BRENTON POINT
WEALTH ADVISORS

December 11, 2019

Investing Environment Review and Outlook – Volume 33

We maintain our bullish 5 ratings for all equity classes (U.S., Developed and Emerging Markets). Goldilocks conditions prevail – including moderate economic growth, benign inflation below 2%, and a loose Federal Reserve. Historically, these conditions were positive for future equity returns. Additionally, following strong return years like 2019, January results were mixed (43% of the cases were higher) but the first quarter was up 86% of the time, with an average return of 4.1%. The worst Q1 decline in these years, was -3.7% in 1990, but there were three years Q1 was up over 10% (1976, 1986 and 1998). Our gold and commodity ratings remain a neutral 3, recommending no exposure. Our long-term bond rating remains a bearish 1 based on the positive 66 reading from our economic outlook indicators. We expect stronger than expected economic growth and higher long term interest rates in 2020.

Expect Higher Volatility (Up or Down) in January

At year end investors typically experience low volatility, and this year is no exception so far. Since October 3rd, the biggest peak to trough decline in the S&P 500 was just 1.9%. However, January can be a shock. Since 1950, the first two weeks of January saw 35% higher volatility than late December. The average return (up or down) in the first two weeks of January was 2.7% vs. just 2.0% for the last two weeks of December and even more dramatic since 2000 at 1.8% and 2.9%. For instance, since 2000 there were three years the S&P 500 was down over 6% in the first two weeks of January (2008, 2009, 2016) and 3 years when it was up over 4% (2003, 2018, 2019).

Chart 1: S&P 500 Volatility is Low in December

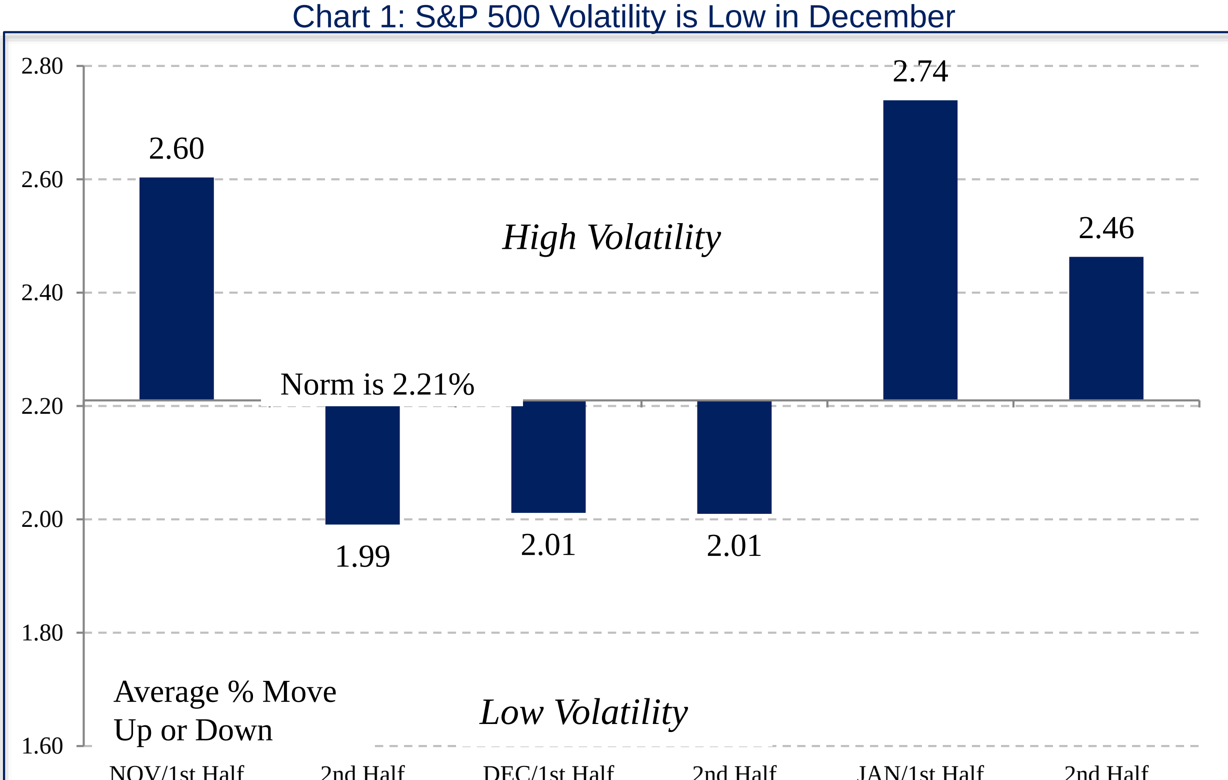
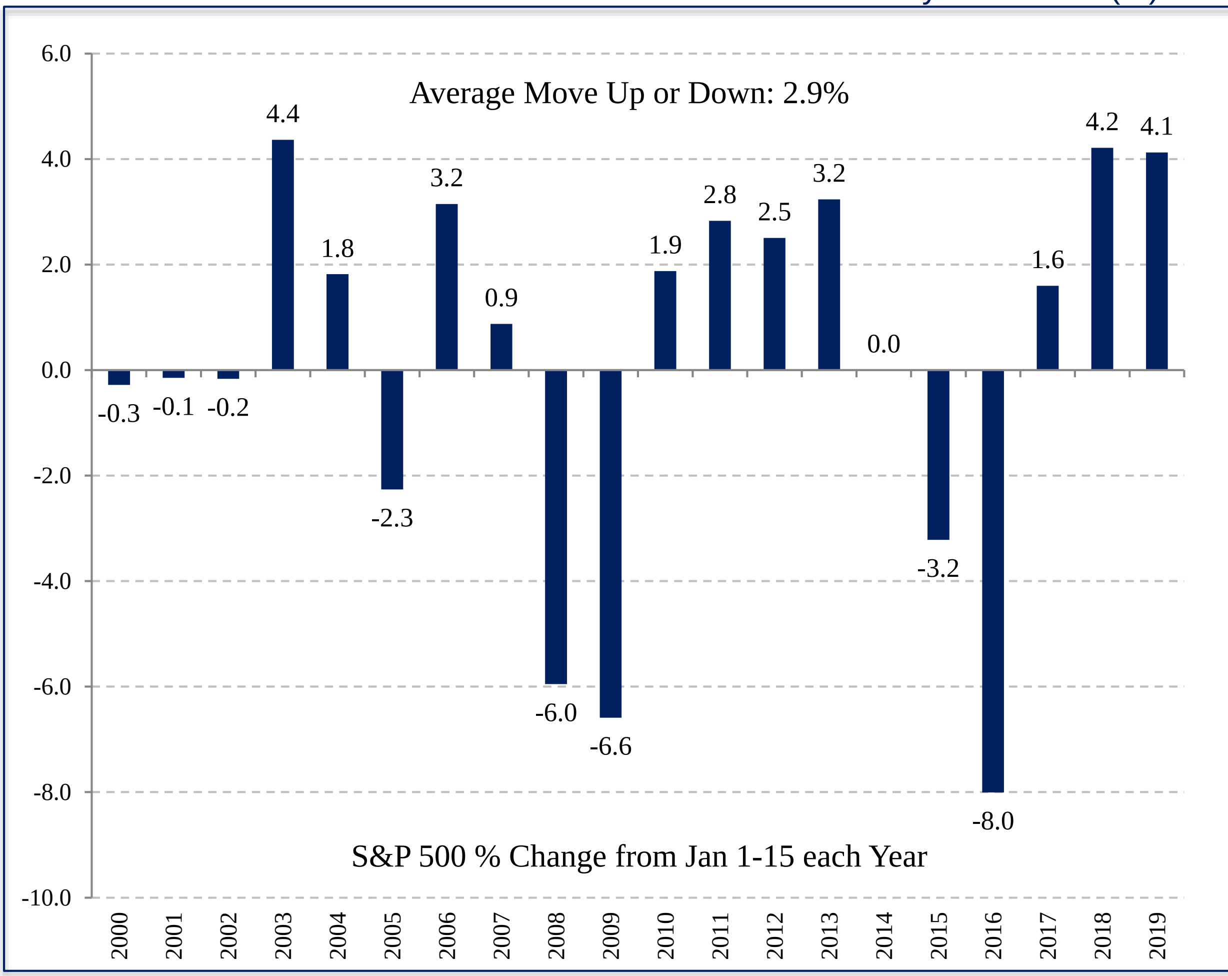


Chart 2: S&P 500 Performance in First 2 Weeks of January since 2000 (%)



Impeachment: Not a Market Risk

On September 24th House Speaker Pelosi announced a formal impeachment inquiry. Public hearings started on November 13th and a vote on formal charges is possible before year end. Conviction and removal from office requires a Senate vote, which is unlikely with Republican control. The 1974 Nixon impeachment coincided with the worst equity bear market since WW II, while the 1998 Clinton impeachment had no material market impact.

So far, this year is more comparable to the Clinton case. In both Clinton's and Trump's cases, their own party controlled the senate, so removal from office was never considered likely. In September, Trump's approval rating was 43%, significantly higher than Nixon's at 25%, although Clinton's approval was higher at 66%. The most telling difference is in the economic environment. During Nixon's impeachment, inflation was 10% and rising due to sharply higher oil and gasoline prices after an OPEC embargo. The Fed hiked interest rates from 5.5% to 10% in 1973 and a deep recession and bear market followed.

In Clinton's case, inflation was benign at 1.8%, and the Fed had just cut 3 times after the collapse of Long-Term Capital Management. The impeachment had no apparent market impact. Six months after the House voted on Clinton's impeachment, the S&P 500 was up 13.7%. Current conditions are very similar in those respects with inflation also at 1.8% and three Fed cuts this year. Politics receives a lot of headlines and can certainly affect stocks on a daily basis, but for the primary trend in stocks, politics is usually less significant than the economic environment.

Chart 3: Nixon 1974 Impeachment: 10% Inflation

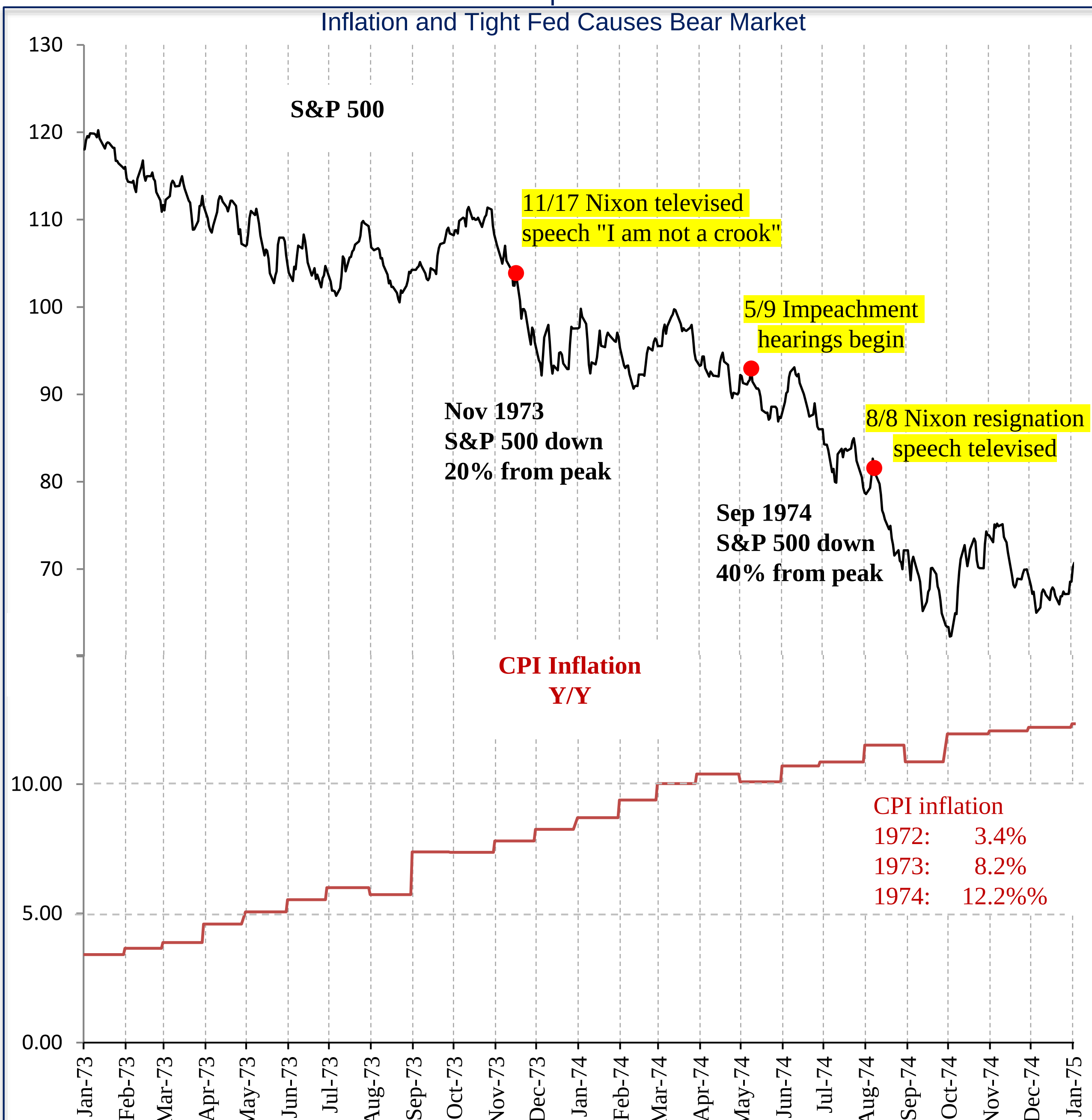


Chart 4: Clinton Impeachment: Inflation 1.8%
No Market Impact

December 11, 2019

Chart 5: 2019 Impeachment: Inflation 1.8%

In summary, Goldilocks conditions remain with Fed support through 3 rate cuts this year and $60 bil/month of outright purchases of Treasury Bills. Combined with moderate growth and inflation below 2%, the conditions remain bullish for equities. If the economy strengthens as we expect, our view could improve for commodities. Thank you for your support and please contact your advisor with any questions.

Michael Schaus
Director of Market Research