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ESTABLISHED 1876

**Market Commentary**
**October 2019**

## Introduction

After two strong quarters of market performance, stocks and bonds still managed to eke out positive returns in the third quarter. Economic data moderated throughout the quarter however rebounded higher towards the end of the quarter. The labor market continues to be a bright spot for the economy with the unemployment rate holding steady at 3.7% as of August. A strong labor market has supported strong consumption here in the U.S., so while GDP growth has declined from the first quarter, it is still up 2.0% as of the second quarter. Lastly, inflation slightly ticked up from the start of the quarter with the Consumer Price Index (CPI) up 1.7% year over year as of August. With sluggish economic data released globally due to uncertainty surrounding matters such as trade, the Federal Reserve cut short term interest rates twice during the quarter by 0.25% each. Despite geopolitical headlines such as tariff battles between the U.S. and major trading partners, Brexit and tension in the Middle East, stock and bond markets have moved higher with help from the Fed and more positive economic surprises recently. While our portfolios have participated in these moves higher, we do not dismiss the influence these unresolved events have had on market sentiment. For this reason, we continue to take risk in our portfolios but do so in a conservative manner.

## Domestic Equities

U.S. stocks managed to generate a positive return of 1.70% for the third quarter despite growing fear of a global slowdown. Similar to the second quarter, volatility persisted, as the S&P 500 posted a positive return of 1.44% in July, then reversed course in August down -1.58% and then rebounded in September up 1.87%. The selloff in August can be primarily attributed to the heightening of trade tensions between the U.S. and China and recession angst over the 10-year Treasury yield falling below the 2-year Treasury yield (which has preceded the last 7 recessions). While tariffs are never good for any country involved, they tend to hurt foreign countries like China more than the U.S. due to their higher dependency on exports. Although U.S. businesses may be more sheltered from trade tension, they still incur higher costs as a result of the tariffs that go into effect and more so, may be reluctant to invest in their own businesses because of uncertainty surrounding future tariffs. Despite escalating trade tension throughout the quarter, earnings growth for companies in the S&P 500 were up 1.6%. With earnings growth projected to be negative for Q3 2019, stock valuations that aren't the most attractive, and a softer economic backdrop we recommend a neutral stance on equities.

## International Equities

International developed equities and emerging market equities returned -1.07% and -4.25% for the third quarter, respectively, both lagging the S&P 500. The Eurozone economy grew at a 0.2% rate in the second quarter, below its long-term trend. The weakness was driven by Germany, which saw GDP contract by 0.1% on the quarter. Slowing economic growth in China and rising trade tension represent challenges for the Eurozone, as China was the eurozone's third-largest export destination and largest source of imports. European Central Bank President Mario Draghi announced in September that the ECB would resume net asset purchases of twenty billion Euros per month to help support their economy. The ECB policy rate and ten-year German Bund yields are negative, well below the levels seen in developed counterparts such as the U.S., U.K., and Japan. Weak productivity, high unemployment, and an aging population are likely to drag on economic growth in the area over the longer term.

Within emerging markets, trade tension continues to weigh on major emerging market economies such as China and other developing countries that are dependent on the Chinese economy. The U.S. raised tariffs in September of 15% on an additional $112 billion of imports from China. China's economic growth has continued to slow, as July marked the fourth straight month of contraction in manufacturing PMI before the August reading came in above 50, signaling expansion. The economy could show further weakness in the months ahead as new rounds of tariffs take effect. There are many uncertainties in international and emerging markets, but due to inexpensive valuations and the potential resolutions to the pending conflicts, there may be buying opportunities in the future. Despite slowing economic data, both international and emerging market equities have been positive this year up 12.80% and 5.89%, however, still lag the S&P 500.

## Fixed Income

Fixed income continued its successful run in 2019 to post positive returns in the third quarter of 2.27% as measured by the Bloomberg Barclays US Aggregate Bond index. Lower quality corporate bonds benefited from investors' continued appetite for risk while longer maturity bonds were supported by falling long term interest rates. The Federal Reserve continued its easing cycle with another 0.25% rate cut in August, as the central bank attempts to navigate an aging U.S. economy amid a global manufacturing slowdown and continued geopolitical uncertainty. Chairman Powell has refused to elaborate on the Fed's next move, though market expectations are for one more cut before the end of the year. As a result of the market's downward projection for interest rates and a broader flight to quality, demand for longer duration securities increased and pushed yields downward, with the 10-year U.S. Treasury yield dipping as low as 1.45% after ending the previous quarter at 2.00%. Moving forward, we believe fixed income yields will remain lower for longer but provide diversification in a portfolio.

## Alternatives

The Morningstar Diversified Alternative index returned 0.93% for the third quarter underperforming the S&P 500 but with significantly less volatility (as measured by standard deviation). Gold, which many investors regard as a "safe-haven" asset, is back in demand and pushed the price to six-year highs in July. Gold ended the third quarter at 1,465/oz. On the other hand, oil prices have felt pressure. A lingering trade war, weakening global economic data, a strong dollar, and persistently high supply levels have pressured oil prices to fall mostly below $60 since June, until recent attacks on Saudi Arabian oil fields decreased production and pushed prices higher. Overall, U.S. crude fell -7.53% over the course of the third quarter to $54.07 per barrel.

## Real Estate

The recent improvement in housing data has raised optimism that the housing market could be regaining its footing after hitting a soft patch during the first half of 2019. Housing starts and building permits surged in August to their highest levels since 2007, increasing 12.3% to a seasonally adjusted annual rate of 1.364 million units and 7.7% to a rate of 1.419 million units respectively. Similarly, new home sales rose 7.1% to a seasonally adjusted annual rate of 713,000 units in August while the NAHB index, an index that tracks homebuilder optimism and a leading indicator for the housing market, hit a yearly high in September as it rose to 68 from an upwardly revised 67 reading in August. Falling mortgage rates and solid demand may be offsetting headwinds from tariffs and a tight labor market faced by builders. The average rate on the 30-year fixed mortgage ended the third quarter at 3.99% down almost 1.18% from its peak of 5.17% in November of 2018.

## Conclusion

With fear of a potential recession being the main focus of investors throughout the year, stocks and bonds continue to move higher. The question we are now asking ourselves is "what is the next catalyst for the market to move even higher?" Although economic data has surprised to the upside more recently, we remain cautious given the uncertainty surrounding trade policy and future Federal Reserve decisions. The equity market can certainly be helped by an accommodative Fed, but we would like to see more substantial economic activity to confirm a trend to the upside. With that in mind, we remain cautious but continue to take a neutral stance on risk assets.