TRIVANT

CUSTOM PORTFOLIO GROUP, LLC

January 2020

Quarterly Insights

Fourth Quarter 2019

EXECUTIVE SUMMARY

2019 - The S&P 500 Index Was Up 31.49%

In 2019, the domestic S&P 500 Index was up 31.49%. There was also good news abroad. Other developed markets and Emerging Markets were up in the 20% range. Our initial 2019 market prediction for the S&P (+8%) was understated because it was predicated on monetary policy expectations. The Fed initially anticipated two rate hikes in 2020. Instead, the Fed surprised us with three rate cuts. The Bloomberg Barclay's Aggregate Bond Index rose 8.68% in 2019.

We Believe The S&P 500 Index Will Rise 11% In 2020

We believe the S&P 500 Index will rise 11% in 2020. There is a healthy US economy, very low unemployment, rising S&P 500 earnings, and reasonable market valuation. The Fed Funds Rate (1.5%) will likely stay where it is. We have both monetary stimulus and fiscal stimulus to fuel the economy. The Fed has started to purchase government securities from the market in order to increase the money supply and encourage lending and investment ("quantitative easing", or "QE"). The level of purchases ($101B a month) is reminiscent of the QE initiated in 2008 ($95B a month). Federal government spending increased 10.23% in 2019 and is projected to increase 4.78% in 2020.

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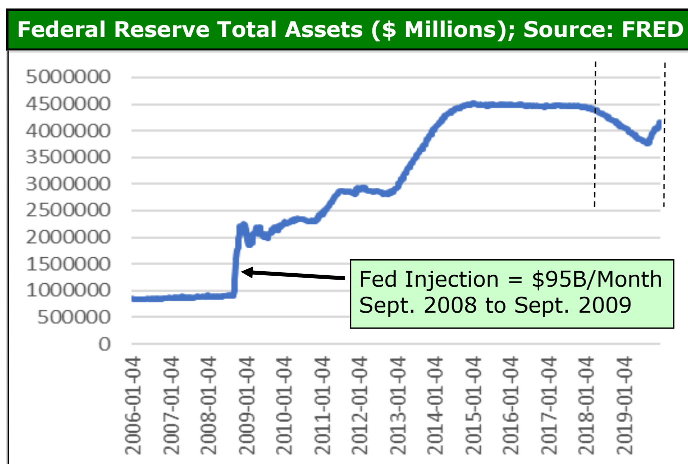
Stock Outlook: We Believe The S&P 500 Index Will Rise 11% In 2020

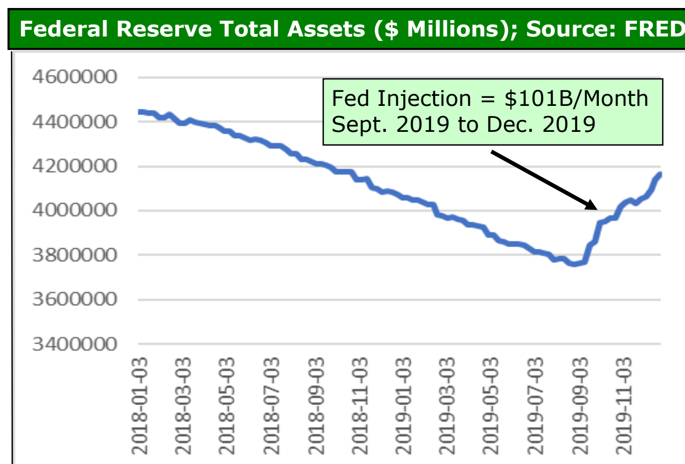
We believe the S&P 500 Index will rise 11% in 2020. Both the Fed and the federal government are taking aggressive actions to grow the economy. Regarding monetary policy, the Fed has initiated quantitative easing and low interest rates. Regarding fiscal policy, the government is spending a lot of money. Amidst these factors, the US business environment remains strong. We have

- A healthy economy (the Fed estimates 2020 US GDP growth of 2.2%)
- Easing trade tensions with China
- Very low unemployment (the Bureau of Labor Statistics reports a 3.6% December unemployment rate)
- Rising S&P 500 earnings (FactSet: earnings will be 9.6% higher in 2020 from 2019 on sales growth of 5.4%)
- Reasonable market valuation (the current trailing PE ratio is 18.9 according to Lipper Alpha Insight)

The Fed Is Fueling The Economy By Pumping Up Its Balance Sheet

Quantitative easing (QE) is a monetary policy where the Fed purchases government securities from the market in order to increase the money supply and encourage lending and investment. Reminiscent of the QE that took place in 2008, the Fed has started to increase its balance sheet and will continue this path into 2020.





The Federal Government Is Fueling The Economy By Increasing Spending

Government spending increased 10.23% in 2019 and is projected to increase 4.78% in 2020. This stimulus is in lockstep with the Fed.

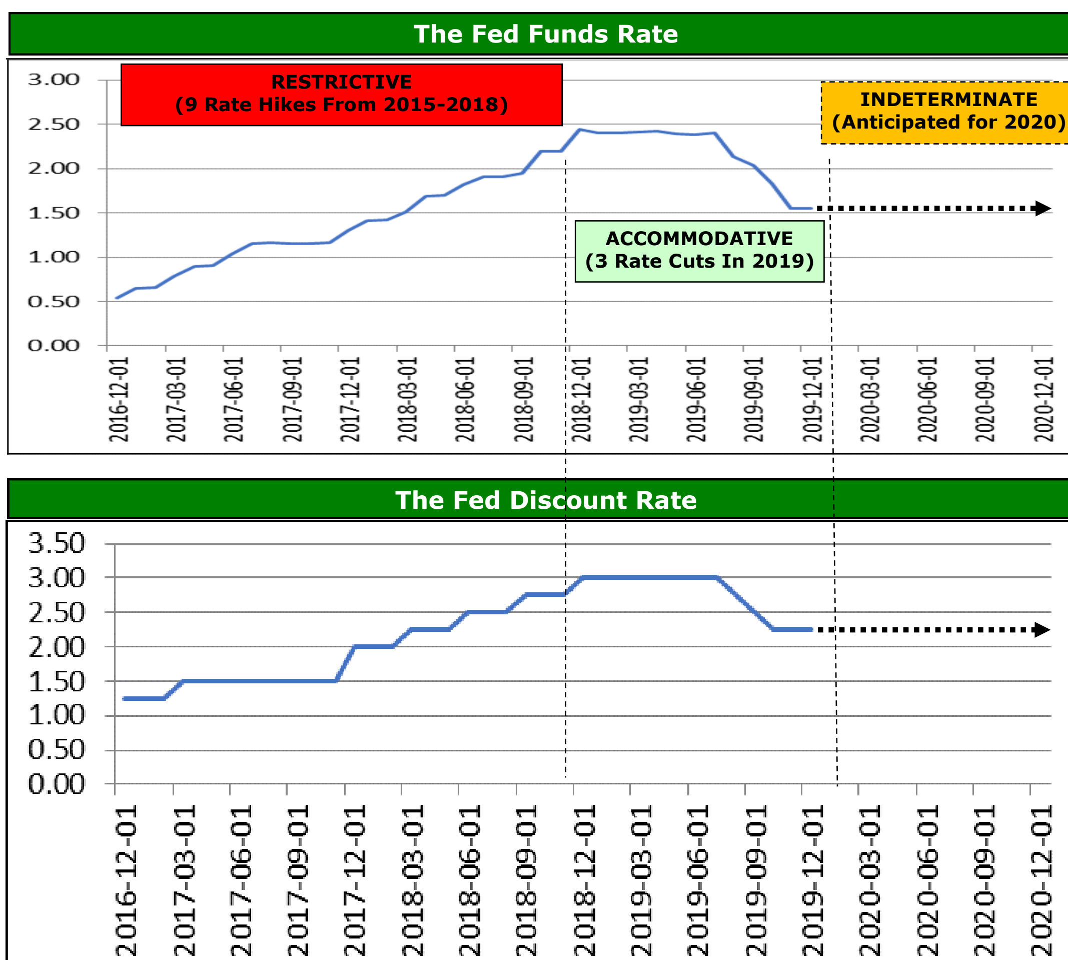
Office of Management and Budget: The White House ($ millions)

Year	Receipts (Revenues)	Outlays (Spending)	Deficit
2016	3,267,961	3,852,612	(584,651)
2017	3,316,182	3,981,628	(665,446)
2018	3,329,904	4,109,042	(779,138)
2019 Estimate	3,437,656	4,529,188	(1,091,532)
2020 Estimate	3,644,772	4,745,573	(1,100,801)

Year	Spending Increase (%)	Administration
2016	4.35%	Obama
2017	3.35%	Obama
2018	3.20%	Trump
2019 Estimate	**10.23%**	Trump
2020 Estimate	**4.78%**	Trump

We Have Very Low Interest Rates That Are Unlikely To Change In 2020

The Fed Funds Rate was hiked nine times (0.25% per hike) since the rate went to zero in 2008. With three surprise rate cuts in 2019, we switched from "Restrictive" to "Accommodative" Monetary Conditions (the Fed Funds Rate and Fed Discount Rate simultaneously fell). The Fed anticipates no rate changes in 2020.



Source: Federal Reserve Bank Economic Data (FRED)

The Fed Is "Boxed In"

The Fed dual mandate is stable prices and full employment. Right now, the Fed has comfortably met these directives (see data below). The Fed is effectively "boxed in". There is little room for further rate cuts because of the resulting inflation risk - and quite frankly, the strong US economy does not justify a further cut. Conversely, there is little room for a rate hike due to relatively weaker global economic conditions and the upcoming US election (the Fed does not want to appear politically biased: a hike would hurt the incumbent). We therefore anticipate a rate pause in 2020 (as does the Fed) and a shift from "accommodative" to "indeterminate" monetary conditions (the Fed Funds Rate and Fed Discount Rate will not be simultaneously rising or falling). The S&P 500 Index historically averages 6.25% under "restrictive conditions", 11.10% under "indeterminate conditions" (our 2020 market prediction) and 14.36% under "accommodative conditions".

Median Economic Projections Of The Federal Reserve Board Members And Bank Presidents (released December 11, 2019)

VARIABLE	2019	2020	2021	2022	LONGER RUN
Change In Real GDP	2.2	2.0	1.9	1.8	1.9
Unemployment Rate	3.6	3.5	3.6	3.7	4.1
PCE Inflation	1.5	1.9	2.0	2.0	2.0
Projected Fed Funds Rate	1.6	1.6	1.9	2.1	2.5

Foreign Exposure Cut Portfolio Performance (Not Risk) Over The Last Decade

The rationale for high (greater than 25%) foreign stock exposure has been erroneously touted as a necessary measure for proper portfolio diversification and risk control. Many managers' models advocate 30%-40% foreign exposure. In fact, we have seen one overly aggressive manager stipulate 40%-50% foreign exposure at all times! Following this line of thought over the last decade would have proven disastrous. Not only would a stock portfolio have carried more risk, it would have suffered greatly in terms of performance. US stocks led foreign stocks in 7 of the last 10 years, often by a large amount. Fortunately we had lower levels of foreign exposure over the last decade (in the range of 8%-18%).

Year	S&P 500 Index (US)	MSCI EMU (Europe)	MSCI Emerging Markets	Out-Performance
2019	31.49%	23.20%	18.42%	**US**
2018	(4.38%)	(16.90%)	(14.58%)	**US**
2017	21.83%	28.06%	37.28%	Emerging Markets
2016	11.96%	1.34%	11.19%	**US**
2015	1.38%	(1.42%)	(14.91%)	**US**
2014	13.69%	(8.39%)	(2.19%)	**US**
2013	32.39%	28.94%	(2.66%)	**US**
2012	16.00%	22.49%	18.69%	Europe
2011	2.11%	(18.40%)	(18.11%)	**US**
2010	15.06%	(3.42%)	19.20%	Emerging Markets

Foreign Exposure Cut Portfolio Performance (Not Risk) Over The Last Half Century

Over the last 50 years, foreign exposure significantly cut portfolio performance and raised portfolio risk (as measured by the standard deviation of returns).

Foreign Exposure Over The Last 50 Years: Less Return And More Risk			
	S&P 500 Index (US)	**MSCI EAFE Index (Foreign)***	**MSCI World Index**
Annualized Return	10.52%	9.21%	9.25%
$1 Invested 50 Years Ago	$148.61	$81.70	$83.38
Risk (Standard Deviation)	17.01%	21.69%	17.44%

* Europe, Australia & The Far East

Why Have Foreign Exposure If It Cuts Performance And Increases Risk?

There are two arguments for having some degree of foreign exposure. First, when we blend US and foreign stocks, we can achieve lower overall portfolio risk than an all-US portfolio. Over the last 50 years, the lowest-risk portfolio would have been weighted 84% US / 16% foreign. Its standard deviation (16.8%) was slightly less than that of the S&P 500 Index (17.01%). Second, domestic/foreign out-performance occurs in streaks.

US Out-Performance Streaks: Last 50 Years

4-Year Streaks: 2013-2016; 1995-1998; 1989-1992
2-Year Streaks: 2018-2019; 2000-2001; 1975-1976

Foreign Out-Performance Streaks: Last 50 Years

6-Year Streaks: 2002-2007; 1983-1988
4-Year Streak: 1971-1974
2-Year Streaks: 2009-2010; 1993-1994; 1977-1978

With smart style rotation decisions, we can benefit from foreign exposure. In our view, a portfolio weighted 80% US / 20% Foreign is reasonable - but a 40%-50% foreign weighting is irresponsible and dangerous! While we may increase our current 9% foreign weight, we will not go overboard. Excessive foreign exposure causes high currency risk, which is especially undesirable for retirees whose expenses are mostly in US Dollars.

Our 2019 Market Prediction Was Inaccurate (Which Was A Good Thing!)

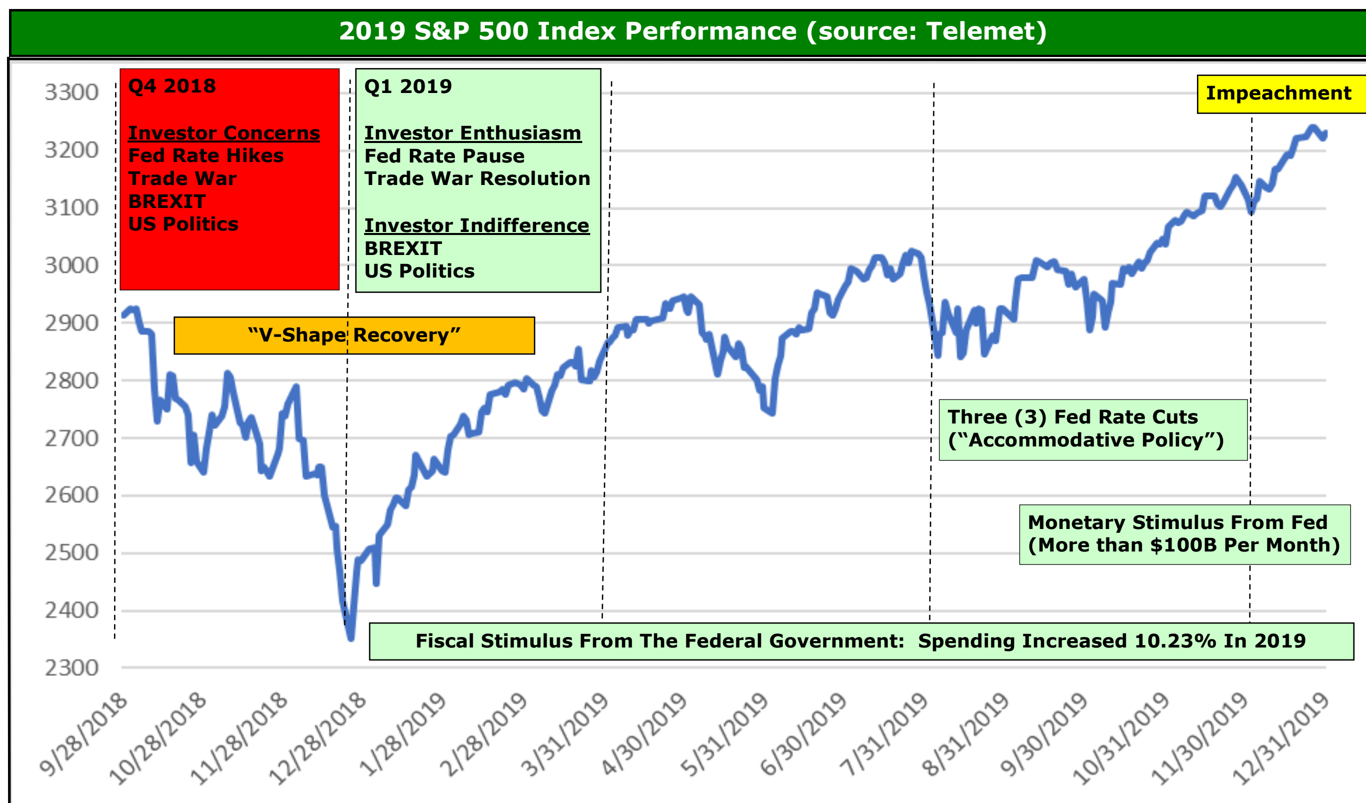
We predicted the S&P 500 Index would rise 8% in 2019 and the index rose 31.49%! Our expectation was predicated on Fed Fund Rate expectations. In December 2018, the Fed anticipated two more rate hikes in 2019 ("restrictive monetary conditions"). We anticipated a 2019 rate pause ("indeterminate monetary conditions"). There were three rate cuts in 2019 ("accommodative monetary conditions"). These were our thoughts:

"We believe the S&P 500 Index will rise 8% in 2019. However, we don't expect a smooth ascent. Negative momentum from Q4 2018 will likely carry through the early part of 2019 and then be followed by a recovery. The pressures that culminated in a tough 2018 (-4.38%) - Fed rate hike sensitivity, the China Trade War, UK BREXIT challenges, and US political turbulence - will not be immediately resolved. However, we expect greater clarity by the end of Q1."

We also viewed the US business environment as strong:
"In this environment, we have
- *A healthy economy (the Federal Reserve estimates 2019 US GDP growth of 2.3%)*
- *Very low unemployment (the Bureau of Labor Statistics reports a 3.9% December unemployment rate)*
- *Decent S&P 500 earnings (the Wall Street consensus estimate is a rise of 8% in 2019)*
- *Reasonable market valuation (the current trailing PE ratio is 15.8 according to Lipper Alpha Insight)"*

What Did We Miss?

1. Accommodative Monetary Conditions - rather than two Fed rate hikes in 2019, we had three rate cuts.
2. Monetary Stimulus - starting in September, the Fed has injected more than $100B a month.
3. Fiscal Stimulus - the federal government increased spending by 10.23% in 2019.
4. US Political Turbulence - political turbulence (culminating in an impeachment) did not derail the market.
5. Trade War With China - the market "brushed off" concerns based on positive tweets from the President.
6. UK BREXIT Challenges - the market hardly reacted during the turmoil or when Boris Johnson prevailed.



2019 - A Remarkably Smooth Market Ascent Given Domestic And Foreign Pressures

We reflect on 2019 as a year where the S&P 500 Index rose in a remarkably smooth manner despite US political turbulence, the China Trade War, challenges in Europe, and BREXIT uncertainty. Early (Q1) rate pause signals, second half rate cuts (3), and Q4 stimulus (all from the Fed) saved the day.

Q1 2019: +13.65%

Q2 2019: + 4.30%

Q3 2019: + 1.70%

Q4 2019: + 9.05%

2019 Total: +31.49%

Biggest Drop (May 6 to June 3): Down 6.41%

1. The US Was The Best Place To Be

We benefited from a very high (over 90%) exposure to US stocks. The US led for reasons including problems in Europe (relatively weaker economy, UK BREXIT uncertainty up until now) and a "flight to quality" (initial response to the ongoing China Trade War). Germany (20.77%,) France (25.72%), the UK (21.05%) and China (23.46%) lagged. With easing trade tensions and Chinese government stimulus , China led in Q4 (+14.71%).

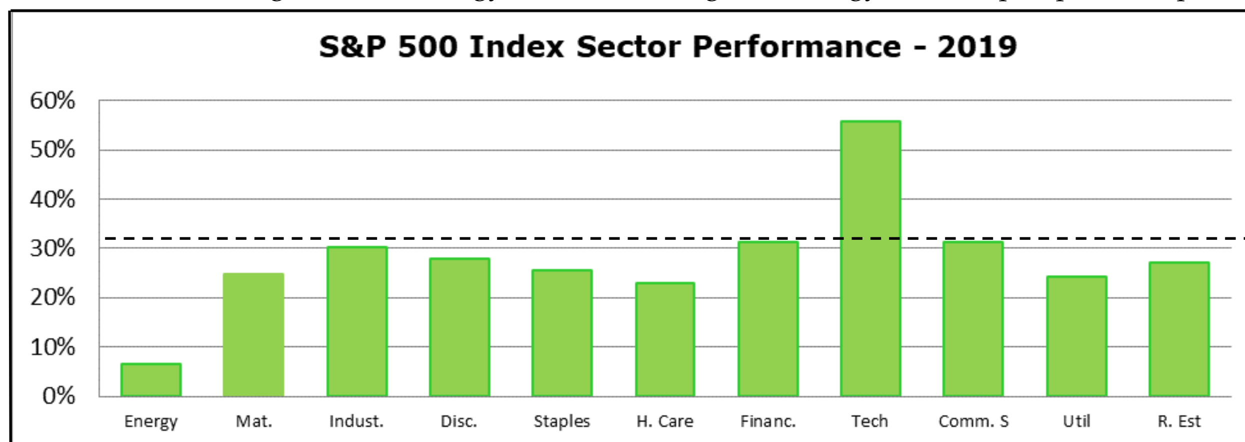
Equity Index Performance

Index	2019
S&P 500 (Domestic)	**31.49%**
MSCI EAFE (Foreign) *	**22.01%**
MSCI Emerging Markets	**18.42%**
MSCI EMU (European Monetary Union)	**23.20%**
MSCI Japan	**19.61%**

* Europe, Australia and the Far East

2. Technology Was The Star Performer

While all sectors were positive, only one sector out-performed the S&P 500 Index: Technology. The Tech out-performance was staggering. Energy was the significant laggard. Industrials, Financials and Communication Services were market performers. The other sectors lagged but not significantly. From a sector positioning standpoint, the key success factors in 2019 were decisions regarding Technology and Energy. For most of the year, we were neutral-weight in Technology and under-weight in Energy. This helped portfolio performance.



The SECURE Act Takes Effect Immediately And Will Affect Most Retirement Savers

The SECURE Act - which stands for "Setting Every Community Up for Retirement Enhancement" - was passed in late December as part of the government's spending bill. For better or worse, it will affect most retirement savers. Let's briefly look at the highlights of the bill and how you may be impacted.

1. The IRA Required Minimum Distribution (RMD) Age Has Been Raised From 70.5 To 72

Up until now, you had to start taking RMDs from tax-deferred retirement accounts (Regular IRAs and 401ks) the year you turned 70.5 years old. The age has been bumped up. For people turning 70.5 in 2020 and beyond, they will now have a higher required beginning age for their RMDs - 72 years old. The SECURE Act also allows for additional contributions to Traditional IRAs after age 70.5 (up until now, contributions could not be made upon reaching 70.5 years old).

STRATEGY CONSIDERATIONS

- Make further contributions to retirement accounts
- Delay IRA withdrawals until 72 years old
- Source income needs from taxable assets for a longer time frame
- Roth Conversions

2. Non-Spouse Inherited IRAs: Entire Proceeds Must Be Taken Within 10 Years

Up until now, if a non-spouse inherited an IRA, he/she could take his/her RMD based on his/her own life expectancy (he/she could "stretch" distributions and the resulting tax bills). This was a huge advantage to a young inheritor. Going forward, this is no longer the case. A non-spousal IRA account inheritor must take the entire proceeds from that account within 10 years of inheriting it.

STRATEGY CONSIDERATIONS

- Original Account Holder: Roth Conversions
- Non-Spouse Inheritor: Thoughtful 10-year withdrawal plan (consider income needs and taxes)

3. Employers Can Offer Annuities To Their Employees In 401k Plans With Total Immunity

Up until now, employers held the fiduciary responsibility to ensure that any annuity products offered for employees' portfolios were appropriate. Under the new rules, the onus falls on the insurance companies that sell the annuities. If employers want to offer annuities in plans, they now have a "safe harbor" that protects them from litigation if something happens with the insurance company offering the annuities.

This is a huge lobbying win for the insurance industry. We do not think this is a win for investors. Annuities are touted as a favorable replacement for bonds, a steady income for life, and an opportunity for tax-deferred growth. We disagree. An investor already has tax-deferred growth in a 401k/Regular IRA (there is no extra advantage to an annuity). Given their high commissions and fees, annuities may not out-perform bonds. An annuity won't offer a steady income for life if the provider has problems. Finally, most annuities have liquidity issues, high redemption costs, and poor legacy considerations.

STRATEGY CONSIDERATIONS FOR ANNUITIES IN 401ks: "Caveat Emptor" (Buyer Beware!)

Please contact us to discuss how the various measures of the SECURE Act may impact you.

Your Portfolio

We made several portfolio adjustments in 2019 to respond to changing market conditions. We plan to do the same in 2020. As your portfolio manager, we are not dealing with market certainty and we are always ready to adjust on the fly. In looking ahead, we are confident in the market and its underlying fundamentals.

In Q4, we made four portfolio adjustments. The rationale for these moves was to raise exposure to Financials and the evolving 5G network, as well as lower exposure to Consumer Staples and the turmoil in Hong Kong.

We bought Charles Schwab Corp (symbol: SCHW; $61 billion market cap), a leader in the brokerage, banking and asset management businesses. SCHW has over $3 trillion of client assets and derives nearly all revenues from the US. We know the company very well. SCHW has been our sole custodian since our inception.

We also bought Taiwan Semiconductor ADR (symbol: TSM; $300 billion market cap), the world's largest dedicated contract chip manufacturer (over 50% of global market share). A main reason we want exposure to TSM is because of its direct participation in the evolution of the 5G network (the next technology wave).

We sold Colgate Palmolive (symbol: CL; $57B market cap) due to its limited growth and our desire to reduce overall exposure to Staples. We also sold AIA Group (symbol: AAGIY; $113B market cap), the largest independent publicly listed pan-Asian life insurance group. Roughly 41% of its sales come from Hong Kong.

We will continue to closely monitor the market and adjust your portfolio as needed. Please feel free to contact us anytime to discuss questions or comments you may have. We will keep you informed of portfolio progress. Thank you for your continued confidence in TriVant.

Respectfully submitted,

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Disclaimer

The information presented herein is intended for informational purposes only. All views are subject to change based on updated indicators. The recommendations made in this publication are made without regard to individual suitability. Investors should consider their own needs and objectives before making any investment decision.

Commentary in this review reflects our portfolio strategy. Many of our clients have different objectives and circumstances which are reflected in unique portfolio considerations. Please note that accounts may not contain all elements of the strategy discussed here. Additionally, individual client customizations and start dates may preclude certain elements of this strategy from being implemented.

Past performance is no guarantee of future results. A risk of loss is involved with investments in stock markets.