MARKET Insights

Webster Private Bank®

October 2019

3rd Quarter Review

In our midyear review, entitled "*The Wall of Worry*" we wrote about the stock market's resilience in the face of geopolitical headwinds. During the third quarter, we saw this resilience tested multiple times, most notably in August. During August 11 of the 22 market trading days saw **1%** plus intra-day moves with 3 of those days seeing declines of over **2.6%**. Tariff headlines and recession fears were largely to blame, as President Trump tweeted an additional **10%** tariff on $300 billion in Chinese imports which went into effect September 1st. China responded by halting purchases of US agricultural products and allowed the yuan to decline to the lowest level since 2008.

September brought some recovery and stabilization for US Large Cap stocks, resulting in third quarter results for the S&P 500 leading major equity markets with a **1.7%** return and pushing year-to-date returns up to **20.55%**. All other major equity markets posted negative returns, with US small cap stocks finishing down **-2.4%**, while developed international markets and emerging markets declined **-1.07%** and **-4.25%** respectively.

Asset Class Returns			Q3 2019	YTD 2019
Equities	US Large Cap	S&P 500 TR USD	1.70%	20.55%
	US Small Cap	Russell 2000 TR USD	-2.40%	14.18%
	International Developed	MSCI EAFE NR USD	-1.07%	12.80%
	Emerging Markets	MSCI EM NR USD	-4.25%	5.89%
Fixed Income	US Investment Grade Bonds	BBgBarc US Agg Bond TR USD	2.27%	8.52%
	US Inflation-linked	BBgBarc US Treasury US TIPS TR USD	1.35%	7.58%
	High Yield Bonds	BBgBarc US Corporate High Yield TR USD	1.33%	11.41%
Alternatives	Market Neutral	Credit Suisse Equity Market Neutral USD	-0.17%	1.60%
	REITs	MSI US REIT Diversified	7.38%	25.71%
	Commodities	Bloomberg Commodity US TRD	-1.84%	3.13%

Source: FactSet Indexes, total returns in USD as of September 30, 2019. US Large Cap is S&P 500 index, US Small Cap is Russell 200 index, Intl Developed is MSCI EAFE index, Emerging Markets is MSCI EM index, Investment Grade is Barclays US Aggregate index, High Yield is Barclays Corporate US High Yield index, Absolute Return is Credit Suisse Equity Market Neutral index (through August 31, 2019), Commodities is S&P GSCI index, REITs is MSCI US REIT Diversified index.

As we turn the calendar to October, the geopolitical climate is once again heating up, with the newest headline out of Washington being the prospect of impeachment of President Trump which joins the ongoing US/China tariff saga, continued Brexit drama in the UK, and possibility of increased tariffs on European imports.

MARKET Insights

2019 Investment Themes – An Update

With three quarters of the year behind us, we review below the investment themes that we laid out at the beginning of the year, along with the current positioning of portfolios.

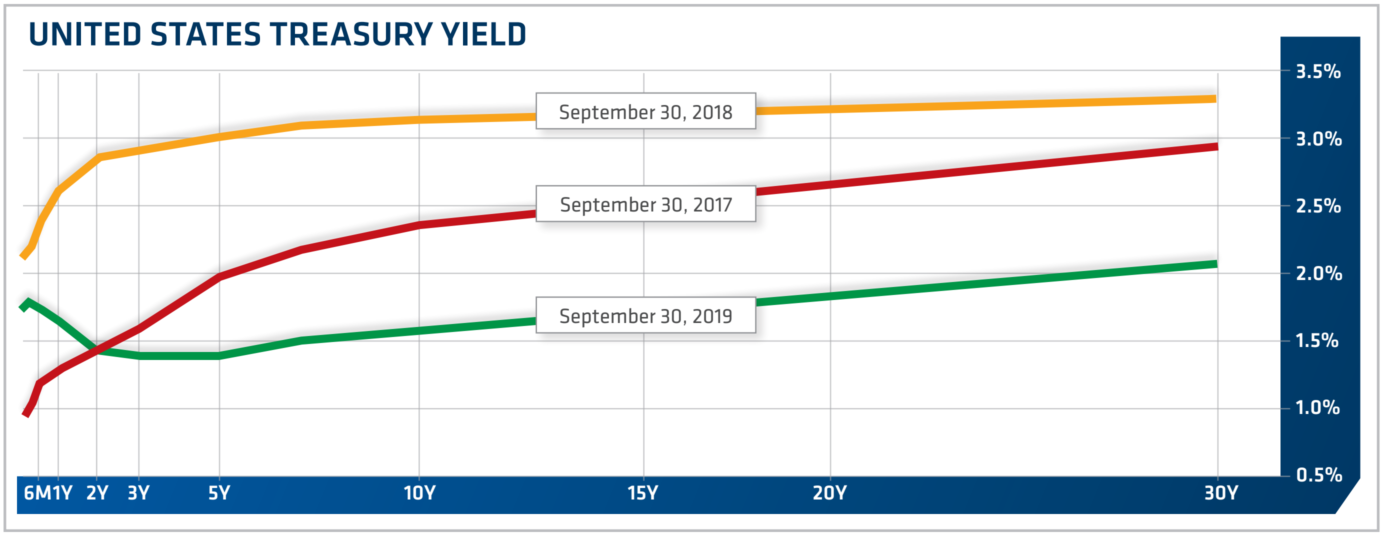
1 *The Path of Interest Rates is Changing*

With the 10-year treasury yield hitting **1.50%** in August, the path has indeed changed. After rising from **1.36%** in 2016 to a high of **3.2%** in October 2018, the 10-year has plummeted in 2019, resulting in eye-popping returns for bonds, with the Barclays Aggregate Bond Index up **8.52%** thus far in 2019. Beginning in 2018, we shortened maturities in anticipation of higher rates, opting to focus on credit risk to deliver attractive yields. As a result, the "price return" on our bond portfolio appreciated less than the aggregate bond market. While our conservative fixed income positioning has cost us in relative price return, our portfolio outyields the broad bond market. With an expectation of a gradually steepening yield curve, we believe we are appropriately positioned to minimize the negative price returns associated with rising interest rates while earning attractive yields on client portfolios.

2 *Volatility is Here to Stay*

As stated earlier, August saw volatility increase dramatically, with 11 of 22 trading days experiencing intra-day price swings exceeding **1%**. With no end in sight for geopolitical turmoil, volatility is sure to remain elevated. However, we do not see recession within the next 6 – 9 months, and the US continues to experience slow and steady GDP growth with low inflation. Over the last 25 years, the S&P 500 has gained an average of **+4.3%** in the fourth quarter, with 19 of 25 producing a positive result. As a result of this outlook, we have selectively added to equities on weakness, and are currently maintaining a modest overweight to US equities at the expense of international equities.

The chart below shows the yield curve at three points in time. The red line is the Treasury yield curve in 2017, yellow is 2018 and green is current (September 30, 2019). Rates rose substantially between 2017 and 2018, and then dramatically dropped between 2018 and present.

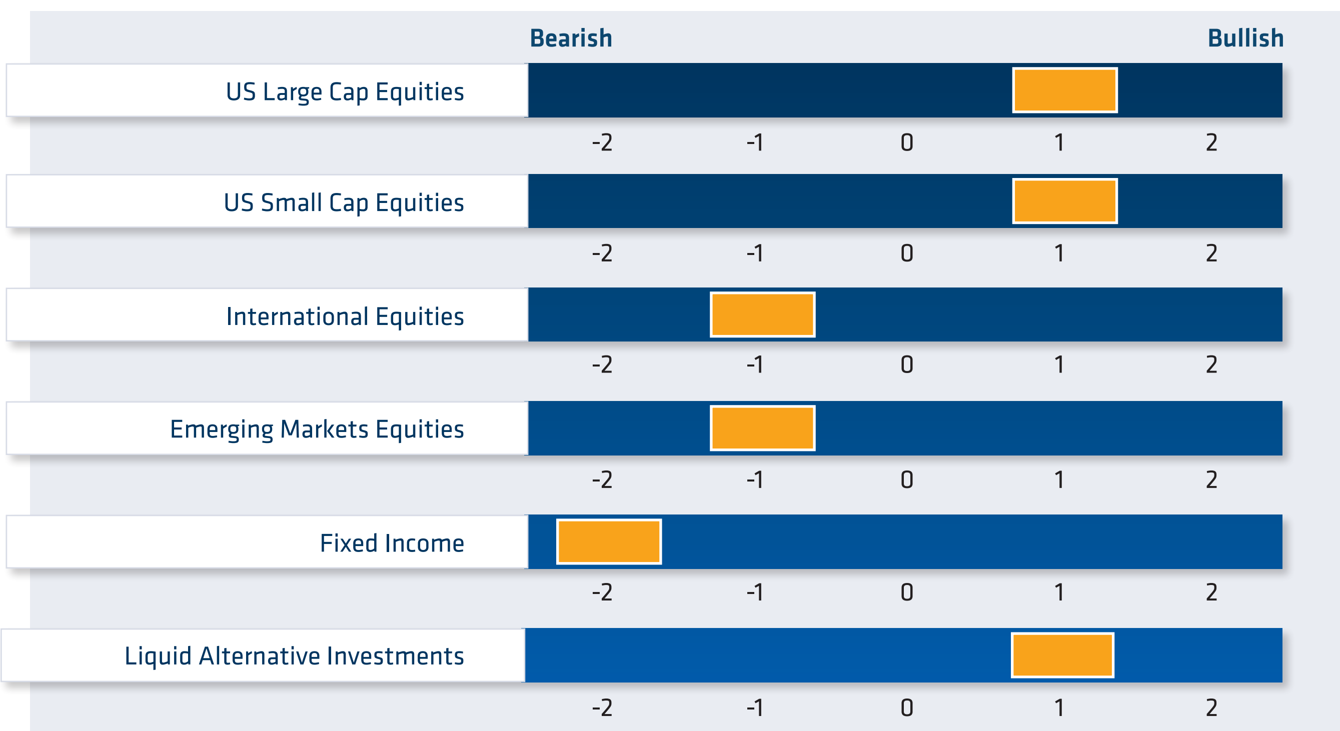


3 Earnings Growth Becomes More Difficult

At the start of the year, earnings forecasts called for substantial declines in year-over-year revenue and earnings for the first half. As compared to 2018, where we witnessed double digit earnings growth, earnings have slowed substantially, but actual Q1 and Q2 results have come in better than expected and ahead of consensus. FactSet's estimated earnings decline for the third quarter is **-3.8%**. If this proves to be true, it will mark the first time the index has reported three straight year-over-year earnings declines since Q4 2015 through Q2 2016.

> "the US continues to experience slow and steady GDP growth with low inflation"

BEARISH VS. BULLISH



MARKET Insights

Summary

With the tea leaves looking a bit murkier at present, we are content to focus on high quality US equities in a diversified portfolio with a slight underweight to international markets. Overall GDP growth outside of the US continues to trend at anemic rates, and without a catalyst for growth we do not foresee adding to foreign markets in the near term.

The US economy continues to chug along with slow and steady GDP growth, low inflation, and full employment. While the situation in Washington DC may be taking all of the headlines at present, the longer-term economic outlook continues to look positive. We will continue to manage accounts prudently, taking advantage of short-term declines and balancing risk and reward accordingly.

As always, we welcome your comments, insights and concerns. Please contact your Webster Private Bank Portfolio Manager at any time for a discussion about your personal investment portfolio.

TO VIEW A MORE DETAILED DESCRIPTION AND ANALYSIS OF THESE INSIGHTS, VISIT WWW.WEBSTERBANK.COM/PB

We hope you've found this commentary helpful. When you're ready to put these insights into action, visit www.WebsterBank.com/pb, contact your Webster Private Bank Portfolio Manager, or email us at pbinfo@websterbank.com.

Webster Private Bank®