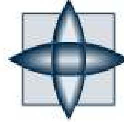
Q4 2019 NEWSLETTER



IMPACT

FINANCIAL STRATEGIES

October 1st, 2019

Today, October 1st, 2019 actually feels like the first day of winter, at least here in Fort Collins, and I find myself without a jacket writing to you on a gloomy and drizzly day. That, combined with the constant barrage of sensational and dramatic (mostly negative) news coming at us faster than ever, can make it difficult to have an unbiased and fair view of what is really happening in the markets and the economy. However, as I did last quarter, I will try to do exactly that. I'll briefly recap some of what transpired over the last three months, and what we are watching as we head into the end of the year.

It is hard to imagine that the first three quarters of this year have been the best three-quarter performance since 1997 in the S&P 500*. And, when we remember how the fourth quarter of last year (2018) felt, it is hard to believe that we are starting the traditionally best quarter of the year for markets*. Nevertheless, the numbers are the numbers, with mores specific info below. But, I thought I would take a moment to catch you up on what is happening here at Impact Financial Strategies first.

Without a doubt, the highlight of the quarter for us was the addition of Keysha. Many of you have already had a chance to talk to her, and if you haven't, then I know the experience will be a pleasurable one. Our team is really clicking, and I am optimistic that it will only get better and lead to a higher quality experience for you. In my entire career, she is the best Client Associate I have ever had, or worked with. We are so grateful that she has joined us. Please feel free to take a look at her biography on our webpage to learn more about her. In addition to Keysha, we are actively looking to add a new member to our team in the role of a para planner. We are hoping to fill that position sometime this quarter. If you know of someone that might be a fit, please pass along their contact info!

The biggest obstacle that I have found during this transition has been getting up to speed on an entirely new system, and learning new software, which includes a much more robust financial planning offering. Please know that my number one goal is to get updated in deliverable financial plans back in your hands as soon as possible. It is hard to understand how long it takes to rebuild 19 years' worth of data. I assure you, however, that the output will be worth the wait. **THANK YOU** for your patience in this endeavor.

Finally, I did hear from some of you as to the value you see in this newsletter. If you did not share last quarter, please let me know your thoughts on this. These offerings take time, and the only reason I am doing it is to add value to you. Please let us know if it is doing so.

Also, please feel free to pass this along to anyone you think might appreciate this timely perspective. For your advocacy and your trust: Thank you again. <u>You</u> are why we work so hard. – Enjoy!!! Justin

MARKETS ARE RESILIENT ONCE AGAIN, DESPITE MORE VOLATILITY

Markets in the third quarter of 2019 looked surprisingly similar to the second quarter as more U.S.-China trade war uncertainty and a lack of clarity on future interest rate policy caused a sharp increase in volatility in the middle of the quarter, but the S&P 500 remained resilient and ultimately recouped those losses to finish the quarter not far from the new all-time highs established in late July.

The third quarter started strong as news of a "trade truce" between the U.S. and China, which was announced at the G20 meeting in late June, combined with better-than-expected second-quarter corporate earnings to propel the S&P 500 to new all-time highs in July. Also helping markets rally was anticipation of the first interest rate cut by the Federal Reserve since 2008, which became reality on July 31st when the FOMC cut the Fed Funds Rate by 25 basis points.

But that strong start to the quarter was quickly undone in early August thanks to increased tariffs between the U.S. and China (the trade truce was short-lived), uncertainty over future Fed policy, and concerning signals from the bond market regarding economic growth and inflation.

The U.S.-China trade truce that was agreed to in late June didn't last much more than a month as President Trump announced new 10% tariffs on $300 billion worth of Chinese imports on August 1st, citing a failure by the Chinese to fulfill promises to increase purchases of U.S. agricultural products. Then, in late August, China retaliated by levying various new tariffs on $75 billion worth of U.S. imports, and President Trump immediately responded by increasing existing tariffs on all $550 billion of Chinese imports. The tariff tit-for-tat weighed on markets throughout August.

Also pressuring stocks in August was uncertainty regarding U.S. monetary policy. As mentioned, the Fed cut interest rates by 25 basis points on July 31st, but they did not definitively signal more rate cuts were coming, and disappointment from that lack of clear guidance, combined with growing worries over future economic growth, added to the volatility in August.

Finally, a closely watched part of the U.S. Treasury yield curve, the "10s-2s spread," inverted (meaning that yields on shorter-term notes exceeded those of longer-term notes) for the first time since 2007. This signal has historically preceded a recession by an average of 18 months, although admittedly, it's not a perfect indicator. Regardless, seeing this signal for the first time in over a decade led to a deterioration in investor sentiment and added to the August volatility.

Despite this trifecta of headwinds, markets again showed impressive resilience in the final month of the quarter, just as they did in the second quarter of 2019.

Early in September, there was improvement in U.S.-China trade relations as President Trump authorized a short delay on the implementation of some of the recently announced tariff increases, and both the U.S. and China agreed to face-to-face meetings in October in another attempt to end the now 18-plus-month trade war.

Additionally, the Federal Reserve cut interest rates for a second time on September 18th and clearly signaled more willingness for future cuts if conditions warranted further action.

Finally, after a brief period of being inverted, the yield curve normalized in early September in part due to better-than-expected U.S. economic data and subsequently easing concerns of a future recession.

Due to the improving market fundamentals listed above, the S&P 500 rebounded solidly in September and came close to matching July's all-time highs, although the initiation of an impeachment investigation by the House of Representatives on President Trump caused a modest pullback late in the month.

In sum, the volatility we witnessed in the third quarter, which remains historically typical, was not surprising due to the numerous macroeconomic uncertainties facing this market and the economy.

But the third quarter was also a reminder that volatility does not automatically mean poor performance. Resilient corporate earnings, stable U.S. economic growth and an accommodative Federal Reserve combined with rising optimism towards U.S.-China trade to offset the volatility and deliver another quarter of positive returns.

Third-Quarter Performance Review – Defensive Sectors Outperform

Major index returns were somewhat mixed in the third quarter as three of the four major indices, the S&P 500, Nasdaq 100 and Dow Jones Industrial Average, finished the quarter with positive returns, while the Russell 2000 saw negative returns. That mixed performance largely reflected the deterioration in U.S.-China trade relations and rising concerns about global economic growth.

By market capitalization, large caps once again outperformed small caps, which is a continuation of the trend witnessed in the second quarter. Large-cap outperformance was partially due to investors reacting to rising future recession fears, as large caps are historically less sensitive to a slowing economy. From an investment style standpoint, growth outperformed value due to strength in consumer sectors, industrials and large-cap tech.

On a sector level, eight of the 11 S&P 500 Index sectors finished the third quarter with positive returns. But in a departure from the first two quarters of 2019, traditional defensive stock sectors with high dividend yields (like utilities and REITS) handily outperformed. Falling Treasury yields and concerns about future economic growth fueled the outperformance of these higher-yielding sectors.

Sector laggards, meanwhile, were the same as the second quarter. The energy sector experienced negative returns again thanks to further declines in the price of oil and the healthcare sector was pressured by continued political risks via increasing calls for the expansion of government healthcare programs, dubbed "Medicare for all," and consistent, yet so far unsuccessful efforts by the government to lower the cost of prescription drugs.

US Equity Indexes	Q3 Return	YTD Return
S&P 500	1.70%	20.55%
DJ Industrial Average	1.83%	17.51%
NASDAQ 100	1.29%	23.42%
S&P MidCap 400	-0.09%	17.87%
Russell 2000	-2.40%	14.18%

Source: YCharts

Looking internationally, foreign markets saw negative returns in the third quarter thanks primarily to concerns about global economic growth. Foreign developed markets declined but relatively outperformed emerging markets due to the European Central Bank cutting interest rates and restarting its quantitative easing (QE) program for the first time since September of 2018. Emerging markets, meanwhile, saw moderate declines thanks to concerns about global economic growth, combined with pressures from a stronger U.S. dollar.

International Equity Indexes	Q3 Return	YTD Return
MSCI EAFE TR USD (Foreign Developed)	-1.00%	13.35%
MSCI EM TR USD (Emerging Markets)	-4.10%	6.23%
MSCI ACWI Ex USA TR USD (Foreign Dev & EM)	-1.70%	12.06%

Source: YCharts

Commodities again experienced mixed returns as gold continued to surge and hit fresh multi-year highs while oil declined. Gold rallied in the third quarter thanks to global central bank rate cuts (the Fed and European Central Bank) and an increase in geopolitical tensions (especially with respect to the U.S. and Iran). Meanwhile, oil was volatile last quarter as short-lived geopolitically driven rallies related to the bombing of a Saudi Arabian oil production facility were offset by rising concerns over slowing global economic growth reducing future energy demand.

Commodity Indexes	Q3 Return	YTD Return
S&P GSCI (Broad-Based Commodities)	-4.18%	8.61%
S&P GSCI Crude Oil	-6.93%	18.15%
GLD Gold Price	4.26%	14.53%

Source: YCharts

Switching to fixed income markets, bonds were broadly higher in the third quarter, as we'd expect given global rate cuts, rising concerns about future economic growth, and still subdued inflation readings. The leading benchmark for bonds (Bloomberg Barclays US Aggregate Bond Index) experienced solidly higher returns for the fourth straight quarter.

Looking deeper into the fixed income markets, longer-duration bonds once again outperformed those with shorter durations which is a continuation of what we observed in the first half of 2019 and reflective of a market that is responding to the recent rate cuts and threats of potentially slowing economic growth.

Corporate bonds saw solidly positive returns in the third quarter, although investment-grade bonds handily outperformed high-yield bonds, and that move to higher-quality corporate debt also underscored concerns about future economic growth and corporate earnings.

US Bond Indexes	Q3 Return	YTD Return
BBgBarc US Agg Bond	2.27%	8.52%
BBgBarc US T-Bill 1-3 Mon	0.54%	1.76%
ICE US T-Bond 7-10 Year	2.72%	9.85%
BBgBarc US MBS (Mortgage-backed)	1.37%	5.60%
BBgBarc Municipal	1.58%	6.75%
BBgBarc US Corporate Invest Grade	3.05%	13.20%
BBgBarc US Corporate High Yield	1.33%	11.41%

Source: YCharts

Fourth-Quarter Market Outlook

Once again, the S&P 500 successfully weathered an increase in volatility this past quarter, as positive current economic fundamentals, interest rate cuts, better-than-expected corporate earnings and renewed hope for resolution on U.S.-China trade helped the S&P 500 maintain strong year-to-date gains.

However, the increase in volatility we saw in May, and again most recently in August, is an important reminder that while markets remain broadly resilient, risks to investment portfolios and the economy need to be carefully monitored. There are still multiple unknowns currently facing investors as we begin the final three months of 2019.

First, the ongoing U.S.-China trade war is clearly the most important influence on the markets. And while there has been rising optimism for some sort of temporary resolution, the fact remains that the U.S. and China still have substantial tariffs in place on imports, with more potentially coming in December. Those tariffs continue to be a headwind on global economic growth, and slowing global growth is a risk to markets that we will continue to watch closely.

Turning to the economy, the outlook remains uncertain. Currently, U.S. economic growth is solid and the envy of the world's developed economies. And, accommodative policy by the Federal Reserve will continue to support that growth. However, Fed rate cuts don't bring guarantees of sustained periods of economic growth, and the ongoing U.S.-China trade war paired with the reappearance of some concerning indicators, such as an inverted yield curve, mean we must remain vigilant in detecting any potential future economic slowdown.

Finally, both domestic and geopolitical dramas require close watching over the coming months. Domestically, the impeachment inquiry of President Trump has the potential to weigh on investor sentiment, while internationally U.S.-Iran tensions are as high as they've been in years, and any conflict between the U.S. and Iran will almost certainly be a negative for stocks, broadly speaking.

Bottom line, U.S. markets were resilient in the third quarter and the performance of most markets year to date remains impressive. However, our experience has taught us that while markets may be resilient, risks still need to be monitored closely, and so we will continue to do so as we have all year.

What happens next with the U.S.-China trade war (will there be a trade truce?), Federal Reserve policy (will the Fed cut rates again in 2019?), and future economic growth (does the yield curve invert again?) will likely determine whether markets maintain, and potentially add to, year-to-date gains—or whether we see similar bouts of volatility like we did in May and August of this year.

We understand that markets always face uncertainties at the start of a new quarter, and we are committed to monitoring these situations and their impact on the markets and your portfolio. Positively, current corporate and economic fundamentals remain solid, and it is those factors that determine the longer-term path of markets, not the latest political drama or salvo in the U.S.-China trade war.

At *Impact Financial Strategies* we understand that volatility, regardless of the cause, can be unnerving, even if it is historically typical. That's why 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 (calm and volatile) have taught us that successful investing remains a marathon, not a sprint.

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 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,

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DISCLOSURES

All Data is effective as of Sept 30, 2019.

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* source https://www.barrons.com/articles/stocks-fourth-quarter-dow-jones-industrial-average-51569878472)

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.