DT INVESTMENT PARTNERS, LLC

Q4 2019
FINANCIAL MARKETS COMMENTARY

"A Buying Frenzy For Stocks And Bonds"

DT INVESTMENT PARTNERS

RISK-BASED ASSETS PERFORMANCE SUMMARY

- ◊ Stocks and bonds staged their biggest simultaneous gains in more than 20 years as the S&P 500 Index soared 29% in 2019, while the U.S. bond market rally pushed the yield on the benchmark 10-year Treasury note down more than three quarters of a percentage point. This marked the first time since 1998 that the U.S. Large Cap stock index has jumped by at least 20%, while Treasury yields have slipped by that much.

- ◊ During the fourth quarter, all risk-based assets rose in price, led by Emerging Market stocks (See page 5) thanks to a 3% decline in the U.S. dollar, an improving outlook on the global economy, progress between the U.S. and China on their trade war, and the Fed's three interest-rate cuts which boosted investors' optimism that the decade long economic expansion can continue. U.S. Large Cap and International Developed Market stocks also generated strong gains for the quarter.

- ◊ The S&P 500 Index posted a series of recent highs during the quarter on the way to its best performance in 6 years. The 10-year yield, which falls when bond prices rise, approached its all-time low in yield back in September, before stabilizing below 2%. Traditionally safer assets like gold along with copper and oil also soared during the quarter. The gains marked a sharp reversal from the fourth quarter of 2018 when a rally for U.S. stocks faltered and the S&P 500 Index posted its worst December since 1931 to finish the year down 6%.

- ◊ All U.S. Large Cap sectors rallied during the fourth quarter led by technology as investors sought growth-oriented companies in a low growth world. Aging demographics and the declining likelihood of "Medicare for All" policies being enacted helped support healthcare sector stocks. The financial sector also made strong gains thanks to yield curve steepening, Fed rate cuts, and improving global economic conditions.

BOND PERFORMANCE SUMMARY

- ◊ U.S. Government bonds had their strongest year since 2011 due to fears of a looming global slowdown made worse by trade conflicts between the U.S. and China. However, Treasury prices declined/yields rose during the fourth quarter as positioning for another Fed rate cut disappeared with investors gaining confidence in the outlook for economic growth. Progress on U.S.-China trade, closer movement towards an orderly Brexit agreement, and a modest recovery in manufacturing data in Europe and China supported this view. The yield curve steepened with 10 year maturity Treasuries yielding 0.35% more than 2 year maturity Treasuries.

- ◊ Investment Grade (IG) Corporate Bonds, Treasury Inflation Protected Securities, and Mortgage-Backed Securities all generated positive returns for the quarter with IG Corporate Bonds once again leading the way as investors sought higher relative yields in a very low interest rate environment. Municipal bonds wrapped up their best year since 2014 on the back of a global interest rate rally and record demand with $90 billion of fund inflows. In the fourth quarter, with interest rates low, several tax-exempt municipal bonds were refunded (refinanced) with taxable municipal bonds.

CONTRIBUTORS & DETRACTORS TO PERFORMANCE

- Performance contributors versus the Global Stock/Intermediate Maturity U.S. Bond blended benchmark index during the quarter included our overweight allocations to U.S. Large Cap stocks and IG Corporate bonds and our outside-of-benchmark allocation to mortgage-backed securities.

- Detractors to performance versus the benchmark index included our underweight allocation to Risk-Based Assets. In particular, our underweight to Emerging Market and International Developed Market stocks detracted from performance.

GLOBAL MARKETS & ECONOMY

- Stocks headed higher in the fourth quarter and didn't look back despite a weak global economy, a trade war, decelerating corporate earnings, and a U.S. President facing impeachment. The third Fed rate cut of the year combined with Fed liquidity injections to support the bank funding market and a de-escalation of trade tensions between the U.S. and China helped U.S. Large Cap and European stocks reach new highs.
- Global manufacturing activity continued contracting in the fourth quarter due to tariff pressures, uncertainties from the trade war, and slow economic growth outside the U.S. As a result, business investment remained subdued.
- However, hiring by employers stayed strong and consumers continued to spend. At the end of the quarter, the U.S. reached a limited (Phase One) trade deal with China and a new trade pact with Canada and Mexico. U.S. business activity improved to a five month high in December while China's industrial output and consumer spending accelerated.
- As the final quarter of the year came to a close, the House voted to impeach President Trump but had yet to deliver the impeachment document to the Senate for a trial. It is very unlikely that the Republican-controlled Senate would convict the President. Unfortunately for the U.S. economy, the impeachment proceedings significantly diminish the likelihood that any fiscal stimulus programs will be enacted before the 2020 election.
- On the last day of the quarter/year, the White House announced that Phase One of a trade deal with China would be signed on January 15th in Washington D.C. More importantly, President Trump will be traveling to Beijing early in the New Year to begin Phase Two of the trade talks.
- As we enter the New Year, stocks are near all-time highs and investor sentiment is exuberant, global monetary policy is easy and interest rates, inflation, and unemployment are all low. Consumers are spending, there are signs of stabilization in global economic growth, the U.S. banking system is well capitalized, and the yield curve is positively sloped. The impending memorialization of a Phase One trade deal along with hopes for a Phase Two deal soon thereafter should keep investors' appetite for risk strong and the probability of recession low.
- The four primary keys to financial market performance that we identified early in 2019 are beginning to look more favorable towards a pro-risk investment stance as we enter 2020. The Fed lowered interest rates 3 times in 2019 and signaled that it is prepared to keep the fed funds rate very low in 2020 and possibly longer. The Fed believes that inflation will remain tame as the economy grows modestly and the job market remains solid. We still believe that deflation is a greater risk than inflation and the Fed is justified in keeping rates lower for longer.
- Although Chinese policymakers have begun to embark upon policy stimulus, they remain increasingly concerned about debt-driven economic growth and are hesitant to aggressively stimulate their economy. A resolution in the trade war with the U.S. is most likely needed before the world's second largest economy fully rebounds.
- The U.S. dollar fell 3% during the quarter as the Fed cut interest rates for a third time in 2019 and pumped extra liquidity into the money markets to support intra-bank lending. Inflation remains low and investors anticipate a rebound in economic growth outside the U.S. A weaker dollar is more supportive for the prices of international and emerging markets stocks and commodities.

PORTFOLIO STRATEGY & OUTLOOK

- U.S. and Chinese officials are scheduled to meet in Washington D.C. on January 15th to sign Phase One of a trade agreement. President Trump has announced that he will be going to Beijing shortly thereafter to work on Phase Two. At this time, the specifics of the Phase One deal are unknown. However, a pending deal may mean that the trade dispute has reached its point of maximum tariffs and the negative consequences should begin to slowly dissipate. This could lead investors to push stock prices higher in hopes of an improvement in business confidence and spending/investment while significantly reducing any threat of recession.

- S&P 500 corporate earnings have declined for the past 3 quarters and fourth quarter earnings are estimated to fall by 1.4%. If -1.4% is the actual decline for the quarter, it will mark the first time the index has reported four straight quarters of year-over-year earnings declines since Q3 2015 through Q2 2016. ***In order for earnings to rebound, there will need to be an easing in the trade war combined with a rebound in global economic growth, particularly Chinese economic growth, and a weaker U.S. dollar.***

- Optimism and exuberance among individual investors about the short-term direction of the stock market reached its highest level of the year in December. The overwhelming view among both individual and institutional investors for 2020 is that stocks will once again outperform bonds and cash, although the magnitude of gains will be much more subdued than in 2019. The consensus reasoning for such is that interest rates will remain low, global monetary policy will remain accommodative, the U.S. economy will continue to grow, and a breakthrough will be reached in U.S.– China trade talks. All of that is quite possible. However, it would be naïve to ignore the potential for geopolitical risks such as tensions in the Middle East, unrest in Hong Kong, the U.S. presidential impeachment proceedings, and the 2020 election to increase investor uncertainty and market volatility.

- With the exception of the past 4 quarters of corporate earnings results, all of our financial market indicators are pointing to another green (positive) year for stock returns. The fact that one of the longest and most unloved bull markets in stocks is now becoming so loved, so quickly, is a bit troubling to us. Nevertheless, we will continue to follow our disciplined investment process and look for opportunities to increase exposure to risk-based assets.

- International Developed and Emerging Market stocks look more attractive than U.S. stocks based upon cheaper relative valuations. If a trade deal is reached and global growth accelerates later this year, the Fed leaves rates unchanged, and the U.S. dollar weakens, then international and emerging markets stocks could greatly benefit.

- As for bonds, yields may grind slightly higher if economic growth rebounds and trade uncertainty gets resolved. However, inflation is unlikely to return anytime soon. The Fed signaled that it plans on keeping interest rates on hold for at least 2020 or even longer. The structural headwinds to higher yields including aging populations, rising savings rates, global de-leveraging, and negative government bond yields outside the U.S. are not going away anytime soon. Therefore, U.S. bond prices should remain well bid/yields low.

- We continue to favor IG Corporate bonds and Mortgage-Backed Securities over Government bonds. Both fixed income spread sectors offer relatively attractive yields compared to government bonds. In the Municipal bond market, we expect the growing supply of new issuance to better meet the strong demand, leaving total returns mostly driven by coupon income in lieu of significant price appreciation.

Andrew Zimmerman, Chief Investment Strategist

ASSET CLASS TOTAL RATE OF RETURN PERFORMANCE SUMMARY AS OF 12/31/2019

Stock Indices	Asset Class	QTD Return	1 Year Return
MSCI AC World Daily TR N	Global Equities	8.95%	26.60%
S&P 500 INDEX	U.S. Large Cap Equities	9.06%	31.48%
S&P 400 MIDCAP INDEX	U.S. Mid Cap Equities	7.05%	26.17%
RUSSELL 2000 INDEX	U.S. Small Cap Equities	9.93%	25.49%
MSCI EAFE	International Developed Market Equities	8.23%	22.77%
MSCI EM	Emerging Market Equities	11.74%	18.63%
FTSE E/N All Eqty ReitTR	Real Estate (REITs)	0.13%	28.66%
U.S. Large Cap Sector Stock Indices			
S&P 500 ENERGY INDEX	U.S. Large Cap Equities - Energy Sector	5.49%	11.81%
S&P 500 HEALTH CARE IDX	U.S. Large Cap Equities - Health Care Sector	14.37%	20.82%
S&P 500 CONS DISCRET IDX	U.S. Large Cap Equities - Consumer Discretionary Sector	4.47%	27.94%
S&P 500 CONS STAPLES IDX	U.S. Large Cap Equities - Consumer Staples Sector	3.51%	27.61%
S&P 500 INFO TECH INDEX	U.S. Large Cap Equities - Information Technology Sector	14.40%	50.29%
S&P 500 UTILITIES INDEX	U.S. Large Cap Equities - Utilities Sector	0.80%	26.40%
S&P 500 INDUSTRIALS IDX	U.S. Large Cap Equities - Industrials Sector	5.50%	29.32%
S&P 500 COMM SVC	U.S. Large Cap Equities - Telecom Sector	9.00%	32.69%
S&P 500 MATERIALS INDEX	U.S. Large Cap Equities - Materials Sector	6.38%	24.58%
S&P 500 FINANCIALS INDEX	U.S. Large Cap Equities - Financials Sector	10.44%	32.09%
S&P 500 REAL ESTATE IDX	U.S. Large Cap Equities - Real Estate Sector	-0.54%	29.01%
Commodities Indices			
ISHARES GOLD TRUST	Gold	2.84%	17.98%
S&P GSCI Tot Return Indx	Broad Commodities	8.31%	17.63%
Bond Indices			
U.S. Aggregate	Core Bonds	0.18%	8.72%
Intermediate	Intermediate Government & Corporate Bonds	0.37%	6.80%
US Corporate High Yield	High Yield Debt	2.61%	14.32%
U.S. Treasury	U.S. Treasuries	-0.79%	6.86%
U.S. TIPS	U.S. TIPs	0.79%	8.43%
U.S. Agency	U.S. Government Agencies	-0.09%	5.89%
U.S. MBS	Mortgage-Backed Securities	0.71%	6.35%
Corporate	Corporate Debt	1.18%	14.54%
Municipal Bond Index	Municipal Debt	0.74%	7.54%

Notes: The DT Investment Partners' Commentary and Outlook discusses general developments, financial events in the news and broad investment principles. It is provided for information purposes only. The material represents an assessment of the market environment at a specific point in time and is not intended to be a forecast of future events, or a guarantee of future results. Investments in various asset classes entail different investment risks. For example, small cap stocks tend to be more volatile than large or mid-cap stocks. International and emerging markets stocks have exposure to currency fluctuations, foreign taxes, political instability and the possibility for illiquid markets. Fixed income investments involve interest rate and credit risks among others. Real estate investing includes risks such as declines in value of real estate, changing economic conditions, tax laws or property taxes. Commodities' investing is highly volatile and subject to changing economic conditions and the vagaries of speculators among other risks. One cannot invest directly in an index. Past performance does not guarantee future results.