PEGASUS
PARTNERS

Market Commentary for Q4'19

2019 was a banner year for the U.S. stock and bond markets. The Russell 3000 Index, which represents approximately 98% of the total U.S. stock market, rose 31.0%, the best year since 2013. Bonds also surged in the year, though most of the return came from a decline in interest rates.

In this day and age of information overload, we have decided to change our quarterly economic and market commentary into a new, visual format that includes more factual information. Instead of a few pages of interesting anecdotes and predictions on the future, we are providing data on seven important economic and market factors that we track on a regular basis. We believe these factors, in total, provide a detailed view of where we are in the current cycle.

Rest assured, we still have very strong opinions on just about everything in the investment world; however, we believe the trends in these seven data points will help paint a picture of what is to come in the next couple of years. Here are the seven categories:

Economic and Market Trends

	2017	2018	*1Q19*	*2Q19*	*3Q19*	*4Q19*	*2019*
U.S. Real GDP Growth	2.2%	2.9%	*3.1%*	*2.0%*	*2.1%*	*2.4%*	2.2%
Global Real GDP Growth	3.8%	3.6%					3.0%
U.S. Yield Curve							
U.S. Unemployment	4.1%	3.9%	*3.8%*	*3.7%*	*3.5%*	*3.6%*	3.6%
Consumer Price Index	2.1%	2.4%	*1.9%*	*1.6%*	*1.8%*	*2.2%*	1.9%
S&P 500 Price/Book	3.2	2.9	*3.3*	*3.3*	*3.4*	*3.7*	3.7
Shiller Price/Earnings	33.3	28.4	*30.1*	*30.0*	*28.8*	*31.1*	31.1

Positive
Relatively Positive
Neutral
Relatively Negative
Negative

Notes: 4Q19 and full year 2019 figures are unrevised and estimated statistics.

Sources: BEA, IMF, Department of Treasury, BLS, Standard & Poor's, Robert Shiller, FactSet

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1. U.S. Real GDP Growth

Other than one quarter above a 3% annual rate and one quarter below 2%, real GDP has consistently grown in the low 2% range. As we say internally, this "barbecue" economy with low and slow growth is generally good for investment markets. *Current Rating:* *relatively positive*

2. Global Real GDP Growth

On a worldwide basis, economic growth has been at a slightly faster pace than within the U.S. However, emerging markets typically grow at a faster clip than developed markets during expansion years. Global growth slowed slightly during 2019. *Current Rating:* *neutral*

3. U.S. Interest Rate Yield Curve

The shape of the yield curve from short and medium-term interest rates (0-10 years) to long-term interest rates (10-30 years) is often a leading indicator for future economic growth. Typically, an upwardly sloped curve indicates expectations for continued economic growth and inflation. Conversely, a downwardly sloped curve commonly suggests a recession is coming. *Current Rating:* *neutral*

4. U.S. Unemployment

High rates of unemployment usually occur during a recession or times of financial distress. Today's 3.6% unemployment rate is well below the historical average and indicates a very healthy job market. *Current Rating:* *positive*

5. Consumer Price Index

Along with the producer price index or GDP deflator, the consumer price index measures the price changes of a basket of goods. Though imperfect, the index gives investors a good idea of how fast purchasing power is being reduced by inflation. Today, inflation is well controlled. *Current Rating:* *positive*

6. S&P 500 Price/Book Value

The Standard & Poor's 500 Index is one of the longest standing major benchmarks. With accurate historical data, we can measure current index price-to-book value compared to prior periods of expansion and recession. Today's 3.7x measure is at the higher end of valuations in the last fifty years.
Current Rating: *negative*

7. Shiller Price/Earnings

Courtesy of Yale professor Robert Shiller, we can measure long-term price-to-earnings ratios adjusted for inflation over the last decade. Shiller's data spans over a century. The current reading of 31.1 is *twice* the historical median and the highest ever, with the notable exception of the "dot com" period from 1998-2001. *Current Rating:* *negative*

Overall Trend Assessment for Equities and Bonds

Adding up the positives and negatives leaves us in a *neutral* position to start calendar 2020. On the bright side are accommodative policies from Washington D.C. and a strong U.S. consumer. High valuations for both stocks and bonds suggest consistent, positive economic growth here and abroad is necessary to maintain the pricing of public securities. In addition, years with presidential elections have, on average, been worse for the markets than years in between elections for the highest office. However, the willingness of the Federal Reserve to maintain financial peace remains a comfort factor for investment risk-takers.

On an unrelated note, Congress recently passed the SECURE Act that addresses a few items related to IRAs. We would characterize the bill as having some positives and some negatives for Pegasus families. Among the positives is a change in the required minimum distribution ("RMD") age from 70 ½ to 72 years old, effective at the start of this calendar year. Roth IRAs will still have no RMDs during your lifetime. However, the new law eliminated the "stretch IRA" provision by requiring beneficiaries to withdraw IRA assets by the end of a ten-year period. For a full list of the law's changes, please contact us at Pegasus.

Your specific asset allocation reports, portfolio performance, long-term performance analysis and cash flow statement are enclosed as well. We welcome your thoughts and questions.

Sincerely,

Pegasus Partners

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