TILIA NEWS

INVESTMENT MANAGEMENT | FIDUCIARY ADVICE | RETIREMENT PLANNING

Don't Let the 2020 Election Alter Your Investment Plan

Not surprisingly, we are starting to get questions & concerns about next year's elections. Many investors feel the need for a contingency plan, just in case the candidate which stands on the opposite end of the political spectrum from the investor ends up in the White House.

You won't hear us dismiss these ideas or fears. We want you to be comfortable & confident with your investments. Armed with those feelings, investors can endure the ups & downs of the short run in order to reap the long-term rewards of the market. Sometimes action is required to get you into the comfort zone, but you won't find us endorsing wholesale changes based on who runs the government. Instead we'll talk to nervous investors about raising cash levels, trimming stock allocations 5-10%, or adding some extra diversification. The portfolios we've built for you reflect ***your*** long-term goals & needs. Those

Evaluating the Health of Markets & the Economy

Once a year or so in this newsletter, we like to take a step back and paint a picture of markets & the economy through a broad lens. Given the never-ending cycle of negative headlines, we hope this can serve as a sober, data-driven assessment of the current investment landscape.

In the past we've generally listed positives and negatives and used them to arrive at some conclusions. 2019 has been a little odd, in that there are very few resounding positives or negatives. As much as the phrase gets over-used, this has been a "goldilocks" environment. Here is a list of things we think are important right now.

1) Fourth quarter Gross Domestic Product (GDP) forecasts range from 0.3% (Atlanta Fed) to 1.5% (Merrill Lynch), as of November 15th. *This suggests meager growth, but not a recession. If large corporations can get some visibility on trade policy, growth could potentially reaccelerate as we move into 2020.*

2) Retail sales were up 0.2% month-over-month in October, and rose 3.9% year-over-year, excluding gasoline purchases. *The U.S. consumer looks fine. Walmart's quarterly earnings report was also strong, which is a great bellwether for the American consumer.*

3) Mortgage delinquencies fell in the 3rd quarter to the lowest level since 1995. Nationwide foreclosure inventory is the lowest since 1985. *No signs of stress in the housing market.*

4) The Bureau of Labor Statistics "All Items Index" suggests inflation of 1.8% over the last 12 months, which is consistent with data from the Federal Reserve. *For now, this looks good. Inflation consistently above 2% could force the Federal Reserve to change course on its low interest rate policy.*

5) Heavy Truck Sales were +3% year-over-year in October, and the sales rate remains near September 2019's all-time-high. *Leading up to the last few U.S. recessions, heavy truck sales have collapsed.*

6) Nationwide home prices were +3.5% year-over-year in September, according to the CoreLogic House Price Index.

goals and needs won't change on November 6th, 2020, so your portfolio should stay largely the same.

It is far too early to tell who will win the Democratic nomination, or the outcome or effect of the impeachment hearings. Even if we knew the winner of the Presidential election in advance, we still couldn't predict the reaction of financial markets, or whether the S&P 500 would be higher or lower 1 year following the results. Worrying too much about it is a useless exercise. Far-left or far-right proposals will be subject to compromise, business leaders will adapt & the world will keep turning.

When it comes to your portfolios, what matters to us is your investment time horizon, expected cash needs/contributions in the foreseeable future, the level of reserve you have in case of emergency, and the amount of volatility you can handle without throwing in the towel on your investments. That information helps us determine the proper allocation for you, which drives the majority of your investment results. None of this should have anything to do with what party or individual has the larger share of power in Washington in any given year.

Sources: calculatedriskblog.com, yardeni.com, instituteforsupplymanagement.org

Considering the level of household wealth tied up in primary residences, a buoyant housing market will always be important.

7) Hotel performance (Occupancy, Average Daily Rate & Revenue per available room) is basically flat in 2019, after a strong 2018. Demand is up slightly, but so is the supply of rooms. *While not growing substantially, business & personal travel remains healthy.*

8) The Institute of Supply Management's (ISM) manufacturing report was in contraction territory in October, but improved slightly from September. *This is the 3rd straight month the report has come in below a score of 50, which shows some moderate weakness in the U.S. manufacturing sector. Manufacturing makes up around 11% of U.S. GDP.*

9) On the flip side of #8, the ISM non-manufacturing report for October, which covers a much broader slice of the domestic economy, was firmly in growth territory at 54.7%. Activity re-accelerated after hitting a 3 year low in September. *This is a solid report. A sustained move below 50 would warrant caution.*

10) After the run-up in stock prices in 2019, stock valuations are elevated vs. historical averages. As of the end of Q3, the S&P 500 was valued at 23.1x trailing 12 month earnings, vs. an average of 19.4x over the last 50 years. *While this seems high, ultra-low interest rates can support higher prices. The dividend yield for the S&P 500 is roughly equal to the interest paid by a 10 year government bond (1.76% vs. 1.80%). Even at today's valuations, stocks still represent the best chance to outpace inflation over time.*

11) There is no abundance of investor greed & speculation. Prior to the major downturns in 2000 & 2008, the amount of investor margin debt (money borrowed against stocks and bonds) exploded higher. According to Yardeni Research, margin debt has fallen considerably in 2019, and as a percentage of the broad market value, we are at one of the lowest points of this economic cycle for margin borrowing. *Without investors being over-leveraged, it is difficult to envision a serious market panic.*

12) Perhaps most importantly for markets, the Federal Reserve has reiterated its commitment to keeping interest rates very low for the foreseeable future. On top of the new lower tax rates, corporations are borrowing money at incredibly low rates, locking in cheap financing for years to come. This should help prolong the economic cycle. As we've discussed countless times, these low rates also make bonds a poor substitute for stocks for investors in need of long-term appreciation. Large institutional investors in particular require mid-to-high single digits returns to meet long-term funding needs, and they have little choice but to invest more heavily in "risk-assets", including stocks going forward.