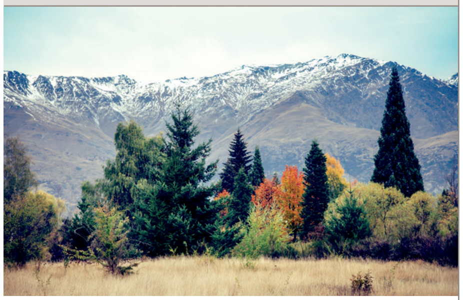
RAYMOND JAMES®

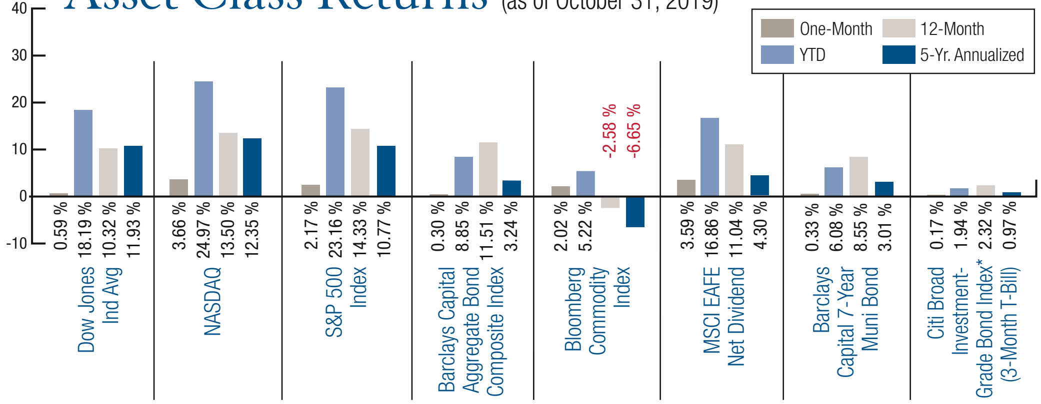
market update

From the Office of Jeff Sgroi, CFP®



"When we strive to become better than we are, everything around us becomes better, too."
– *The Alchemist by Paulo Coelho*

Asset Class Returns (as of October 31, 2019)



Market & Economic Synopsis

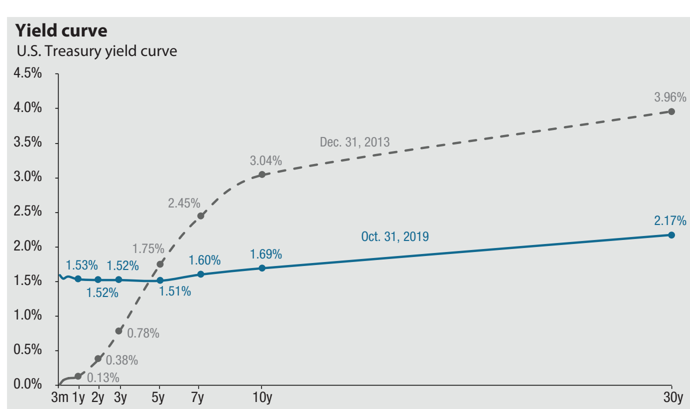
- Federal Open Market Committee lowers Fed Funds Rate for third time in 2019, but hints future cuts may be limited.
- Homebuilders Index gains over 50% YTD on robust residential construction and low-mortgage rates.
- Demonstrations continue in Hong Kong, as protestors seek greater democracy in the Beijing-controlled territory.
- U.S. unemployment rate hovers around multi-decade low of 3.6%.
- Oil prices stabilize recently, as WTI and Brent crude trade on either side of $60, respectively.
- U.S. Treasury yield curve steepens slightly, temporarily alleviating concerns brought on by inverted yield curve earlier in the year.
- Information technology, communication services, and industrial sectors lead domestic equity markets year to date. Energy and healthcare lag other sectors and broader markets.
- U.S. economy enjoys record 128th month (and counting) of economic expansion.

Observations and Outlook for the Fixed Income Market

Because all-time highs have been recently attained in the U.S. equity markets, much of our attention and excitement has been focused there. Often overlooked is the performance, and significance, of the fixed income markets. With an aging baby boomer population and many portfolio allocations shifting toward a more conservative, income-oriented focus, the importance of bonds cannot be overlooked.

Fixed income markets are driven by many factors, including economic strength, interest rates, inflation pressures, and more. Likewise, although different types of debt may generally move in harmony with one another, different debt asset classes move independently enough to create fantastic investment opportunities from time to time. Below are some of our current observations and views.

A FLAT YIELD CURVE

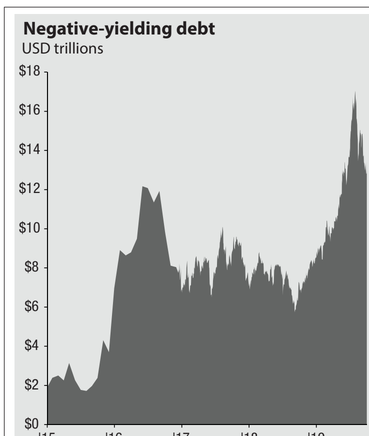


Source: FactSet, Federal Reserve, J.P. Morgan Asset Management.
Guide to the Markets –U.S. Data are as of October 31, 2019.

As of October 31, 2019, the U.S. Treasury yield curve was extremely flat. In simple terms, this means both borrowing expenses and lending income opportunities are comparable, regardless of duration. It tends to mean lower earnings for banks and large financial institutions and can translate into lower credit availability. As illustrated, an example of a more "normal" yield curve shows an upward sloping curve from December 31, 2013. Certainly, the Federal Reserve and economists prefer to see the more traditional slope. It will take monetary policy, economic stability, and open-market forces to bring our current yield curve back to a more traditional position.

NEGATIVE-YIELDING DEBT

Global negative-yielding debt reached an all-time high recently, brought on by weak global economies and subsequent extraordinary efforts by foreign central banks to stimulate economic growth. In short, an example of negative-yielding debt is when depositors are required to pay financial institutions for the opportunity to hold their cash. Specifically, the Bank of Japan and European Central Banks have driven down rates in their respective



Source: J.P. Morgan Asset Management, Bloomberg.
U.S. holdings include households, non-profit organizations, the federal government, nonfinancial corporate businesses, nonfinancial noncorporate businesses, state and local governments, U.S. chartered depository institutions, foreign banking offices in the U.S., banks, credit unions, insurance companies, defined benefit and defined contribution retirements plans, money market funds, mutual funds, closed-end funds, ETFs, broker dealers and holding companies.
Guide to the Markets – U.S. Data are as of October 31, 2019.

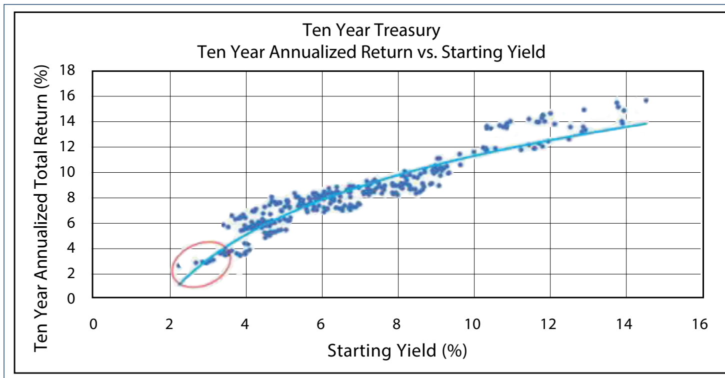
regions in an effort to keep borrowing costs low in an economic experiment comparable to the United States' three rounds of quantitative easing by the Federal Reserve. Long-term effects of negative-yielding debt remains to be seen.

MUNICIPAL BOND MARKETS

Our friends at Thornburg Investment Management recently posted some interesting observations about the flow of cash into the municipal bond fixed income markets. Specifically, the first three quarters of 2019 enjoyed $70 billion of inflow. Of that inflow, $14 billion has moved into high-yield strategies (i.e., higher risk). As they point out, due to the current low-yield environment, investors have had to take additional risk by owning lower-credit debt in order to reach income goals. Thornburg also points out that future changes in performance (i.e., reversal in previously strong municipal fixed-income returns) could be driven by future legislative changes to the State and Local Tax (SALT) deduction that drove new money into this asset class the past two years. In the meantime, we believe that municipal fixed income is a fairly priced asset class as a whole, potentially offering excellent tax-equivalent yields in most non-qualified investment accounts.

PATIENCE IS A VIRTUE

As the chart below illustrates, investors holding debt with a 10-year maturity should expect muted returns over the next 10 years. With the 10-year U.S. Treasury sitting at 1.777% at the time of this writing, upcoming returns are likely to track current inflation rates as a best-case scenario. In short, low-starting yields beget low returns, as would be expected.



Source: Bloomberg L.P. as of September 30, 2019. Data monthly from April 1982.
Ten Year return represented by the Merrill Lynch 10 Year Treasury Futures Total Return Index.
Ten Year Yield represented by the Bloomberg US 10 Year Generic Yield Index.

Despite low-interest rates and benign economic global growth, we believe fixed income remains a good portfolio diversifier due to its low correlation to equity markets. With so many factors moving fixed-income markets and bond prices, we will continue to seek value and diversification in this important and relevant asset class.

From the Homefront

The soccer season was a great success, although we didn't win a single game. All of our 1st and 2nd grade players gave it their best—we had great participation, effort, and attitudes. We are hoping to keep the "Ninjas" together for next year, when we should be a bit older within our age group and hopefully more competitive.

I took Stella back East to Massachusetts to visit my parents in October. It was only the second time she had been to the home where I grew up, and she was much younger during her first trip. We enjoyed a visit to my elementary, junior high, and high schools; a trip to the local ski area where I spent many days on the hill; and walks around the neighborhood looking for birds. At right is a picture of Stella with Grampy entering a corn maze at one of our local farms.

Stella continues to participate in Girl Scouts, and naturally Lily and Hannah want to follow in the steps of their older sister. Hannah has joined the Daisies (1st grade Girl Scouts) and Lily has joined the Tigers (1st grade Cub Scouts). Lily recently took first place in the Cub Scouts' "Rain Gutter Regatta" for her age group, and has gained a lot of confidence in speaking with adults as she has participated in a food drive and wreath sale.

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