Investment Watch

4th Quarter, 2019

Up, Up & Away

What a Year! What a Decade! Reliable, steady growth rising ***Up, Up & Away*** from the depths of the Great Recession has delivered the longest economic expansion in U.S. history. This historic recovery has also been the weakest on record averaging only 2% GDP growth per year. At the same time, this slow but steady growth has propelled job growth well beyond expert expectations slashing the unemployment rate to 3.5%, the lowest in 50 years. This unique economic expansion was boosted by abnormally low interest rates and muted inflation, likely the result of the unconventional, experimental monetary polices instituted by the Federal Reserve to thwart a financial collapse now ten years ago.

Just like the U.S. economy, this Bull Market has been the longest, but slower than most. A *decade-long expansion* has propelled the longest running stock market Bull in history, lasting 128 months (and still counting) surpassing the '90s 113 months. However the '90s bull market is the strongest on record while the current Bull Market takes a respectable second place. 2019's unexpected, amazing S&P 500 stock performance of 31.49% caped off a remarkable decade of gains totaling over 350%. With any luck it won't foreshadow the demise of this Bull's epic run.

A few months ago, warning signs driven by fiscal downdrafts stirred fears of recession -

- ⇒ Global growth had been slowing,
- ⇒ Trade wars were looming,
- ⇒ The Yield Curve became inverted when long-term rates fell below short-term rates, and
- ⇒ Recession talks filled the airwaves.

Then synchronized global events materialized and have calmed investor fears -

- ⇒ The low point in global growth may be over as world banks embark on more stimulus boding well for foreign economic growth,
- ⇒ A trifecta to rejuvenate global trade: 1) U.S. House of Representatives, in a rare instance of political cooperation, overwhelming passed the U.S. Mexico Canada Agreement updating NAFTA, 2) Britain's political stalemate over BREXIT is resolved, and 3) finally the initial U.S. and China trade agreement is to be signed in early January,
- ⇒ The Federal Reserve lowered short-term interest rates three times in 2019 resulting in a normal yield curve with longer-term rates higher than short-term, and
- ⇒ Both large and small business' confidence spiked higher quieting recession fears.

During the past decade tech companies grew into giants transforming our world. Although the iPhone was first released in 2007, the iPhone revolution really began in 2010 with the release of the iPad and the iPhone 4, incorporating a high-resolution retina display, quality camera and video, and FaceTime. Apple soared to become the first trillion dollar company. The iPhone changed us and the way we navigate our world.

Along with Apple, other tech giants transformed the American landscape. Facebook, Google, Amazon, Netflix, Spotify altered our daily lives from how we communicate with each other, buy things, view and act on our personal relationships, get from here to there, share our experiences, and even wake up in the morning. On the horizon, 5G is hyped to change everything we know and do, all within the next decade.

The tech takeover has rocketed large cap growth stocks to extraordinary heights doubling the return of value stocks over the past there years. However, many analysts believe that growth stocks have risen too far, too fast and that value stocks are now undervalued will outperform their growthy brethren in the future.

Stock market performance is ultimately driven by corporate profits. At times, like over the last two years, there is a disconnect between the growth of profits and gain in stock values. Factset reports, S&P 500 profits rose 18% in 2018, juiced by the tax cut, but the S&P 500 was <u>down</u> 2.8%. This year meager corporate profits only contributed a miniscule 0.8% in gains while the index <u>soared</u> 31.49%. Analysts describe this as Price/Earnings expansion, that is the stock Prices rose but the earnings were virtually zero.

<u>Optimists</u> believe that we are in a *"low for longer"* interest environment which will support higher stock prices for the foreseeable future. They expect profit gains will catch up with these lofty valuations. <u>Pessimists</u> counter that Santa is on a *"flight of fantasy"* and that stock prices are sky high and must return to earth.

Surprisingly, both agree that this historic expansion will survive through next year. Maybe corporate profits will catch up with the valuations or maybe we're on a "*flight of fantasy*". Time will tell, but the 2019 ***Up, Up & Away*** stock and bond gains are in the record books and for the time being they're also in our pocketbooks.

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