The Compass

First Quarter 2020

Executive Summary

- Volatility continues, fueled by the Coronavirus.
- U.S./Mexico/Canada Agreement (USMCA) and the U.S./China Phase One trade agreement boost investor confidence.
- The Fed cut rates three times in 2019, bringing the Fed funds rate to the 1.50-1.75% level.
- Unemployment remains low at 3.5%. Inflation is at 2.1% for the 12 months ending November 2019. GDP was 2.1% for 3Q2019.
- The S&P 500 ended the year with a total return of 31.49%, its best since 2013.
- U.S. Treasury yields ended lower, but still look attractive when compared to negative interest rates seen globally in sovereign debt.

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- SECURE Act of 2019
- How Phishing E-Mails Work

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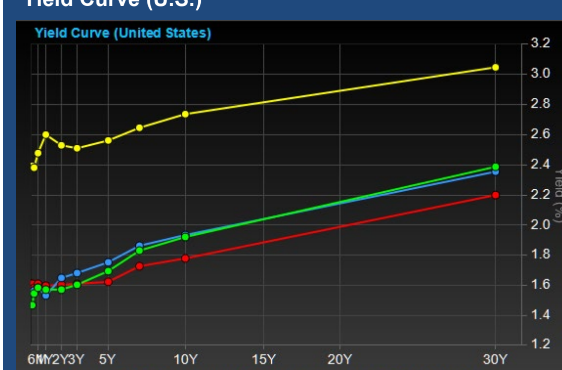
S&P 500 12 Month Price Chart

Source: FactSet 12/31/19

Yield Curve (U.S.)



Source: FactSet 12/31/19

U.S. Markets	12/31/19 Close	QTD % Change	1 Year % Change
Dow Jones Industrial Avg	28,538	6.02%	22.34%
S&P 500	3,231	8.53%	28.88%
NASDAQ	8,973	12.17%	35.23%
Russell 2000 (small caps)	1,668	9.52%	23.72%
Treasury Yields	**12/31/19**	**09/30/19**	**One Year Ago**
2 year	1.58%	1.63%	2.53%
10 year	1.92%	1.68%	2.74%
30 year	2.39%	2.12%	3.05%

Source: FactSet 12/31/19; U.S. Dept. of the Treasury.

Overview

There is an old investment saying that the markets like to climb a wall of worry. Based on the way the markets started 2019 and with all the concerns the markets faced throughout the year – I will worry a lot if the markets can repeat those returns. In previous editions we covered many different topics in the last year of the decade and it always seemed there was a new obstacle to hurdle. Regardless of those concerns the U.S. markets delivered returns that should have left all investors in a happy celebrating mood to ring in the New Year.

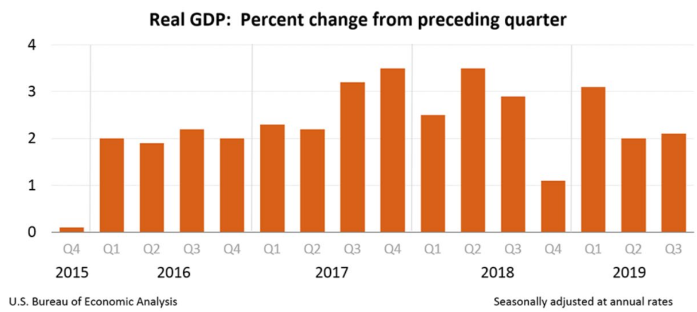
Past editions have discussed further volatility in the markets, which makes most investors unsettled. The markets were volatile, but in only an upward direction to close out the year. This is the type of volatility that most investors applauded. As the year progressed several other concerns were put behind investors, such as potential trade wars, as the U.S. and China agreed to a Phase 1 agreement, along with the signing of a trade agreement with our 2 border partners (U.S.-Mexico-Canada). This is all while others have subsided somewhat, but still have the potential of throwing a wrench in the continued recovery, both domestically and internationally. Some of these but not all consist of Brexit and the upcoming elections. There will always be new concerns that have effects outside our borders but the implications to our economy and markets are uncertain (Coronavirus).

While the new decade has started off on the right foot, the only perfect vision (20/20) is hindsight. Let us be the last ones to wish you a Happy New Year and a Joyous and Prosperous New Year.

Economic Backdrop

The Fed lowered rates by 25 basis points in October, its third rate cut in 2019, bringing the Federal funds rate to the 1.50%-1.75% level. Its October 2019 press release reiterated much of what was stated in its September 2019 release. The labor market remains strong and economic activity is growing at a moderate pace. The unemployment rate remains at an historic low of 3.5%, with job gains seen in retail trade and health care, while leisure and hospitality continued to trend up. Inflation is running near the Fed's 2% target rate, coming in at 2.1% for the 12 months ending November 2019; excluding food and energy the index came in at 2.3%. The food index rose 2.0% over this 12 month period, while the energy index declined -0.6%. Consumer spending has been rising at a strong pace, while business fixed investment and exports remain weak.

The third estimate for 3rd quarter 2019 Gross Domestic Product (GDP) came in at 2.1%, slightly above 2.0% reported for the 2nd quarter 2019. The increase was attributed to consumer spending, federal government spending, residential investment, exports, and state and local government spending, partly offset by negative contributions from nonresidential fixed income investment and private inventory investment, and an increase in imports. (Source: U.S. Bureau of Economic Analysis.)



Equities

It seemed to be relatively quiet progression though the year, but the 4th quarter finished 2019 with a bang. Pretty impressive to see many new highs being reached after a ho-hum previous 2 years. The S&P500 posted 26 all time closing price highs and finished the year up 31.49% when accounting for dividends. This was the best annual return since 2013. The NASDAQ also posted impressive gains with returns investors have not seen since 2009. As investors prepare for 4th quarter earning reports companies look to reverse the unimpressive 3Q19 earnings season. Earnings for the S&P500 were down for the quarter -0.4%. The negative print was led by Energy (-37.8%) and Materials (-11%), as the Comm Services and Technology sectors also reported negative earnings. The other 7 sectors reported positive earnings growth led by Healthcare (8.8%) and Utilities (6.7%).

Revenues did show positive growth for the quarter. Up some 3.8%, but down from last quarters 4.7% y/y growth. There were only 2 sectors that did not grow revenues, Energy (-8.2%) and Industrials (-1.7%). Healthcare +15.4% and Comm Services +9.8% were the 2 sectors that led to the positive report and offset the negative impact. As 4thQ19 reports start to trickle in investors and traders will pay more attention to the expectations looking forward, and less to the reports looking backwards. Additional commentary will be important around what investments they have planned for the upcoming and their confidence for expectations.

Fixed Income

The fixed income markets also participated in the positive direction for the year as rates have decreased from the lower 3% range in late 2018 to the closing rate of 1.92% for the U.S. 10 year Treasury. This is slightly higher than the 3Q close of 1.68%. This is as rates around the world have come down and many sovereign debts remain at negative levels. These low rates continue to be debated around the world by all involved as it has always been widely suspected that the bond market is "smarter" than the equity markets. Are these rates low as a forecaster of slower/no growth or are there other factors which are more structural in nature.

The U.S. economy continues to report numbers that are supportive of growth and no signs of recession. GDP at the latest report (4Q19) cam in at 2.1% and averaged 2.3% for 2019. The 3 month average for jobs added has been 214,000 and slight tick up in the unemployment number to 3.6%. This is a good sign as more citizens entered the "looking for a job" market. Average hourly earnings is also up more than 3% for the most recent report. The consumer also continues to be strong.

As real and relatively low, let alone negative, rates persist around the world, fixed income investors continue to face many headwinds. The main concern is how do investment advisors provide a fixed income at this time. We have seen 2 trends take place. First is that investors have plowed more funds in their fixed income allocation. This will have a direct impact on the growth side of the portfolio. The other is to take more risk. Both directional (length of bonds owned) or credit (riskiness of issuer). Either way this could be dangerous.

If the equity markets can be irrational, why can't the fixed income markets?

Outlook

The new decade has started off on solid footing, which is adding to the returns that were delivered to close out the last decade. Rates continue to be low around the world and supportive of prices and valuations. This along with the continued accommodation of monetary policy world pushing rates down leads to taking more risk in all asset classes despite tepid fundamentals. Continue to use your long-term asset allocation targets to guide your returns while managing your risk.

Always vigilant, our commitment to you is to navigate your portfolio through both calm and turbulent times in an effort to meet your goals and objectives.

The most important lesson in investing is humility. *- Sir John Templeton, 1912-2008*

Highlights from the SECURE Act

What is the SECURE Act? SECURE is an acronym for the Setting Every Community Up for Retirement Enhancement Act of 2019. This bill was passed in December 2019 with provisions to prevent older Americans from outliving their assets. It also makes it easier for small business owners to set up retirement plans for their employees that are less expensive and easier to administer. The following bullets are by no means all-inclusive, but provide some of the highlights of the bill:

- The Act changed the age for which a Required Minimum Distribution (RMD) is first required from age 70½ to age 72. This allows the value of retirement accounts to continue to grow tax-deferred for an additional year and a half. Note that the changes do not affect retirement plan owners who turned 70½ prior to January 1, 2020.
- As an increasing number of Americans continue to work beyond traditional retirement age, contributions to IRAs may be made by an individual indefinitely as long as there is earned income. There is no cap on the age for IRA contributions. Restrictions apply.
- The bill removes a provision known as a "Stretch IRA" that allowed non-spouses inheriting retirement accounts to "stretch" out disbursements over their lifetime. Under the new bill, full payout of the inherited IRA must be made within 10 years of the death of the original account holder. The new rules do not apply if the date of death was prior to January 1, 2020.
- Eligibility to participate in employer-sponsored retirement plans has been expanded to include part time workers, with certain requirements.
- The bill allows for penalty-free withdrawals from retirement plans for any "qualified birth or adoptions."
- Distribution rules for 529 education plans have been partially relaxed. Distributions can be made tax free for such things as qualified education loans and equipment related to the beneficiary's participation in an apprentice program, with restrictions.

This is a general summary of some of the highlights of the Act. Whether you are still working, approaching retirement, or already retired, we recommend you contact your tax professional to see how the bill may affect you.

Sources: www.IRS.gov; www.congress.gov; www.waysandmeans.house.gov.

Have a question about retirement accounts? Call 800-439-8745 or click https://www.cypresstrust.com/ for a free consultation.

How Phishing E-Mails Work

By Jim Parry, Vice President IT Services
Cypress Trust Company

Phishing is a method of trying to gather personal information using deceptive e-mails. The goal is to trick the email recipient into believing the message is something they want or need — for instance, an alert from their bank or a request from someone in their company — and to click a link or download an attachment. The attackers pretend to be a trusted entity of some kind, often a real or plausibly real person, or a company the victim might do business with.

There are a variety of techniques that fall under the umbrella of phishing. There are a couple of different ways to break attacks down into categories. One is by the *purpose* of the phishing attempt. Generally, a phishing campaign tries to get the victim to do one of two things:

Hand over sensitive information. These messages try to trick the user into revealing important data — often a username and password that the attacker can use to breach a system or account. The classic version of this scam involves sending out an email tailored to look like a message from a major bank; by spamming out the message to millions of people, the attackers ensure that at least some of the recipients will be customers of that bank. The victim clicks on a link in the message and is taken to a malicious site designed to resemble the bank's webpage, and then hopefully enters their username and password. The attacker can then access the victim's account.

Download malware. Like a lot of spam, these types of phishing emails aim to get the victim to infect their own computer with malware. Often the messages are "soft targeted" — they might be sent to an HR staffer with an attachment that purports to be a job seeker's resume, for instance. These attachments are often .zip files, or Microsoft Office documents with malicious embedded code. The most common form of malicious code is ransomware.

There are steps you can take that will help protect you from phishing e-mails, including:

- Always check the spelling of the URLs in email links before you click or enter sensitive information
- Watch out for redirects, where you're subtly sent to a different website with identical design
- If you receive an email from a source you know but it seems suspicious, contact that source with a new email, rather than just hitting reply

At Cypress Trust Company, protecting our clients' privacy is a top priority. We take precautions to protect your information and believe that such protection is vital to our business. We maintain physical, electronic, and procedural safeguards to store and secure client information to protect against unauthorized access. It is important for clients to implement similar precautions when using their personal computers. As part of our commitment to help you stay cyber-aware, look for tips and recommendations in each issue of The Compass newsletter which you can use to help keep your personal information safe.