Yes, there are risks. I am watching them, rest assured.

As always, please feel free to pass this timely perspective along to anyone you think might appreciate it. For your advocacy and your trust: Thank you again! You are why we work so hard. Happy New Year!
Sincerely, Justin

Trade Clarity and Interest Rate Cuts Lead to Big Returns in 2019

Markets welcomed the positive resolution of several key macroeconomic unknowns in the fourth quarter, and that improved clarity sent the broader stock market higher over the past three months. The solid fourth quarter gains helped the S&P 500 index achieve its best annual return since 2013.

At I stated at the start of the fourth quarter, markets were facing four significant macroeconomic uncertainties: Could the U.S. and China strike a trade deal? Would the Fed cut interest rates for a third time in 2019? Could U.S. and global economies stabilize? Would Brexit get passed? Each of these unknowns, which had weighed on markets earlier in 2019, saw positive progress throughout the final three months of the year.

By far, the most important event for markets during the fourth quarter was the agreement to a "phase one" trade deal by the U.S. and China. Since early 2018, the U.S.-China trade war, and the tariffs that came with it, pressured the global economy and weighed heavily on investor sentiment. Twice in 2019, first in May and again in August, tariff increases caused a significant spike in market volatility.

But in mid-October, after intensive negotiations, both the U.S. and China agreed, in principle, to a phase one trade deal that would result in the reduction of some existing tariffs, the promise of no additional tariffs, and increased imports of American goods by China. Anticipation of this "in principle" deal being formally agreed to powered stocks higher from mid-October through mid-December. And then on December 13th, more specific details of the phase one deal were announced, and that clarity helped stocks extend the 2019 rally into year-end.

Improvement in U.S.-China trade relations wasn't the only positive event in the fourth quarter though. The Federal Reserve met market expectations by cutting its benchmark interest rate by another 25 basis points at the meeting on October 30th. That cut brought the total reduction in interest rates in 2019 to 75 basis points, the largest annual reduction in over a decade. Additionally, at the December policy meeting the members of the Federal Open Market Committee showed they do not expect to raise interest rates in 2020. That added clarity for Fed policy expectations, specifically that the market can expect rates to stay low for the foreseeable future, also helped power stocks higher in the fourth quarter.

The global and U.S. economies also showed signs of stabilization in the fourth quarter after losing positive momentum for much of 2019. First, in the United States, concerns were growing that sluggish business spending and investment would potentially cause a broader economic slowdown. But the market's preferred measure of business spending and investment, the monthly Durable Goods report, rebounded in the fourth quarter, easing some of those growth concerns. Internationally, measures of Chinese manufacturing activity, which had shown the industry was in contraction for the past several months, turned positive again in December, and that implied activity was stabilizing. So, while concerns remain about the next direction of the global economy, these signs of progress in the fourth quarter helped stocks rally.

Finally, after three-and-a-half years of Brexit uncertainty, investors can finally expect some progress as the mid-December elections in the United Kingdom resulted in a strong conservative (or Tory) party majority. As a result, the Brexit agreement with the EU is expected to pass Parliament in early 2020.

In sum, the fourth quarter of 2019 was a reminder that macroeconomic fundamentals matter, and the positive news on four key macroeconomic fronts fueled a broad rally in the stock market and makes it more likely, but not certain, that we will see improved global economic growth and better earnings in 2020.

4th-Quarter and Full-Year 2019 Performance Review

The major U.S. stock indices were all solidly higher in the fourth quarter led by the tech-heavy Nasdaq which handily outperformed thanks to rising optimism on U.S.-China trade and expectations for a rebound in economic growth. The S&P 500, Dow Jones Industrial Average and Russell 2000 (the small-cap index) all had smaller, yet positive, quarterly returns. The performance of the major indices in the fourth quarter mirrored the full-year performance, as the Nasdaq easily outperformed the other three indices in 2019 as investors sought the secular growth potential of the tech sector amidst macroeconomic uncertainty.

By market capitalization, large caps outperformed small caps for the full year. That reflected investor concerns about a potentially slowing global economy, as large caps are historically less sensitive to slowing growth than small cap stocks. Notably, however, small caps did narrow the performance gap in the fourth quarter, which implied rising optimism towards the global economy in 2020, following the announcement of the U.S.-China trade deal. From an investment style standpoint, growth outperformed value again in the fourth quarter due to strength in large-cap tech. That widened the performance gap for the full year 2019, as growth considerably outperformed value, again thanks mostly to strength in the tech sector.

On a sector level, 10 of the 11 S&P 500 sectors finished the fourth quarter with positive returns. Technology, financials and healthcare stocks led markets higher in the fourth quarter, which is a reversal from the defensive sector outperformance we witnessed in the third quarter of 2019. Expectations that the U.S.-China trade deal would lead to better economic growth combined with higher bond yields helped power the rally in tech and financials, while healthcare gained on a reduction in political headwinds as candidates who favor expansion of the government healthcare programs, dubbed "Medicare for all," dropped in the polls. For 2019, the big fourth-quarter rallies by tech and financials helped those two sectors outperform on a full-year basis.

Sector laggards in the fourth quarter were the traditionally defensive market sectors. Real Estate was the only S&P 500 sector to finish negative in the fourth quarter, while utilities and consumer staples underperformed the S&P 500 as the U.S.-China trade deal caused investors to rotate into sectors that are more sensitive to a potential upswing in global growth. On a full-year basis, energy was the relative sector laggard as market worries about a slowing global economy combined with the potential oversupply of oil weighed on energy shares, although the energy sector still finished 2019 with a respectable annual gain.

S&P 500 Total Returns by Month in 2019											
Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
7.78%	2.97%	1.79%	3.93%	-6.58%	6.89%	1.31%	-1.81%	1.72%	2.04%	3.40%	2.86%

Source: Morningstar

US Equity Indexes	Q4 Return	2019 Return
S&P 500	9.07%	31.49%
DJ Industrial Average	6.67%	25.34%
NASDAQ 100	12.99%	39.46%
S&P MidCap 400	7.06%	26.20%
Russell 2000	9.94%	25.52%

Source: YCharts

Looking internationally, foreign markets saw positive returns in the fourth quarter thanks mostly to the U.S.-China trade deal, although most foreign markets still underperformed U.S. markets. Foreign developed markets posted solid gains in the fourth quarter but lagged emerging market returns. Emerging markets outperformed both foreign developed markets and the S&P 500 in the fourth quarter thanks to rising expectations for a global economic rebound, combined with some declines in the U.S. dollar. For the full year 2019, foreign markets registered solidly positive returns, with foreign developed markets modestly outperforming emerging markets. However, both underperformed the S&P 500 in 2019.

International Equity Indexes	Q4 Return	2019 Return
MSCI EAFE TR USD (Foreign Developed)	8.21%	22.66%
MSCI EM TR USD (Emerging Markets)	11.93%	18.90%
MSCI ACWI Ex USA TR USD (Foreign Dev & EM)	8.99%	22.13%

Source: YCharts

Commodities enjoyed strong gains in the fourth quarter, led higher by a rally in oil while gold saw a more modest rally over the past three months. Oil prices rose in the fourth quarter thanks to the decision by “OPEC+” to deepen production cuts this year, combined with the U.S.-China trade deal raising expectations for global growth and future oil demand. Gold, meanwhile, spent much of the fourth quarter in negative territory as investors rotated out of the safe-haven metal and into more risky assets following the de-escalation of the U.S.-China trade war. But, a late-year decline in the U.S. Dollar, combined with a mild increase in geo-political tensions, helped gold rally late in December and register a positive return for the quarter. For 2019, commodities produced positive returns which were driven by a large gain in the price of oil, although commodities as an asset class lagged the S&P 500 on a full-year basis.

Commodity Indexes	Q4 Return	2019 Return
S&P GSCI (Broad-Based Commodities)	8.31%	17.63%
S&P GSCI Crude Oil	14.44%	34.09%
GLD Gold Price	2.90%	17.86%

Source: YCharts

Switching to fixed income markets, the total return for most bond classes were positive in the fourth quarter, although longer-dated Treasuries saw mild declines, which is not surprising given rising expectations for a rebound in global growth. The leading benchmark for bonds (Bloomberg Barclays US Aggregate Bond Index) experienced slightly positive returns for the fifth straight quarter.

Looking deeper into the fixed income markets, longer-duration bonds underperformed those with shorter durations in the fourth quarter which was a reversal from most of 2019. That is reflective of a market that is responding to the recent Fed rate cuts and beginning to expect a rebound in global economic growth going forward.

Confirming that improved sentiment, corporate bonds saw solidly positive returns in the fourth quarter as high yield debt outperformed investment-grade debt. The outperformance of lower-quality but higher yielding corporate debt also underscored rising optimism about future economic growth and corporate earnings.

US Bond Indexes	Q4 Return	2019 Return
BBgBarc US Agg Bond	0.18%	8.72%
BBgBarc US T-Bill 1-3 Mon	0.44%	2.21%
ICE US T-Bond 7-10 Year	-1.23%	8.50%
BBgBarc US MBS (Mortgage-backed)	0.71%	6.35%
BBgBarc Municipal	0.74%	7.54%
BBgBarc US Corporate Invest Grade	1.18%	14.54%
BBgBarc US Corporate High Yield	2.61%	14.32%

Source: YCharts

1st Quarter and 2020 Market Outlook

The markets' performance in 2019 was a good reminder of the difference a year can make. In January 2019, the S&P 500 was coming out of its first negative year in a decade; worries about the global economy were surging due to the U.S.-China trade war and the Federal Reserve had just hiked interest rates the previous month.

Now, we begin 2020 on the opposite end of the spectrum.

The S&P 500 just registered its best annual return since 2013, worries about the global economy are receding thanks to the U.S.-China trade deal and the Fed cut interest rates three times in 2019.

For us, the takeaway from this is clear: What happened in the markets last year doesn't mean much for what could happen in the markets this year.

Put in more familiar phrasing: Past performance is not indicative of future results.

So, while the macroeconomic environment is favorable as we begin 2020, a new year always brings new challenges and uncertainties, especially when it's an election year.

More specifically, as we begin 2020, we are monitoring several unknowns that, with the market at historically high valuation levels, and as mentioned above, we expect volatility in 2020.

Regarding U.S.-China trade, markets are now wondering what's in the phase one trade deal. The text of the agreement should be released in early-January, and while sentiment towards the deal is clearly positive, specific details remain very light. At some point, the market will demand that the details of the trade deal meet now-elevated expectations.

Turning to the economy, markets are expecting a rebound in global economic growth. So, the upcoming economic data needs to continue to show signs of stabilization and, ultimately, a re-acceleration of economic growth not just in the United States, but globally.

Looking at domestic politics, markets have ignored the impeachment of President Trump and that's not likely to change as the odds he is removed from office by the Republican-controlled Senate are very low. But there is an election coming in November, and while many analysts don't expect it to begin to influence the markets until later this summer, we could know who the Democratic nominee is by the end of March. Depending on who that person is, it could cause unexpected volatility. Meanwhile, on the geopolitical front, we have relative calm, although tensions with North Korea and Iran are clearly rising.

Bottom line, the fundamental outlook for the economy and asset markets has improved since the depths of the 2018 correction, and stocks have responded accordingly. But it's very important to realize that, despite the strong performance in 2019, markets still face significant uncertainties, and we are committed to monitoring these situations and their impact on the markets and your portfolio.

At *Impact Financial Strategies*, we've been through both good and bad markets, and those experiences ensure that we guard against complacency following a year of strong annual returns. We remain committed to helping you navigate this ever-changing market environment, with a focused eye on ensuring we continue to make progress on achieving your long-term investment goals.

Our years of experience in all types of markets (both positive and negative) have taught us that successful investing remains a marathon, not a sprint. We want to get through the entire race. We are focused on your desired outcomes.

Therefore, it remains critical to stay invested, remain patient, and stick to a plan. That's why we've worked diligently with you to establish a personal allocation target based on your financial position, risk tolerance, and investment time horizon.

The strong market performance of 2019 notwithstanding, we remain vigilant towards risks to portfolios and the economy, and we thank you for your ongoing confidence and trust. Rest assured that our entire team will remain dedicated to helping you successfully navigate this market environment.

Please do not hesitate to contact us with any questions, comments, or to schedule a portfolio review.

Sincerely,

Justin

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* source: https://www.marketwatch.com/story/where-will-the-sp-500-go-in-2020-here-are-the-most-bullish-and-bearish-strategists-2019-12-03

The S&P 500 is an unmanaged index of 500 widely held stocks that is generally considered representative of the U.S. stock market. The Russell 2000 Index measures the performance of the 2,000 smallest companies in the Russell 3000 Index, which represent approximately 8% of the total market capitalization of the Russell 3000 Index. The NASDAQ Composite Index is an unmanaged index of securities traded on the NASDAQ system. The Dow Jones Industrial Average (DJIA), commonly known as "The Dow" is an index representing 30 stocks of companies maintained and reviewed by the editors of the Wall Street Journal. Index performance does not include transaction costs or other fees, which will affect actual investment performance. Individual investor's results will vary. The MSCI EAFE (Europe, Australasia, and Far East) is a free float-adjusted market capitalization index that is designed to measure developed market equity performance, excluding the United States & Canada. The EAFE consists of the country indices of 22 developed nations. The MSCI Emerging Markets is designed to measure equity market performance in 25 emerging market indices. The index's three largest industries are materials, energy, and banks. The MSCI ACWI (All Country World Index) is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of developed and emerging markets. The Barclays US Aggregate Bond Index is a broad-based flagship benchmark that measures the investment grade, US dollar-denominated, fixed-rate taxable bond market.

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The Bloomberg Barclays U.S. Corporate High Yield Bond Index is composed of fixed-rate, publicly issued, non-investment grade debt, is unmanaged, with dividends reinvested, and is not available for purchase. The index includes both corporate and non-corporate sectors. The corporate sectors are Industrial, Utility and Finance, which include both U.S. and non-U.S. corporations. The Barclays Capital US Aggregate Index is an unmanaged market value weighted performance benchmark for investment-grade fixed rate debt issues, including government, corporate, asset backed, mortgage backed securities with a maturity of at least 1 year

Keep in mind that individuals cannot invest directly in any index, and index performance does not include transaction costs or other fees, which will affect actual investment performance. Individual investor's results will vary. Diversification and asset allocation do not ensure profit or protect against loss. Holding investments for the long term does not insure a profitable outcome. Investing involves risk and you may incur a profit or loss regardless of the strategy selected. Keep in mind that there is no assurance that any strategy will ultimately be successful or profitable nor protect against a loss.

There is no guarantee that these statements, opinions or forecasts provided herein will prove to be correct.

The S&P Midcap 400 is a measurement of changes in 400 domestic stocks chosen by capitalization, liquidity, and industry group representation. It is a capitalization-weighted index, with each stock's weight proportional to its market value. This Index includes the effects of reinvested dividends. The S&P GSCI is the first major investable commodity index. It is one of the most widely recognized benchmarks that is broad-based and production weighted to represent the global commodity market beta. The index is designed to be investable by including the most liquid commodity futures, and provides diversification with low correlations to other asset classes. The S&P GSCI Crude Oil index provides investors with a reliable and publicly available benchmark for investment performance in the crude oil market. The Bloomberg Barclays 1-3 Month U.S. Treasury Bill Index includes all publicly issued zero-coupon U.S. Treasury Bills that have a remaining maturity of less than 3 months and more than 1 month, are rated investment grade, and have $250 million or more of outstanding face value. In addition, the securities must be denominated in U.S. dollars and must be fixed rate and non convertible.

The Bloomberg Barclays US Mortgage Backed Securities (MBS) Index tracks agency mortgage backed pass-through securities (both fixed-rate and hybrid ARM) guaranteed by Ginnie Mae (GNMA), Fannie Mae (FNMA), and Freddie Mac (FHLMC). The index is constructed by grouping individual TBA-deliverable MBS pools into aggregates or generics based on program, coupon and vintage. The Bloomberg Barclays U.S. A Corporate Bond Index measures the investment-grade, fixed rate, taxable corporate bond market. It includes USD denominated securities publicly issued by US and non-US industrial, utility and financial issuers. The ICE U.S. Treasury 7-10 Year Bond Index is part of a series of indices intended to assess the U.S. Treasury market. The Index is market value weighted and is designed to include U.S. dollar denominated, fixed rate securities with minimum term to maturity greater than or equal to seven years and less than ten years.