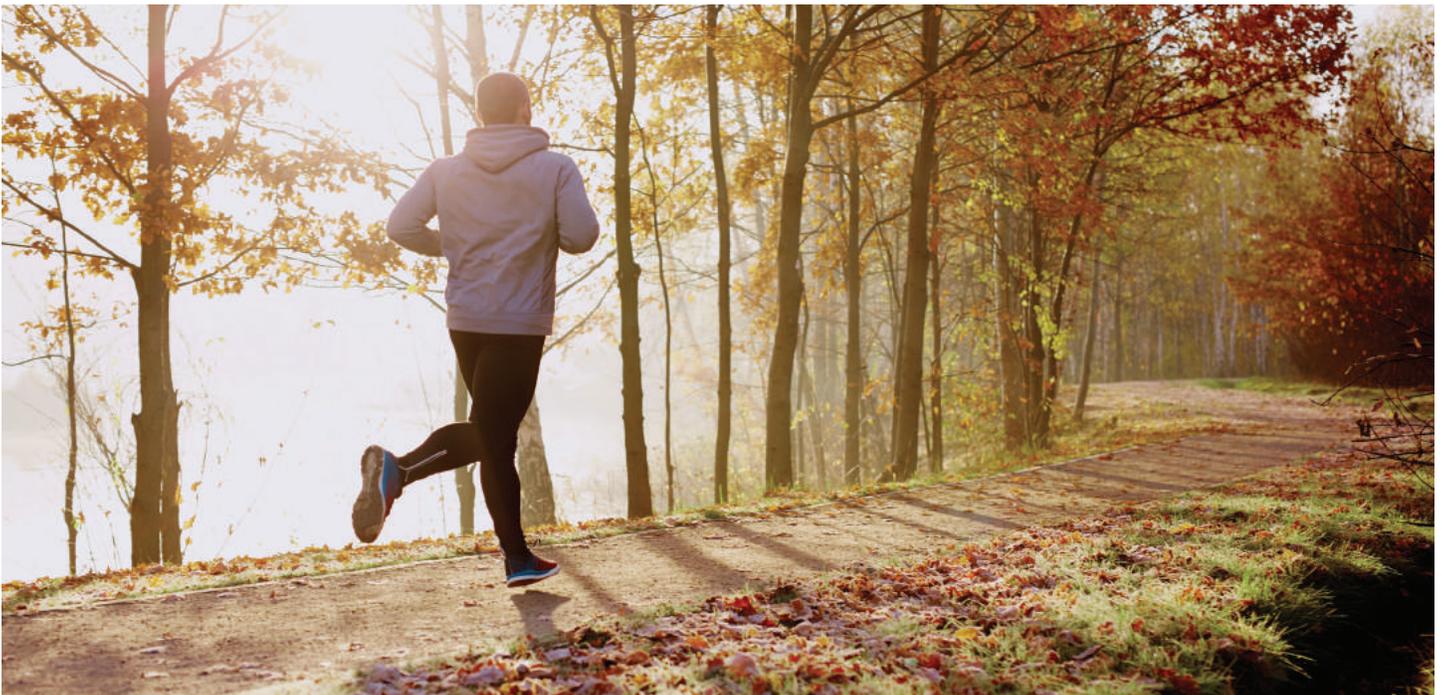


# MATTERS OF TRUST



From the desks of  
William M. Giffin, CEO (left) and  
Kevin Rice, Investment Analyst (right)



## ECONOMIC OUTLOOK IN A MARKET MARATHON

Last weekend marked the 42nd Chicago Marathon.

If you haven't had a chance to see runners cross the finish line, you should put it on your bucket list. It is a heart-warming event. Forty thousand runners from every state and 100 countries have one goal: cross the finish line. It's inspiring, even humbling, seeing months of hard work pay off for the runners. Some are attaining a personal—

maybe seemingly impossible—goal. Others are running for a cause, family or friend.

The finish line is a place of celebration, satisfaction and, finally, even rest.

When trying to understand the market and its multi-faceted components, it feels like we might never cross a finish line. Trade talks continue, Brexit is still unsettled, conversations about Fed rates linger,

and an impeachment process is ongoing. We are mid-race, with no sight of the finish line.

In this quarterly commentary, we look at the events that impacted the performance over the past three months and provide an outlook for what's ahead.

### FEDERAL RESERVE

As predicted, the Fed cut rates by a quarter point at the July Federal

Open Market Committee (FOMC) meeting. This was the first cut since December 2008. After the meeting Chairman Powell cited that the cut was necessary to insure the economic expansion against risks from slower global growth and trade uncertainties.

In September the Fed once again lowered rates by another 25 basis points and cited that inflation remained subdued, global growth remains slow, and various trade conflicts are still unresolved. The FOMC has now undone the last two rate hikes from 2018, when the fiscal stimulus of the U.S. tax cut boosted real economic growth and the trade war was not negatively influencing the economy. At the end of September, the Fed funds futures had a 75% probability of a rate cut at the December meeting and an 85% probability of a rate cut at the March meeting. See Exhibit 1.

► **TC Wealth Partners' View**

*We believe that the Fed will cut rates again by a quarter point in the fourth quarter and another quarter point in the first quarter of 2020. Our belief, though, is contingent upon shifts in trade policy. Future rate cuts are likely if additional tariffs on China are imposed. If tariffs are rolled back, we believe that the Fed would likely not cut rates further. The rate cuts will help extend the economic expansion, but market expectations for the Fed continuing to cut rates will increase volatility.*

*If tariffs are rolled back, we believe that the Fed will not likely cut rates further.*

**TRADE**

During the quarter the trade war escalated, as the U.S. announced it was imposing multiple rounds of new tariffs and China announced retaliation. Chinese officials continue to urge the U.S. to remove sanctions on technology company Huawei, while the U.S. demands intellectual property reform and a sustained market for its agricultural exports.

In August, Trump widened the trade war with China, announcing that he would raise a 10% tariff on \$300 billion in Chinese goods. That went into effect on September 1, but was raised to 15%. Trump then announced he would raise \$250 billion in goods being tariffed at 25% to 30% beginning October 15.

Progress in negotiations was made on October 10th after the White House announced a tentative "Phase 1" agreement to suspend the October 15th tariff increase in return for greater Chinese purchases of US agricultural products. Expectations are that the agreement would be signed by Presidents Trump and Xi at the APEC Summit in Santiago, Chile in mid-November. Negotiators did not agree to suspend tariffs that are scheduled for December on about \$360 billion of imported Chinese goods.

► **TC Wealth Partners' View**

*We expect that "Phase 1" of the trade agreement to be signed in November. We believe that the December tariffs will likely be implemented but could be delayed until early 2020 given the proximity of Christmas. As businesses*

**EXHIBIT 1: FED FUTURES IMPLIED PROBABILITY**



Source: TC Wealth Partners, Bloomberg.

## EXHIBIT 2: GLOBAL PURCHASING MANAGERS INDEX



Source: TC Wealth Partners, Bloomberg.

continue to struggle with tariffs and uncertainty in supply chains, we believe that this uncertainty will put a damper on their investments and could impact their hiring decisions.

### BUSINESS INVESTMENT & LABOR MARKET

Manufacturing activity contracted in August, with the ISM Manufacturing Index<sup>1</sup> slipping to 47.8. This was the fourth straight monthly decline and the weakest level since June 2009. The survey is now below the 50 mark, which indicates contraction. The measure of export orders, a proxy for overseas demand, fell to 41, the lowest level since March 2009. American producers continue to struggle with headwinds from abroad as well as the effects of a strong dollar.

In September, employers added 136,000 jobs to the U.S. economy.

<sup>1</sup>ISM Manufacturing Index is based on a survey of purchasing managers at more than 300 manufacturing firms by the Institute for Supply Management (ISM); the index monitors changes in production levels from month to month.

The average pace of job gains in the last three months are now 157,000 compared to 163,000 in the first six months of the year, a sign that growth in the labor market continues to remain sluggish. Even with a slower pace of hiring in recent months, the labor market remains tight. The unemployment rate fell to a 50-year low of 3.5%.

*Capital expenditures will likely drag growth through the remainder of the year.*

Despite signs of a still-tight labor market the average hourly earnings did not grow in September.

Trade tensions have taken a toll on manufacturing confidence and industrial production around the world. The services sector remains relatively resilient as manufacturing

weakness has not dragged down the services component of the global economy. With trade tensions hitting certain regions and sectors particularly hard, there is now pronounced geographic and sector divergence within the global economy, increasing the risks to global growth. See Exhibit 2.

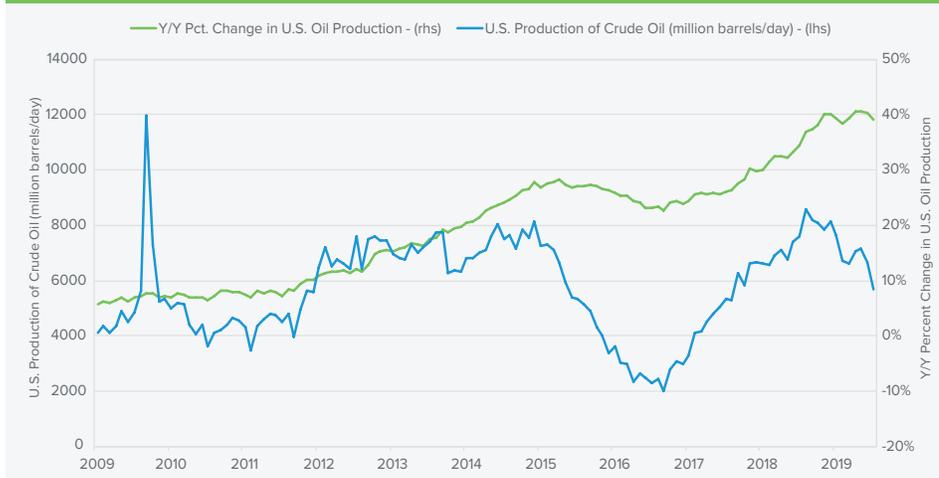
### ► TC Wealth Partners' View

*With still present trade uncertainty and slowdown in global growth, we expect manufacturing to remain sluggish and for capital expenditures to serve as a drag on growth through the remainder of the year. With demand for labor slowing and many companies contending with higher input costs as the trade war lingers, we do not expect to see any meaningful strengthening in job growth in the coming months. We continue to believe that higher income and elevated consumer spending should support future economic growth.*

### BREXIT

October will be a crucial month for the resolution of Brexit. Having originally intended to leave the European Union (EU) by the end of March, the UK is nearing the end of its second Brexit extension. UK Prime Minister Boris Johnson has pledged that if he cannot agree to a withdrawal deal with the EU at an upcoming summit on October 17 and 18, he will not ask for a further extension, and the UK will leave the EU without a deal on October 31. Expectations are that the British parliament will go against Johnson and force a vote to stop the exit and request an extension for a Brexit deal.

### EXHIBIT 3: U.S. OIL PRODUCTION



Source: TC Wealth Partners, Bloomberg.

#### ► TC Wealth Partners' View

Analysts believe that there is a 45% chance that the UK will leave with a deal, a 25% chance that it will leave without a deal, and a 35% chance that UK will never leave the EU. Given these odds we believe uncertainty surrounding the UK's future in the EU will loom over the markets for a while. The Fed has mentioned Brexit uncertainty as one potential factor weighing on the U.S. outlook. We believe that it is possible that a no-deal Brexit could cause a period of volatility in financial markets.

#### OIL

On September 14, two oil processing sites in Saudi Arabia were attacked by what the U.S. and the Saudis claim was a mixture of missile and drone strikes from Iran. The attack resulted in the worst oil supply disruption in history: 6% of the world's production was impacted. On the day of the attack oil prices jumped 15%, but prices have fallen since. The average price of oil is now down 26% since September 2018.

#### TC Wealth Partners' View

Historically, oil shocks have preceded recessions in the U.S. With the increase in shale oil production, the U.S. has become less dependent on oil imports. Therefore, we do not believe that the attack will be as negative for the U.S. economy as in the past. See Exhibit 3. We do believe, however, that the supply disruptions will likely have a greater impact on China as 25% of their crude oil imports are from Saudi Arabia. Experts believe that these attacks were in response to U.S. reinstated sanctions on Iran. We believe that there will not be any military strikes on Iran and that the U.S. will instead increase sanctions on Iran to force them to abandon its

*We believe that economic conditions will outweigh the political turmoil in the coming months*

nuclear programs and its support for terrorist organizations across the Middle East.

#### IMPEACHMENT

On September 24, House Speaker Nancy Pelosi announced a formal impeachment inquiry against President Trump, accusing him of unlawfully urging the Ukrainian president to investigate former vice president Joe Biden. The inquiry initiates the investigative and fact-finding process and is not the same as an impeachment conviction, which would require a House vote and passage by two-thirds of the Republican-led Senate. Since Republicans maintain control of the Senate the chance of a conviction is unlikely.

#### ► TC Wealth Partners' View

We anticipate there may be swings in the market due to the impeachment headlines. We believe that economic conditions will outweigh the political turmoil in the coming months given unemployment is near a 50-year low, wages continue to rise, and the Fed is supportive of the U.S. economy.

#### EQUITY MARKET

The S&P 500 Index rose by 1.7% during the third quarter and is now up 20.6% for the year, its best performance since 1997 (see Exhibit 8). Over the last 30 years (1989-2018), the S&P 500 has gained an average of 4.5% over the final three months of the year and 24 of the last 30 fourth quarters (80%) have produced a positive gain (see Exhibit 4). The Russell 1000 Growth Index has performed the best this year returning 23.3%. Information Technology continues to be the

## EXHIBIT 4: FOURTH QUARTER GAINS OF S&P 500



Source: TC Wealth Partners, Bloomberg.

best performing sector this year, returning 31.4%, and Health Care has been the worst performing sector, returning 5.6% (see Exhibit 8). The announcements for Q3 2019 earnings begin in the coming weeks, and S&P 500 Q3 earnings are estimated to decline year-over-year by -3.7%. The last time the S&P 500 had three straight quarters of year-over-year earnings declines was Q4 2015 through Q2 2016.

### ► TC Wealth Partners' View

We believe that companies are excellent at managing expectations and EPS growth projections have likely fallen too far, leaving room for upside surprises. We expect markets to remain volatile over the fourth quarter as slower global growth, trade wars and uncertainty surrounding the Federal Reserve's next move will weigh on the markets.

## INTERNATIONAL MARKETS

Global equities, as measured by MSCI AC World ex U.S. index, returned -1.7% in Q3 as investors reacted to the continued escalation of the trade war and slowdown in

the global economy. According to the Organization for Economic Co-operation and Development (OECD), global growth is projected to slow over the next five quarters (see Exhibit 5).

U.S. stocks outperformed their developed market peers, driven by the continued strength in the U.S. technology sector. Exhibit 8 indicates that the MSCI Asia Pacific index remains one of the worst performers year-to-date as growth has continued to slow in export-dependent economies within the

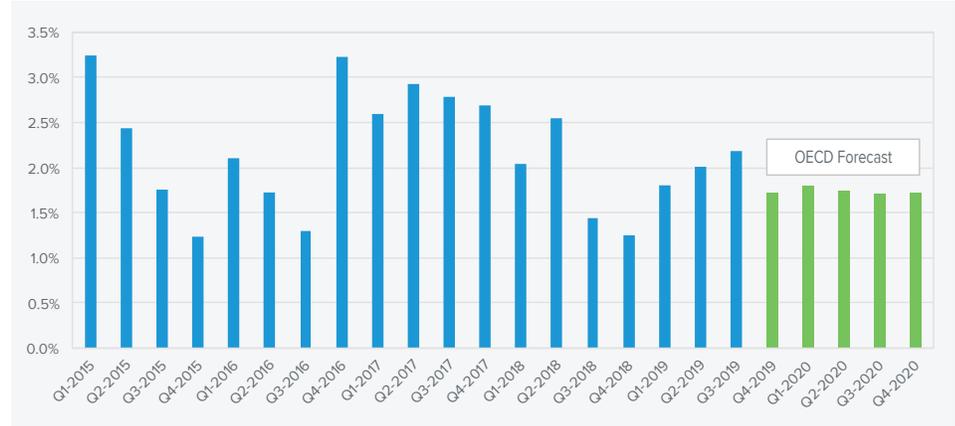
*Developed international market valuations relative to the S&P 500 remains extremely low.*

region. European equities continue to perform well despite the Euro's strength and the growth in the Eurozone economy remaining anemic. During the quarter, 16 central banks lowered rates, and two dozen more are in discussions to cut rates in the fourth quarter.

### ► TC Wealth Partners' View

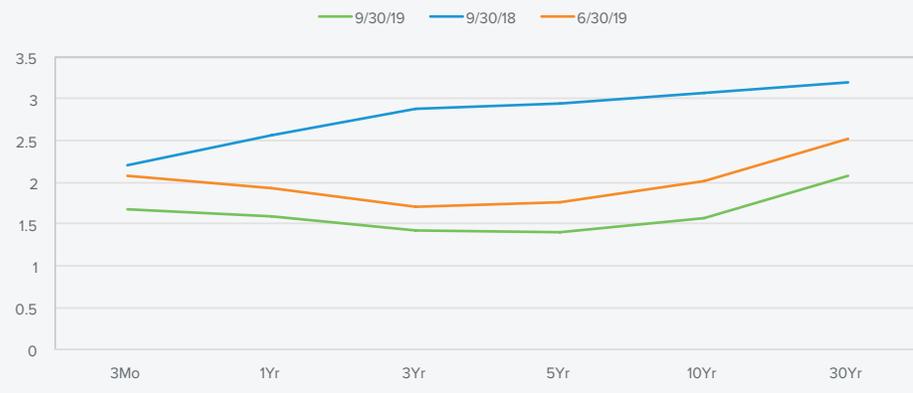
Developed international market valuations relative to the S&P 500 remain extremely low, reflecting continued investor preference for U.S. securities, given higher confidence in U.S. economic and corporate profit outlook. Within EM, valuations look attractive, but analysts have slashed expectations for corporate sales and profit growth as trade tensions between the U.S. and China continue to be a headwind.

## EXHIBIT 5: OECD QUARTERLY GLOBAL GDP GROWTH



Source: Organization for Economic Co-operation and Development (OECD).

## EXHIBIT 6: U.S. 10-YEAR TREASURY YIELD



Source: TC Wealth Partners, Bloomberg.

### FIXED-INCOME MARKET

The Bloomberg Barclays U.S. Aggregate Bond Index returned 2.27% for the quarter and the 10-year U.S. Treasury yield fell to 1.6% on September 30. As you can see in Exhibit 6, the yields across the curve have dropped since the end of last quarter, and the curve has flattened since last year. After inverting in May, the yield curve remained inverted during the quarter. Furthermore, the current inversion is happening in the context of widespread negative-yielding bonds abroad, the unwinding of the Fed's balance sheet and strong demand for long Treasuries as pristine collateral for repurchase agreement (repo) trades.

Across the globe fixed-income rates continued to fall during Q3 as the Bloomberg Barclays Global Aggregate ex U.S. Bond Index returned -0.58%. Global bond yields

*Investing in the markets has always been a marathon, not a sprint.*

fell further on signs of economic weakness, increased trade tensions and central bank dovishness. Negative yielding debt globally increased by \$2 trillion during the quarter and is now at \$15 trillion, or approximately 30% of the global bond market (see Exhibit 7).

#### ► TC Wealth Partners' View

*Investors are turning to U.S. Treasuries as a form of insurance during these*

*times of economic uncertainty. Traditionally, the U.S. yield curve has reflected conditions in the U.S. economy, and an inverted Treasury yield curve was a recession warning. We believe that as long as the central banks in developed economies are intervening to hold down yields in the effort to stimulate their economies, global demand for Treasury bonds will impact U.S. rates. We do not see an imminent risk of recession, but we are concerned about slower economic growth and muted inflation.*

Investing in the markets has always been a marathon, not a sprint. Our work as financial advisors is not to win a 100- or 200-meter dash. We take a long view of the entire 26.2-mile race. As trusted partners, we will continue to monitor the market conditions as they change and make the necessary changes to our clients' portfolios. We exist to help our clients reach their goals, so they can live intentionally and with purpose. ■

## EXHIBIT 7: NEGATIVE GLOBAL BOND YIELDS



Source: TC Wealth Partners, Bloomberg.

## EXHIBIT 8: MARKET PERFORMANCE

S&P 500 SECTORS	Q3-2019	YTD	1Yr	3Yr	5Yr	10Yr
Utilities	9.33%	25.40%	27.10%	13.59%	12.88%	12.50%
Real Estate	7.71%	29.71%	24.74%	10.35%	10.18%	12.17%
Materials	-0.12%	17.11%	2.70%	9.01%	5.37%	9.22%
Information Technology	3.34%	31.37%	8.60%	22.55%	18.20%	17.10%
Industrials	0.99%	22.58%	1.35%	11.29%	9.71%	13.40%
Health Care	-2.25%	5.64%	-3.57%	9.64%	8.94%	14.21%
Financials	2.01%	19.60%	3.91%	15.43%	10.47%	10.74%
Energy	-6.30%	6.00%	-19.21%	-2.67%	-5.06%	3.32%
Consumer Staples	6.11%	23.28%	16.85%	7.89%	9.26%	12.28%
Consumer Discretionary	0.51%	22.46%	2.36%	15.81%	14.02%	17.67%
Communication Services	2.22%	21.74%	5.69%	3.28%	5.17%	9.49%
DOMESTIC EQUITY INDEXES	Q3-2019	YTD	1Yr	3Yr	5Yr	10Yr
Russell 3000	1.16%	20.09%	2.91%	12.82%	10.43%	13.07%
Russell Midcap	0.48%	21.92%	3.17%	10.68%	9.08%	13.05%
Russell 1000 Growth	1.49%	23.29%	3.71%	16.89%	13.38%	14.93%
Russell 1000 Value	1.36%	17.81%	3.99%	9.41%	7.78%	11.45%
NASDAQ	0.18%	21.56%	0.55%	15.94%	13.59%	15.58%
S&P 500	1.70%	20.55%	4.25%	13.39%	10.82%	13.22%
FIXED-INCOME INDEXES	Q3-2019	YTD	1Yr	3Yr	5Yr	10Yr
Global Aggregate ex. US	-0.58%	4.38%	5.34%	0.43%	0.87%	1.27%
US Aggregate	2.27%	8.52%	10.30%	2.92%	3.38%	3.75%
Treasury	2.40%	7.71%	10.48%	2.24%	2.91%	3.08%
High Yield	1.33%	11.41%	6.36%	6.07%	5.37%	7.94%
TIPs	1.35%	7.58%	7.13%	2.21%	2.45%	3.46%
Municipals	1.58%	6.75%	8.55%	3.19%	3.66%	4.16%
Asset Backed Securities	0.92%	4.13%	5.42%	2.24%	2.25%	2.82%
Mortgage Backed Securities	1.37%	5.60%	7.80%	2.32%	2.80%	3.14%
Commercial Mortgage Backed Securities	1.89%	8.61%	10.40%	3.31%	3.78%	6.12%
INTERNATIONAL EQUITY MARKETS	Q3-2019	YTD	1Yr	3Yr	5Yr	10Yr
MSCI World	0.66%	18.16%	2.44%	10.85%	7.82%	9.65%
MSCI ACWI	0.09%	16.71%	1.96%	10.32%	7.26%	8.96%
MSCI ACWI ex US	-1.71%	12.05%	-0.69%	6.89%	3.45%	5.00%
MSCI EAFE	-1.00%	13.39%	-0.75%	7.09%	3.86%	5.49%
MSCI EM	2.69%	20.45%	5.24%	9.16%	7.05%	7.37%
MSCI Europe	2.63%	19.90%	6.41%	8.27%	6.03%	8.32%
MSCI Asia Pacific	-1.26%	9.40%	-2.50%	6.87%	5.20%	5.93%
MSCI North America	1.51%	20.72%	4.12%	12.96%	10.18%	12.59%
MSCI EM Asia	-3.33%	6.14%	-3.60%	6.65%	4.41%	5.55%
MSCI EM Latin America	-5.58%	6.54%	7.08%	7.17%	-0.48%	-0.20%
MSCI EM Europe & ME	-6.83%	5.64%	1.44%	4.43%	-0.55%	1.53%

Source: TC Wealth Partners, Bloomberg.

## NOTEWORTHY

### SPONSORSHIPS

#### AID (ASSOCIATION FOR INDIVIDUAL DEVELOPMENT)

*Unmask Our Potential Benefit  
Fishermen's Inn*  
Elburn, IL  
October 2019

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### ATTENDED

#### KATHRYN MCGOUGH

Midwest RIA Summit  
Panel Moderator: "What the Next  
Generation Wants"  
Chicago, IL  
August 2019

#### KEVIN RICE

Midwest RIA Summit  
Presenter: Trends and Market Forecast  
Chicago, IL  
August 2019

#### TAMI BOWMAN

TIM HATTENDORF  
Great Lakes Users Group (GLUG)  
Milwaukee, WI  
August 2019

#### KATHY SCHELLING

RIA Compliance Consultants  
Omaha, NE  
September 2019

#### TAMI BOWMAN

Advanced Pension Conference  
Chicago, IL  
September 2019

#### DAVE FISHER

Fidelity Investments  
Inside Track Conference  
Chicago, IL  
September 2019

TC Wealth Partners<sup>LLC</sup>  
Trust Company  
of Illinois

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