THIRD QUARTER 2019

MARKET REVIEW & OUTLOOK

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OVERVIEW - THIRD QUARTER 2019

Major financial asset classes posted mixed results in the third quarter of 2019 after moving higher simultaneously for the first half of the year. The United States generally fared better than the rest of the world as both equity and fixed income markets were positive. Going forward, we are reminding clients to be prepared for an increase in volatility as new developments on the US/ China trade war, Fed policy, economic growth, the upcoming presidential election, and a potential impeachment trial will continue to impact markets.

In our writings and conversations with clients we always stress the power of combining a comprehensive financial plan with a structured, consistent, and repeatable investment process. We continue to believe this is the best approach for helping our clients navigate through financial markets and ultimately reach their goals and objectives.

At Winthrop Wealth Management, we feel privileged to work with you and your families. We hope that you have an enjoyable Fall and holiday season (it will be here before you know it!). As always please call us with any questions, we look forward to speaking with you in the near future.

- **US Equity Markets:** The S&P 500 returned +1.7% in the third quarter and is now up +20.6% in 2019 – the best start to a calendar year since 1997 and the 21st overall since 1928. The market reached a new all-time high on July 26th. *Page: 1*
- **US Fixed Income Markets:** The Barclays US Aggregate Bond index (Agg), which acts as a proxy for the investment-grade bond market, increased by +2.3%. The Agg is now up +8.5% in 2019. Interest Rates: Treasury yields declined throughout the quarter due to low global interest rates and expectations of lower inflation and economic growth in the United States. Yield Curve Inversion: The 10YR-3M spread ended the quarter inverted at -16bps while the 10YR-2YR finished positive at +4bps after inverting for a few days toward the end of August. *Page: 2*
- **US – China Trade War Update:** The US and China both implemented new tariffs before agreeing to resume negotiations in mid-October. The trade war has been a drag on the global economy. *Page: 3*
- **The Fed:** The Federal Open Market Committee (FOMC) cut the federal funds rate by a total of 0.50% to a range of 1.75% to 2.00%. We expect that trade policy will continue to drive monetary policy. *Page: 4*
- **US Economy:** The economy has bifurcated with the consumer driving growth while the manufacturing sector has slowed to contraction territory. According to the latest Bloomberg survey, GDP is expected to increase by 2.3% year-over-year (Y/Y) in 2019, down from 2.9% in 2018. *Page: 6*
- **Developed International:** The MSCI EAFE index decreased by -1.1% in the quarter and the European Central Bank (ECB) unveiled another round of monetary stimulus. *Page: 7*
- **Emerging Markets:** The MSCI Emerging Markets index declined by -4.3%. The main story in Emerging Markets continues to be the stock market decline and economic slowdown in China. *Page: 7*
- **Key Risks:** A few things we are discussing internally as we balance short-term developments with our long-term viewpoint. *Page: 8*
- **Client Question(s) of the Month:** The answer to, "how's the market doing" can sometimes depend on the index used. We examine the differences between the three most widely referenced US indices. *Page: 9-10*
- **US Equity Market Outlook:** As we move into the fourth quarter of 2019 and beyond, we continue with a balanced outlook for the US equity market, although throughout the year we have defensively shifted portfolios. Our outlook is primarily based on our viewpoints across economic growth, central bank policy, corporate fundamentals, and valuation - the trade war continues to impact each category. *Page: 11*

(Source: Bloomberg)

US Equity Markets									
Index	**Q3 2019**	**YTD 2019**	**1YR**	**3YR**	**5YR**	**2018**	**2017**	**2016**	**2015**
S&P 500	1.70%	20.55%	4.25%	13.39%	11.12%	-4.39%	21.82%	11.95%	1.37%
Russell 3000	1.16%	20.09%	2.91%	12.82%	10.74%	-5.25%	21.12%	12.72%	0.47%
Dow Jones Industrial Average	1.83%	17.51%	4.21%	16.43%	12.58%	-3.48%	28.11%	16.43%	0.21%
Nasdaq	0.18%	21.56%	0.55%	15.94%	13.96%	-2.81%	29.73%	8.97%	7.11%
S&P 400	-0.09%	17.86%	-2.51%	9.37%	9.18%	-11.10%	16.23%	20.73%	-2.18%
Russell 2000	-2.41%	14.15%	-8.92%	8.21%	8.49%	-11.03%	14.63%	21.28%	-4.41%

International Equity Markets									
MSCI Index	**Q3 2019**	**YTD 2019**	**1YR**	**3YR**	**5YR**	**2018**	**2017**	**2016**	**2015**
EAFE	-1.07%	12.80%	-1.34%	6.48%	3.44%	-13.79%	25.03%	1.00%	-0.81%
Europe	-1.79%	13.90%	-2.17%	7.11%	3.23%	-16.90%	28.06%	1.34%	-1.42%
Japan	3.13%	11.12%	-4.69%	6.22%	5.72%	-12.88%	23.99%	2.38%	9.57%
China	-4.40%	7.76%	-3.75%	8.11%	6.24%	-18.75%	55.34%	0.94%	-7.88%
Emerging Markets	-4.25%	5.89%	-2.02%	5.97%	2.50%	-14.57%	37.28%	11.19%	-14.92%
ACWI ex US	-1.80%	11.56%	-1.23%	6.33%	3.08%	-14.20%	27.19%	4.50%	-5.66%

Fixed Income Markets									
Bloomberg Barclays US Bond Index	**Q3 2019**	**YTD 2019**	**1YR**	**3YR**	**5YR**	**2018**	**2017**	**2016**	**2015**
Agg	2.27%	8.52%	10.30%	2.92%	3.28%	0.01%	3.54%	2.65%	0.55%
Treasury Bills	0.54%	1.76%	2.33%	1.49%	0.94%	1.82%	0.82%	0.26%	0.03%
Barclays Capital US Credit Bond	3.05%	13.20%	13.00%	4.50%	4.58%	-2.51%	6.42%	6.11%	-0.68%
Barclays US Corporate High Yield Bond	1.33%	11.41%	6.36%	6.07%	5.34%	-2.08%	7.50%	17.13%	-4.47%
Barclays Capital Municipal Bond	1.58%	6.75%	8.55%	3.19%	3.62%	1.28%	5.45%	0.25%	3.30%

US EQUITY MARKETS

The S&P 500 returned +1.7% in the third quarter and is now up +20.6% in 2019 – the best start to a calendar year since 1997 and the 21st overall since 1928. The market reached a new all-time high on July 26th when the S&P 500 hit 3,028 and now it sits about -2% below that high watermark. We will also point out that a lot of the strong performance in 2019 is partially just a rebound from the selloff we saw at the end of last year when the S&P posted the first calendar year loss since 2008 (-4.4%) and the worst December monthly return since 1931 (-9.0%). On a 1-year basis, the market is up a more modest +4.3%.

Across market caps, Large (S&P 500: +1.7%) outperformed Mid (S&P 400: -0.1%) and Small (Russell 2000: -2.4%). Across styles, Growth (Russell 1000 Growth: +1.5%) slightly outperformed Value (Russell 1000 Value: +1.4%). Eight out of eleven sectors were positive in the quarter, with the beneficiaries of falling interest rates, Utilities (+9.3%) and Real Estate (+7.7%) as the best performers. Energy (-6.3%) and Health Care (-2.3%) were the laggards.

Throughout the year the markets have wrestled with the competing forces of the escalating US/China trade war and accommodative Fed policy. While tariffs and the resulting business uncertainty have weighed on markets, lower interest rates have provided support. During the quarter, the US implemented new 15% tariffs on $110 billion worth of Chinese imports while China responded with tariffs on $75 billion of US products. The Trump Administration also threatened new tariffs and to raise the rate on existing levies before the end of the year. Despite the new tariffs, tensions cooled toward the end of the quarter and the two sides will resume negotiations in Washington in early October. The Federal Reserve did their part to try and offset the negative impacts of the trade war by cutting the federal funds rate by 50bps total (0.25% at the July and September meetings respectively). The Fed may cut again before the end of the year and will likely keep interest rates low for as long as the trade war carries on. *See below for our thoughts on the US/China trade war, the Fed, and our market outlook.*

S&P 500 (YTD 2019)

(Source: Bloomberg)

Quick Thoughts on Impeachment

On September 24th, Speaker of the House of Representatives Nancy Pelosi formally announced an impeachment inquiry of President Trump. The inquiry relates to a July 25th phone call where Trump asked Ukrainian President Volodymyr Zelensky to "look into" former Vice President Joe Biden. According to Bloomberg, the House has initiated impeachment proceedings more than 60 times and voted to impeach 15 federal judges, 1 senator, 1 cabinet secretary, and 2 presidents (Andrew Johnson in 1868 and Bill Clinton in 1998). In order to impeach a sitting president, the House must pass the vote with a simple majority and then the Senate needs to convict with a two-thirds supermajority. Barring new information, a two-thirds supermajority conviction is unlikely in the Senate. The political drama will continue for the foreseeable future, but it probably won't weigh on markets unless the probability of impeachment increases. We will point out that the inquiry decreases the odds that Congress can work together to pass the USMCA trade agreement, a budget deal, drug price legislation, or various other bills.

US FIXED INCOME MARKETS

Bonds produced positive results for the quarter as the decrease in interest rates was positive for fixed income returns (bond prices move inversely to interest rates). The Barclays US Aggregate Bond index (Agg), which acts as a proxy for the investment-grade bond market, increased by +2.3% in Q3 and is now up +8.5% in 2019. Other sectors of the fixed income market, including Treasury Bills (Bloomberg Treasury Bills: +0.5%), Credit (Bloomberg Corporates: +3.1%), Munis (Bloomberg Municipal Bond: +1.6%), and High Yield (Bloomberg High Yield: +1.3%) also posted solid results in the quarter.

INTEREST RATES

Treasury interest rates declined throughout the quarter due to low global interest rates and expectations of lower inflation and economic growth in the United States. The 2-Year Treasury yield declined from 1.75% to 1.62% while the 10-Year Treasury decreased from 2.01% to 1.66%. The decline in global interest rates has been one of the biggest surprises of 2019.

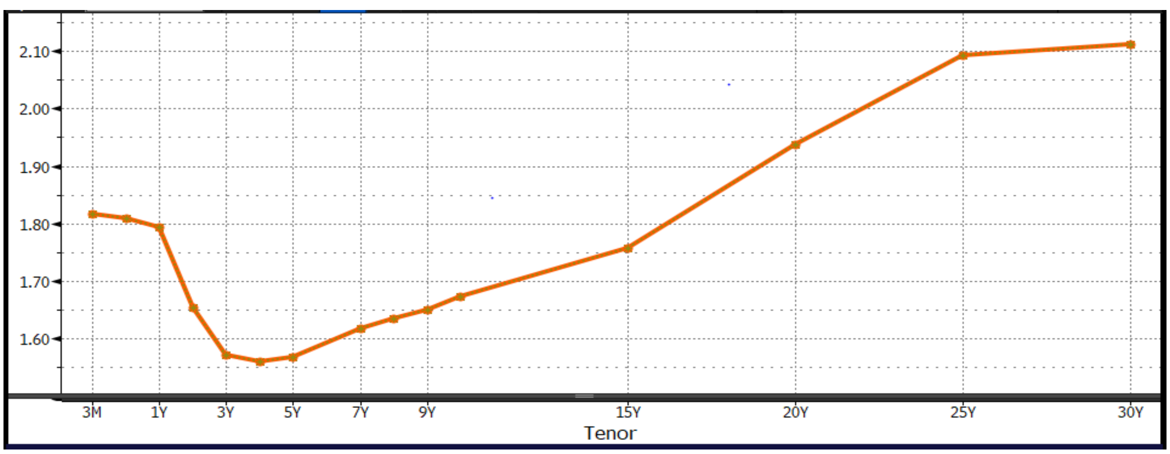
- Low global interest rates: while the 10-Year Treasury yield of 1.66% is close to its all-time low of 1.32% (July 2016), the current yield is still higher than many global rates. Due to weak inflation and economic growth forecasts, and their own versions of quantitative easing, 10-Year yields in Japan and Europe are currently negative. The Japanese and German 10-Year yields ended the quarter at -0.21% and -0.57% respectively. Due to the ongoing Brexit saga, the 10-Year yield in the UK is 0.49%. Currently, there is an estimated $15 trillion in global debt with negative yields. Therefore, US yields are still comparatively attractive for global investors. ***Please see our Client Question of the Month on Negative Yields.***

- Expectations of future inflation and economic growth: Treasury securities are considered close to "risk free" because the principal and interest payments are backed by the US government. In general, when expectations for inflation and economic growth are poor investors will buy Treasuries because of their perceived safety in a weak investment environment. This "flight to safety" pushes Treasury prices up and yields down. Recent inflation readings have been weak as Core PCE Inflation came in at 1.8% Y/Y in August, below the Fed's 2% symmetric target. Core PCE inflation has averaged about +1.6% over the last 10-years, which has helped to keep rates low. Economic growth has slowed as according to the latest Bloomberg survey, GDP is expected to increase by 2.3 Y/Y in 2019 compared to 2.9% in 2018.

TREASURY YIELD CURVE INVERSION

The yield curve is a graph of a Treasury bond's maturity and its rate of return for various time periods. The typical maturities referenced generally range from 3-Months to 30-Years. A yield curve inversion occurs when short-term maturities have higher yields than longer-term maturities. An inversion is the market's sign of a pessimistic economic outlook. Historically, an inversion usually means the market is forecasting an economic recession or slowdown. The inversion usually occurs when there is a "flight to safety" and investors buy longer-term Treasuries. In this scenario, investors expect the Fed will likely cut short-term rates, which explains why they would be willing to accept lower yields for longer maturities. An inversion is usually the markets way of telling the Fed that it needs to cut rates. There are two common spreads associated with a yield curve inversion: the 10-Year Treasury minus the 3-Month Treasury yield (10YR-3M) and the 10-Year Treasury minus the 2-Year Treasury yield (10YR-2YR). The 10YR-3M spread ended the quarter inverted at -16bps while the 10YR-2YR finished positive at +4bps after inverting for a few days toward the end of August. Historically, the average lag time between a yield curve inversion and the start of a recession has been about a year-and-a-half. ***Please see our Q1 2019 Market Recap and Outlook for implications and analysis of a yield curve inversion.***

TREASURY YIELD CURVE



(Source: Bloomberg)

US - CHINA TRADE WAR UPDATE

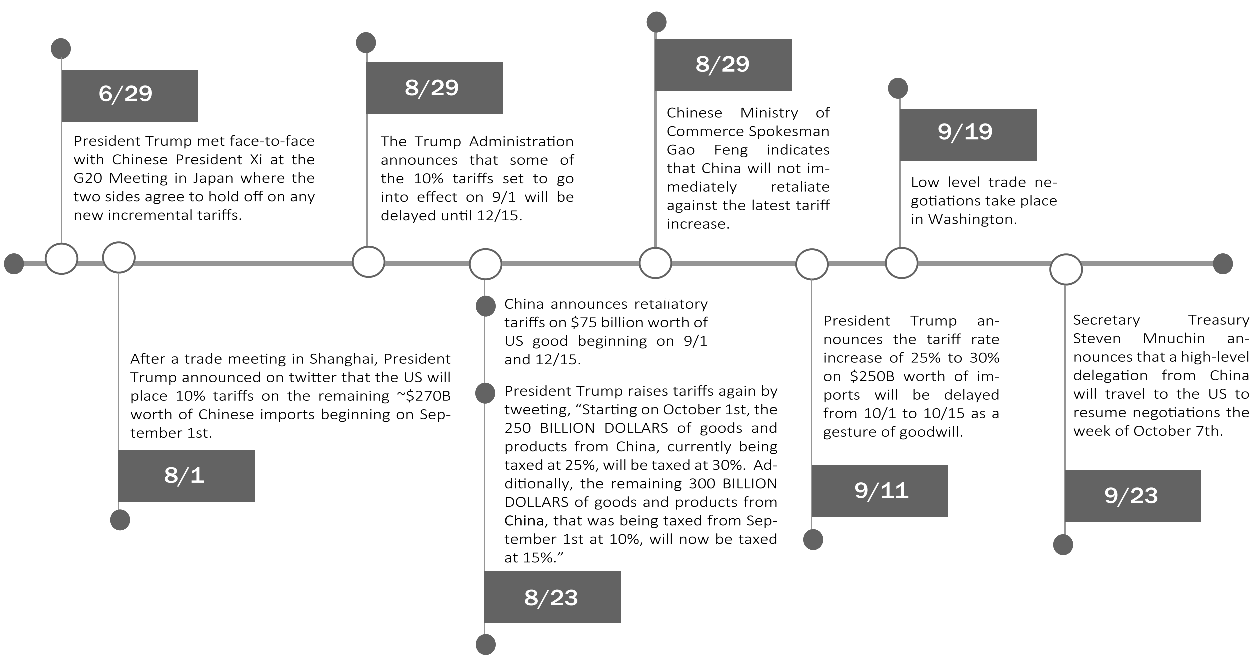
The US and China trade negotiations remained front page news throughout the quarter as tensions and the prospects for a deal continued to ebb and flow. The two sides were able to reach a temporary ceasefire after President Trump met face-to-face with Chinese President Xi at the G20 Meeting in Japan at the end of June. However, the temporary truce did not last long. After a meeting in Shanghai in July yielded little progress, Trump threatened to impose new tariffs on the remaining amount of imports from China starting on September 1st. In mid-August the US decided to roll out the new tariffs in two stages with the later going into effect in mid-December to ease the burden on consumers during the holiday season. After China responded with tariffs of their own, the US announced a plan to increase the rate on current and future levies – this was the current low point in the trade war. Tensions then began to cool as China resumed agricultural purchases and the US agreed to delay the tariff rate increase from 10/1 to 10/15. High level negotiations are expected to resume in the US in early October.

TARIFF SCOREBOARD

	CURRENT	THREATENED
US	25% tariffs on $250B worth of imports including semiconductors, aircraft parts, chemicals, and furniture 15% tariffs on $110B worth of imports including clothes, shoes, and agricultural products	**October 15th:** the tariff rate on $250B worth of imports is scheduled to increase from 25% to 30% **December 15th:** new 15% tariffs on $160B worth of imports including smartphones and laptops
China	5% to 25% tariffs on $110B of imports including oil, soybeans, beef, chicken, and fiber-optic cables	

The trade war is a major issue due to the potential negative impacts on economic and corporate earnings growth. The Federal Reserve Bank of New York estimated that the current tariffs will cost the average US household $831 per year due to higher prices and reduced economic efficiency. The current consensus estimate for 2019 United States GDP growth is 2.3% Y/Y. Bloomberg estimates that the tariffs could decrease Q4 2019 US GDP growth by-0.5%. The Federal Reserve estimated that the impact of trade policy uncertainty will account for a-1% cumulative decline on US GDP by the middle of 2020. JP Morgan estimates that current tariffs will decrease 2020 S&P earnings by-5% to-7% depending on the rate and amount. Several companies have stated they will raise prices, accept lower margins, or shift their supply chains out of China in response to the tariffs.

The trade war has followed a cyclical pattern where discussions don't lead to agreements, tensions rise, tariffs are implemented, the two sides reset, tensions cool, and negotiations resume. While we are pleased that both countries will meet again in October, we still feel that a full and comprehensive agreement is not imminent. A comprehensive agreement would address six areas: forced technology transfer and cyber theft, intellectual property rights, services, currency, agriculture, and non-tariff barriers to trade. Over the past few weeks there have been rumors that a partial agreement that addresses intellectual property and forced technology transfer is possible in the next few months. While President Trump has called for a complete deal, a partial one would be a positive for the global economy and could break the impasse. The trade war will remain a stock market risk and a drag on the global economy until an agreement is signed and tariffs are eliminated. As we've stated before, we remain optimistic that an agreement will eventually be reached as it would be in the best economic interest of both countries.



THE FED

In the third quarter, the Federal Open Market Committee (FOMC) cut the federal funds rate by 0.50% total (0.25% at the July and September meetings respectively). The rate cuts were the first since December 2008 and the current federal funds rate now stands at a range of 1.75% to 2.00%. The September meeting statement continued to contain the phrase the committee will "act as appropriate to sustain the expansion." While the FOMC still has a favorable outlook about the US economy, Chairman Powell stated that "it's better to be proactive" with monetary policy to guard against a slowdown.

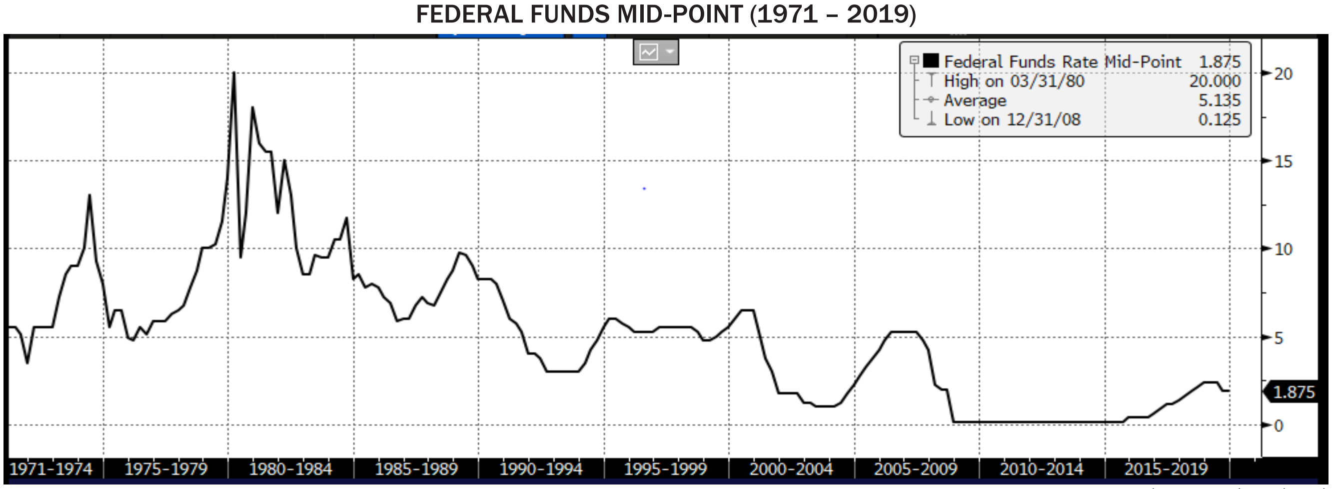
At the July meeting, Chairman Powell cited three reasons for the rate cut: slowing global growth, trade policy uncertainty, and muted inflation. In our opinion, the trade war has significantly contributed to the global economic slowdown this year. In an August speech at the Jackson Hole Symposium on Monetary Policy, Chairman Powell stated that "fitting trade policy uncertainty" into the Fed's framework is a new challenge and there are "no recent precedents to guide any policy response to the current situation." At the latest press conference, Powell said the word "trade" 31 times and noted that trade policy uncertainty has discouraged business investment. Regarding inflation, the Fed's preferred measure, Core PCE Inflation, was 1.8% Y/Y in August, below the 2% symmetric target. Core PCE has averaged 1.6% Y/Y over the last ten years. The Fed is hoping that rate cuts will boost inflation closer to their target.

An interesting note from the September meeting was that three of ten voting members dissented to the committee's decision to lower interest rates. Two members favored no interest rate cut while one voted for a 0.5% cut. This was the first FOMC decision with three dissenters since 2006. Given the varying views of the committee members, Chairman Powell stressed that the Fed will be flexible and data dependent regarding future interest rate moves. Throughout the press conference Powell tried to enforce that future rate decisions are not on a preset course. The markets reacted positively when Powell answered a question about a slowdown by implying flexibility and stating, "if the economy does turn down, then a more extensive series of rate cuts may be warranted." The takeaway is that while the Fed still expects a strong economy, they will react appropriately if needed.

The FOMC also released their Summary of Economic Projections (SEP) where each of the seventeen members individually and anonymously forecast Real GDP, the unemployment rate, inflation, and the federal funds rate. The Fed releases the median economic projection for each data point. The Summary of Economic Projections are not meant to be a policy roadmap, but rather to provide insight into what individuals on the committee are thinking. Individuals do not consult with each other when filling out their projections. The SEP's median forecast for the 2019 federal funds mid-point rate was 1.9% (the present level). However, seven out of seventeen members projected one more 25 basis point rate cut this year (this would decrease the federal funds rate range to 1.50% to 1.75%) - this reinforces the view that the Fed is divided on where to go from here. The current odds for at least one more rate cut by the end of 2019 are currently at about 70%.

One of the biggest surprises of 2019 has been the Fed pivot to a far more accommodative monetary policy than estimated at the end of last year. In December 2018, the Fed projected two rate hikes in 2019 and did not even want to discuss the possibility of altering the balance sheet runoff of $50 billion per month. Throughout the year the Fed has cut interest rates twice and ended their balance sheet runoff. This is an extraordinary shift in policy in a relatively short amount of time. Our view is that the ongoing US/China trade war and resulting economic weakness has forced the Fed to lower interest rates to guard against a material slowdown in the United States. The longer that tariffs remain in place and the more President Trump threatens or implements new tariffs, the more likely the Fed will lower interest rates in response. If the US and China trade talks did not fall apart in May and the two sides reached an agreement as most investors expected at that time, we highly doubt the Fed would have lowered rates in July or September. Going forward, we expect that trade policy will continue to drive monetary policy and further rate cuts will be needed only if the US and China trade war escalates.

FEDERAL FUNDS MID-POINT (1971 – 2019)



(Source: Bloomberg)

US ECONOMY

OVERALL	TREND

The US economy is still doing well despite decelerating from 2018 levels. According to the latest Bloomberg survey, GDP is expected to increase by 2.3% Y/Y in 2019, down from 2018's 2.9% level. The economy has bifurcated with the consumer driving growth while the manufacturing sector has slowed to contraction territory. The consumer remains strong and is supported by a solid labor market (consumer spending accounts for close to 70% of GDP). The housing market has shown signs of acceleration due to the recent fall in mortgage rates. Meanwhile, the manufacturing sector has weakened to contraction territory (ISM Manufacturing Index under 50.0) as tariffs have forced domestic companies to delay major spending outlays and examine alternative supply chains. Manufacturing data has been steadily decelerating since tariffs went into effect in mid-2018.

LABOR MARKET

OVERALL	TREND

- **Unemployment Rate (August): 3.7%**

2019 Average: 3.8% 5YR Average: 4.5% 15YR Average: 6.2%

o The Bureau of Labor Statistics Unemployment Rate tracks the number of unemployed persons as a percentage of the labor force. The unemployment rate is calculated from the Current Population Survey (CPS).

- **Change in Nonfarm Payrolls (August): +130,000**

2019 Average: 166,000 5YRAverage: 204,000 15YR Average: 109,000

o The Bureau of Labor Statistics Nonfarm Payrolls measures the monthly change in the number of employees on business payrolls. Approximately 150k businesses and government agencies representing 700k individual worksites are surveyed each month. Data is from the Current Employment Statistics (CES) survey.

- **Average Hourly Earnings Wage Inflation (August): +3.2% Y/Y**

2019 Average: 3.2% 5YR Average: 2.6% 15YR Average: 2.5%

o The Bureau of Labor Statistics Average Hourly Earnings tracks total hourly compensation (in cash or in kind) paid to employees in return for work done (or paid leave). Data is from the Current Employment Statistics (CES) survey.

CONSUMER

OVERALL	TREND

- **Retail Sales (August): +4.1% Y/Y**

2019 Average: 3.1% 5YR Average: 3.7% 15YR Average: 3.4%

o The US Census Bureau Retail Sales data tracks the resale of new and used goods to the general public for personal or household consumption. Data is adjusted for seasonal variation and holiday and trading-day differences and calculated from a survey of approximately 5,500 retail and food services firms.

- **University of Michigan Consumer Sentiment (September):** 93.2

2019 Average: 95.9 5YR Average: 94.8 15YR Average: 83.0

o The University of Michigan collects data on consumer attitudes and expectations. The index is comprised of measures of attitudes toward personal finances, general business conditions, and market conditions or prices. A higher reading signals better sentiment.

- **Personal Spending (August):** +3.7% Y/Y

YTD Average: +3.9%. 5YR Average: +4.3%. 15YR Average: +4.0%

o The Bureau of Economic Analysis publishes Personal Income and Spending data. Personal Spending tracks consumer expenditures on goods and services. The data is designed to provide insight into the strength of the economy and consumers' buying trends.

HOUSING

OVERALL	TREND

- **Existing Home Sales (August): 5.49 million**

2019 Average: 5.27 5YR Average: 5.35 15YR Average: 5.17

o The National Association of Realtors Existing Home Sales tracks total existing home sales including single family homes, townhomes, condominiums, and co-ops. Data is adjusted for seasonal variation.

- **Case-Shiller 20-City Home Price Index (July): 2.00% Y/Y**

2019 Average: 3.74% 5YR Average: 5.07% 15YR Average: 2.56%

o The S&P Case-Shiller US National Home Price Index tracks the value of single-family housing within the United States. The index is a value-weighted average of 20 metro areas.

- **30-Year Fixed Rate Mortgage: 3.75%**

2019 Average: 4.06% 5YR Average: 3.98% 15YRAverage: 4.66%

o Bankrate.com calculates the national average 30-Year Fixed Rate Mortgage.

MANUFACTURING

OVERALL	TREND

- **ISM Manufacturing Index (August): 49.1**

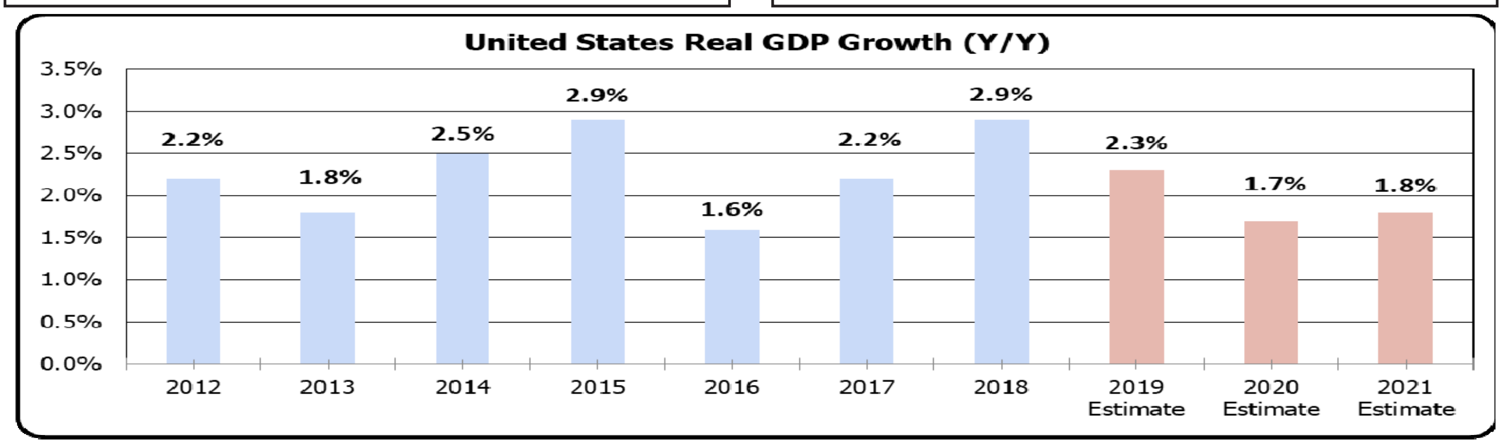
2019 Average: 53.0 **5YR Average:** 54.5 **15YR Average:** 53.3

o The ISM Manufacturing Index is based on a survey of more than 300 manufacturing firms - the index monitors employment, production, inventories, new orders, and supplier deliveries. A reading above 50 indicates that the manufacturing economy is generally expanding; below 50 indicates that it is generally contracting.

- **Durable Goods Orders (August): 0.2% Y/Y**

2019 Average: 1.5% **5YR Average:** 1.7% **15YR Average:** 2.3%

o The US Census Bureau Durable Goods New Orders Ex Transportation survey is a report that tracks the value of new orders received. Durable goods are manufactured products designed to last three years. The survey is based on ~5,000 reporting units representing ~3,100 companies in the Manufacturing Sector.



(Source: Bloomberg)

FOREIGN MARKETS

DEVELOPED INTERNATIONAL

The MSCI EAFE index decreased by -1.1% in the quarter and is now up +12.8% for the year. The EAFE index includes a broad range of equities located in several international countries, including Japan, the United Kingdom, France, Germany, Italy, and others. Within International Markets, the MSCI Europe index declined by -1.8% while the MSCI Japan index gained +3.1% and the MSCI United Kingdom index dropped by -2.5%.

The main story in developed international markets was the economic slowdown in the eurozone and the subsequent monetary stimulus unveiled by the European Central Bank (ECB). In Q2, the eurozone economy expanded by only a 0.2% seasonally adjusted rate. Over the same time period, the German economy declined by -0.1% with government leaders blaming the contraction on the uncertainty caused by the US/China trade war and Brexit. If the German economy contracts again in the third quarter, it will enter an official recession. The ECB responded to the economic slowdown by announcing further rate cuts and a new round of quantitative easing. The central bank moved interest rates further into negative territory by cutting their deposit rate by -0.1% to -0.5%. The ECB's new asset purchase program will be restarted in November at a pace of 20 billion euros per month and will run indefinitely. The new QE program will increase the size of the ECB's balance sheet which now stands at about 4.7 trillion euros – the overall size increased from about 1.5 trillion euros before the financial crisis in 2008. The ECB also nominated former IMF Chairman Christine Lagarde to succeed Mario Draghi as President starting on November 1st.

EMERGING MARKETS

The MSCI Emerging Markets index declined by -4.3% and has returned +5.9% in 2019. MSCI classifies countries as Emerging Markets based on a balance between economic development and financial market accessibility. Some countries included in the Emerging Markets index are Brazil, Russia, India, China, and South Korea. The MSCI China index decreased by -4.4% while MSCI India declined by -0.2%.

The main story in Emerging Markets continues to be the economic slowdown in China partially caused by the ongoing trade war. China's GDP increased by 6.2% in Q2, the slowest pace since 1992 when official records began to be published. Earlier this year, China unveiled its 2019 GDP growth target of 6.0% to 6.5%, a deceleration from 6.6% in 2018. China also announced further fiscal and monetary stimulus measures in order to boost the economy, including tax cuts and a decrease in the required reserve ratio for small and medium size banks. China also devalued their currency (yuan) past the psychologically important 7.0 per dollar level suggesting that the country is preparing for a prolonged trade fight. Despite the stimulus measures, the ongoing trade war and tariffs have had a negative impact as China's manufacturing gauge has been in contraction territory since May and for eight of the last ten months. The trade war will remain a drag on both economies until an agreement is signed.

INTERNATIONAL MARKETS (YTD 2019)

(Source: Bloomberg)

KEY RISKS

This list is not designed to be comprehensive, but rather a few things we are discussing internally as we balance short-term developments with our long-term viewpoint.

US – China Trade War: The US has implemented 15-25% tariffs on $360B worth of Chinese goods and China has placed 5-25% tariffs on $110B worth of US goods. While the resumption of negotiations is positive, the trade war will remain a stock market risk and a drag on the global economy until an agreement is signed and tariffs are eliminated.

US Recession: US economic data showed signs of deceleration from 2018 levels. Although economic data remains at decent levels, we are concerned that the impacts of the US/China trade war, inverted yield curve, manufacturing contraction, and slowing global growth could eventually lead to a recession.

New Tariffs: President Trump has threatened tariffs on countries other than China. In May, President Trump announced that the US would impose tariffs on Mexico that would remain in effect until illegal immigration is curbed. A few days later the two countries were able to reach an agreement to avoid the tariffs. President Trump also delayed 25% tariffs on autos imported from the European Union and Japan. A decision on auto tariffs will likely take place before the end of the year. New tariffs are always one tweet away.

Global Growth Deceleration: Economic growth estimates for 2019 are being cut. China released a growth target of 6.0% to 6.5% (down from 6.6% in 2018). The European Central Bank cut its 2019 GDP forecast from 1.7% to 1.1%. We remain concerned about economic weakness potentially spilling over into the United States.

Yield Curve Inversion: An inverted yield curve (short-term yields higher than long-term yields) has historically been a strong recession indicator. There are two common spreads associated with a yield curve inversion: the 10-Year Treasury minus the 3-Month Treasury yield (10YR-3M) and the 10-Year Treasury minus the 2-Year Treasury yield (10YR-2YR). The 10YR-3M spread ended the quarter inverted at-16bps while the 10YR-2YR finished positive at +4bps after inverting for a few days toward the end of August. Historically, the average lag time between a yield curve inversion and the start of a recession has been about a year-and-a-half.

Brexit: The Brexit situation remains messy and fluid. In July, Boris Johnson took over from Theresa May as the United Kingdom Prime Minister. The UK has until October 31st to finalize a plan on how they are leaving the European Union. Although it is possible that the deadline could be extended further into the future. If there is no agreement it would trigger a so-called “Hard Brexit” where the UK would leave the European Union and then need renegotiate trade deals (this option would cause the greatest amount of short-term economic disruption).

Earnings Disappoint: Earnings growth expectations are for +1.5% in 2019 and +10.5% in 2020. Earnings growth could disappoint if economic growth slows, new tariffs get implemented, or companies lower guidance in fear of potential tariffs.

US Budget Debate: In July, Congress and the White House reached a deal on the government budget and suspended the debt ceiling for the next two years. However, Congress still needs to approve the appropriations bills that specify government spending. In mid-September the House and Senate passed a seven-week stopgap that will fund the government until November 21st, which will hopefully give lawmakers enough time to sort out the details. The impeachment inquiry of President Trump and disagreements over funding the boarder wall make a potential government shutdown more likely.

US Debt Levels: Total US national debt is currently over $22.6 trillion. The public debt to GDP ratio has risen to 82.3% and the 2019 budget deficit is projected at-4.5% of GDP. At some point high debt/deficit levels become unsustainable.

CLIENT QUESTION OF THE MONTH

We've received a few questions over the last several weeks on the differences between major US indices. The answer to, "how's the market doing?", can sometimes depend on the index used. According to the Index Industry Association, there are over 3.3 million indices compiled by 14 different companies. The Financial Times found that on a worldwide basis there are over 70 times more stock indices than there are individual stocks. In our client question of the month we will examine the differences between the three most widely referenced US indices, the S&P 500, the Dow Jones Industrial Average (Dow), and the Russell 3000.

Let's get into the details on the history, structure, methodology, and differences between each index.

History and Structure
S&P 500: The origin of the S&P 500 goes back to 1923, when Standard & Poor's introduced a series of indices that included 233 companies and covered 26 industries. The S&P 500 in its current form was introduced in 1957. The S&P 500 is the only stock market benchmark serving as an economic indicator in The Conference Board Leading Economic Index.

The S&P 500 is widely regarded as the best single gauge of large-cap US equities. Over $6.5 trillion in active funds and $3.4 trillion in passive funds utilize the S&P 500 as a benchmark. The index covers approximately 80% of the investable US equity market. ***Source: S&P Dow Jones Indices***.

The Dow: Charles Dow founded the Dow Jones Industrial Average on May 26, 1896. The Dow was initially comprised of 12 stocks (versus 30 today), including a leather maker, a steel provider, and a sugar producer. According to S&P Dow Jones Indices, the Dow rose to prominence during the stock market crash of 1929 when investors began monitoring the index as a representation for the overall market.

The Dow is a price-weighted index of 30 US blue-chip companies. The index covers approximately 25% of the investable US equity market. The index provides suitable sector representation except for the transportation industry and utilities sector. ***Source: S&P Dow Jones Indices.***

Russell 3000: The Russell US indices were created in 1984 by the Frank Russell Company with the goal of providing accurate representation of the investable US equity market. The Russell indices are designed to provide performance benchmarks for active strategies, as the underlying basis for passive investment products, and as a proxy for US equities in asset allocation decisions.

The Russell 3000 is designed to gauge the entire US stock market. Over $6 trillion in active funds and $1 trillion in passive funds utilize a Russell index as a benchmark. The Russell 3000 index covers approximately 98% of the investable US equity market. Covering the entire US market would require purchasing several thousand small or potentially illiquid companies. ***Source: FTSE Russell.***

How are index weights calculated?
Dow Jones Industrial Average: Price Weighted
In a price-weighted index, the weight of each security is determined by its share price. A stock with a higher share price will have a greater weight and more impact on the index performance than a lower price one. To start, a price weighted index assumes that each security is held in the same quantity. Next, an adjustable divisor accounts for actions that impact the shares outstanding, including, price adjustments, special dividends, stock splits, rights offerings, additions, and/or deletions.

S&P 500 and Russell 3000: Float Adjusted Market Cap Weighted
In a float adjusted market cap index, the weight of each security is determined by its market capitalization (= share price X public shares outstanding). Larger market cap stocks will have a greater weight and more impact on the index performance than smaller ones. Float-adjusted means that the total shares outstanding for each security only includes those that are held by the public and are available for trading. Restricted shares or strategic holdings are not included.

CLIENT QUESTION OF THE MONTH

What are the differences between each index?

The difference between each index is probably best illustrated with the following chart. Note that the S&P 500 and Russell 3000 are similar while the Dow Jones Industrial Average is unique. We believe it is important to understand the differences across methodology, holdings, market caps, sectors, and returns when answering the "how's the market doing?" question or using an index as a benchmark. We will usually reference the S&P as a proxy for the US market since it is the most well-known index, but we prefer the Russell 3000 as a benchmark since it covers most of the investable market by including mid and small cap stocks. At Winthrop Wealth Management, our US equity portfolios most closely resemble the Russell 3000 due to the potential return and diversification benefits of investing in mid and small cap stocks.

S&P 500		Dow Jones Industrial Average		Russell 3000	
Data		**Data**		**Data**	
Inception	1923	Inception	1896	Inception	1984
Constituents	500	Constituents	30	Constituents	3,000
Total Market Cap (trillion)	$25.9	Total Market Cap (trillion)	$7.5	Total Market Cap (trillion)	$31.6
Percentage of US investable market	80%	Percentage of US investable market	25%	Percentage of US investable market	98%
Weighting	Float Adjusted Market Cap	Weighting	Price Weighted	Weighting	Float Adjusted Market Cap
Top 10 Holdings		**Top 10 Holdings**		**Top 10 Holdings**	
Microsoft	4.3%	Boeing	9.1%	Microsoft	3.5%
Apple	3.8%	Home Depot	5.9%	Apple	3.3%
Amazon	3.1%	UnitedHealth Group	5.8%	Amazon	2.6%
Facebook	1.8%	McDonald's	5.5%	Facebook	1.5%
Berkshire Hathaway	1.6%	Apple	5.4%	Berkshire Hathaway	1.4%
JP Morgan Chase	1.5%	Goldman Sachs	5.4%	JP Morgan Chase	1.3%
Alphabet Class C	1.5%	Visa	4.6%	Alphabet Class C	1.2%
Alphabet Class A	1.5%	3M	4.2%	Alphabet Class A	1.2%
Johnson & Johnson	1.4%	Travelers Co	3.8%	Johnson & Johnson	1.1%
Visa	1.3%	IBM	3.6%	Visa	1.1%
Total	**21.6%**	**Total**	**53.2%**	**Total**	**18.3%**
Market Caps		**Market Caps**		**Market Caps**	
Mega Cap (+200B)	39.3%	Mega Cap (+200B)	63.2%	Mega Cap (+200B)	33.2%
Large Cap (15B to 200B)	54.3%	Large Cap (15B to 200B)	36.8%	Large Cap (15B to 200B)	47.1%
Mid Cap (3.5B to 15B)	6.4%	Mid Cap (3.5B to 15B)		Mid Cap (3.5B to 15B)	13.9%
Small Cap (0 to 3.5B)		Small Cap (0 to 3.5B)		Small Cap (0 to 3.5B)	5.8%
GICS Sectors		**GICS Sectors**		**GICS Sectors**	
Communication Services	10.5%	Communication Services	5.0%	Communication Services	9.5%
Consumer Discretionary	10.3%	Consumer Discretionary	13.6%	Consumer Discretionary	10.6%
Consumer Staples	7.5%	Consumer Staples	8.8%	Consumer Staples	6.7%
Energy	4.5%	Energy	4.8%	Energy	4.2%
Financials	13.0%	Financials	15.1%	Financials	13.5%
Health Care	13.6%	Health Care	12.1%	Health Care	13.5%
Industrials	9.3%	Industrials	19.9%	Industrials	10.1%
Information Technology	22.0%	Information Technology	19.6%	Information Technology	21.6%
Materials	2.7%	Materials	1.1%	Materials	2.8%
Real Estate	3.2%	Real Estate		Real Estate	4.2%
Utilities	3.4%	Utilities		Utilities	3.3%
Returns		**Returns**		**Returns**	
YTD 2019	20.6%	YTD 2019	17.5%	YTD 2019	20.1%
1-Year (Annualized)	4.2%	1-Year (Annualized)	4.2%	1-Year (Annualized)	2.9%
3-Year (Annualized)	13.4%	3-Year (Annualized)	16.4%	3-Year (Annualized)	12.8%
5-Year (Annualized)	11.1%	5-Year (Annualized)	12.6%	5-Year (Annualized)	10.7%

(Source: Bloomberg, S&P Dow Jones Indices, and FTSE Russell)

As a quick side note, we notice that references to the Dow mostly occur during periods of market volatility. The price of the Dow is much larger than either the S&P 500 or Russell 3000. As of month end, the price of the Dow was at 26,917, the S&P 500 at 2,977, and the Russell 3000 at 1,743. Note that the price of the index is used to calculate performance and does not reflect the value or total market capitalization of the underlying holdings. While the Dow has the highest price of the three indices, it covers the least amount of the investable US market. We will use the following market drop in August as an example:

Market Return on August 14, 2019			
	Dow	**S&P 500**	**Russell 3000**
Price Movement	-800	-86	-50
Percentage Movement	-3.1%	-2.9%	-2.9%

Anecdotally, we received several more questions referencing the decline in the Dow even though each index was down about -3%. Why? Moves in the Dow just sound more dramatic. The Wall Street Journal headline of "Dow Sheds 800 in Biggest Drop of Year" sounds more severe than "S&P Drops 86" or "Russell 3000 Declines 50". Keep in mind that financial newspapers or televisions stations get paid for readers and viewers, not necessarily for providing sound investment advice. While we monitor the Dow as one of several indices, we notice that others usually bring it up only in reference to large price swings.

EQUITY MARKET OUTLOOK

As we move into the fourth quarter of 2019 and beyond, we continue with a balanced outlook for the US equity market, although throughout the year we have defensively shifted portfolios to help mitigate the potential tail risk of a market selloff caused by the trade war. While we believe the US and China will eventually reach an agreement, we need to be mindful of the risk of an escalation.

In our opinion, the US/China trade war remains the biggest risk to the US economy and stock market. We further acknowledge that it is difficult to have a strong outlook given the uncertainty around future tariffs. While new tariffs are threatened to go into effect on October 15th and December 15th, we have seen threats removed and dates changed several times before. We support the Trump Administration's decision to stand up to China and fight against trade abuses, cybertheft, and forced technology transfer, however we question the use of blanket tariffs (which hurt the US economy) as the best method to reach an agreement. Our view is that the Trump Administration is simultaneously hitting the gas and brake on the stock market and the economy. The gas is lower individual and corporate tax rates, deregulation, high government spending, and low interest rates (from the Fed), which are supporting a strong labor market and consumer. The brake is the trade war and tariffs, which are leading to manufacturing sector weakness and business uncertainty. We would expect President Trump to take his foot off the brake before November 2020 as a recession would not help his re-election chances. However, if President Trump decides to ramp up the trade war it COULD lead to a recession and market selloff.

We would move to a more optimistic stance if the US and China agree to a trade deal where tariffs are rescinded, the Fed remains accommodative, and/or economic and corporate earnings growth start to accelerate. We would turn more cautious if trade talks breakdown and new tariffs are implemented, the Fed returns to restrictive monetary policy, and/or economic and corporate data begin to deteriorate.

Our overall outlook is primarily based on our viewpoints across four different categories. The difficulty in the current environment is that the trade war impacts each segment:

➡ **Economic Growth:** The US economy is still doing well despite decelerating from 2018 levels. According to the latest Bloomberg survey, GDP is expected to increase by 2.3% Y/Y in 2019, down from 2018's 2.9% level. The economy has bifurcated with the consumer driving growth (consumer spending accounts for close to 70% of GDP) while the manufacturing sector has slowed to contraction territory. The consumer is supported by a solid labor market while manufacturing data has been steadily decelerating since tariffs went into effect in mid-2018.

➡ **Central Bank Policy:** In 2019, the Fed pivoted to accommodative monetary policy as they cut interest rates twice and ended their balance sheet runoff. This is an extraordinary shift in policy in a relatively short amount of time. While the FOMC still has a favorable outlook about the US economy, Chairman Powell stated that "it's better to be proactive" with monetary policy to guard against a slowdown. Going forward, we expect that trade policy will continue to drive monetary policy and further rate cuts will be needed only if the US and China trade war escalates.

➡ **Corporate Fundamentals:** S&P 500 earnings are expected to grow at +1.5% in 2019 and +10.5% in 2020. Earnings have decelerated from 2018's +20% level due to the diminishing effects of fiscal stimulus, tariffs, and slowing economic growth. Over long time periods, earnings drive stock prices.

➡ **Market Valuation:** The market valuation ended the quarter slightly higher than its historical average but not excessively so. The S&P 500 Forward P/E is 16.9x, compared to the 25-Year average of 16.2x. The Forward P/E ratio calculated as the current price (2,977) divided by the estimated earnings-per-share over the next 12-months ($176).

Putting it all together, having a balanced outlook and maintaining flexibility is critically important as tariffs can change on a tweet. We will continue to dynamically incorporate new market developments with long-term asset allocation targets as part of our overall investment process.

At Winthrop Wealth Management, we implement a proactive approach to both comprehensive financial planning and investment management. Financial planning drives the investment strategy and provides a roadmap to each client's unique goals and objectives. The comprehensive financial plan defines cash flow needs, optimizes account structures, considers tax minimization strategies, and continuously evaluates financial risks as circumstances and/or goals change. The investment management process is designed to provide well-diversified portfolios constructed with a methodology based on prudent risk management, asset allocation, and security selection. As always, please contact us if you have any updates to your personal or financial circumstances.

DISCLOSURES

The economic forecasts set forth in this material may not develop as predicted and there can be no guarantee that strategies promoted will be successful.

Content in this material is for general information only and not intended to provide specific advice or recommendations for any individual.

Investing involves risk including loss pf principal.

There is no guarantee that a diversified portfolio will enhance overall returns or outperform a non-diversified portfolio. Diversification does not protect against market risk.

Bonds are subject to market and interest rate risk if sold prior to maturity. Bond values will decline as interest rates rise and bonds are subject to availability and change in price.

International investing involves special risks such as currency fluctuation and political instability and may not be suitable for all investors. These risks are often heightened for investments in emerging markets.

The fast price swings in commodities and currencies will result in significant volatility in an investor's holdings.

All indexes mentioned are unmanaged indexes which cannot be invested into directly. Unmanaged index returns do not reflect fees, expenses, or sales charges. Index performance is not indicative of the performance of any investment. Past performance is no guarantee of future results.

The Standard & Poor's 500 Index is a capitalization weighted index of 500 stocks designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries.

The S&P Midcap 400 Stock Index is an unmanaged index generally representative of the market for the stocks of mid-sized US companies.

The Russell 2000 Index is an unmanaged index generally representative of the 2,000 smallest companies in the Russell 3000 index, which represents approximately 10% of the total market capitalization of the Russell 3000 Index.

The prices of small cap stocks and mid cap stocks are generally more volatile than large cap stocks.

The Russell 1000 Growth Index measures the performance of those Russell 1000 companies with higher price-to-book ratios and higher forecasted growth values.

Russell 1000 Value Index measures the performance of those Russell 1000 companies with lower price-to-book ratios and lower forecasted growth values.

The Bloomberg Barclays U.S. Aggregate Bond Index is an index of the U.S. investment-grade fixed-rate bond market, including both government and corporate bonds.

The Barclays Capital U.S. Credit Bond Index measures the performance of investment grade corporate debt and agency bonds that are dollar denominated and have a remaining maturity of greater than one year.

The Barclays Capital Municipal Bond Index is a broad market performance benchmark for the tax-exempt bond market, the bonds included in this index must have a minimum credit rating of at least Baa.

DISCLOSURES

The Barclays Capital US Corporate High Yield Bond index is an index representative of the universe of fixed-rate, non-investment grade debt

The MSCI EAFE Index is a free float-adjusted market capitalization index that is designed to measure the equity market performance of developed markets, excluding the US & Canada. The MSCI EAFE Index consists of the following developed country indices: Australia, Austria, Belgium, Denmark, Finland, France, Germany, Hong Kong, Ireland, Israel, Italy, Japan, the Netherlands, New Zealand, Norway, Portugal, Singapore, Spain, Sweden, Switzerland and the UK.

The MSCI Europe Index captures large and mid cap representation across 15 Developed Markets (DM) countries in Europe*. With 445 constituents, the index covers approximately 85% of the free float-adjusted market capitalization across the European Developed Markets equity universe.

The MSCI Japan Index is designed to measure the performance of the large and mid cap segments of the Japanese market. With 322 constituents, the index covers approximately 85% of the free float-adjusted market capitalization in Japan.

The MSCI India Index is designed to measure the performance of the large and mid cap segments of the Indian market. With 78 constituents, the index covers approximately 85% of the Indian equity universe.

The MSCI EM (Emerging Markets) Index is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of the emerging market countries of the Americas, Europe, the Middle East, Africa and Asia. The MSCI EM Index consists of the following emerging market country indices: Brazil, Chile, Colombia, Mexico, Peru, Czech Republic, Egypt, Greece, Hungary, Poland, Qatar, Russia, South Africa. Turkey, United Arab Emirates, China, India, Indonesia, Korea, Malaysia, Philippines, Taiwan, and Thailand.

The Dow Jones Industrial Average is comprised of 30 stocks that are major factors in their industries and widely held by individuals and institutional investors.

The NASDAQ Composite Index measures all NASDAQ domestic and non-U.S. based common stocks listed on The NASDAQ Stock Market. The market value, the last sale price multiplied by total shares outstanding, is calculated throughout the trading day, and is related to the total value of the Index.

The Russell 3000 Growth Index is an unmanaged index comprised of those Russell 3000 companies with higher price-to-book ratios and higher forecasted growth values. The Russell 3000 Value Index measures the performance of those Russell 3000 companies with lower price-to-book ratios and lower forecasted growth values.

The MSCI China Index is constructed based on the integrated China equity universe included in the MSCI Emerging Markets Index, providing a standardized definition of the China equity opportunity set. The index aims to represent the performance of large- and mid-cap segments with H shares, B shares, red chips, P chips and foreign listings (e.g., ADRs) of Chinese stocks. China A shares will be partially included in this index, making it the de facto index for all of China. It can be used as a China benchmark for investors who use the MSCI ACWI Index or MSCI EM Index as their policy benchmark.

The MSCI ACWI ex USA Index captures large and mid cap representation across 22 of 23 Developed Markets (DM) countries (excluding the US) and 26 Emerging Markets (EM) countries*. With 2,206 constituents, the index covers approximately 85% of the global equity opportunity set outside the US.

The MSCI United Kingdom Index is designed to measure the performance of the large and mid cap segments of the UK market. With 97 constituents, the index covers approximately 85% of the free float-adjusted market capitalization in the UK