KALORAMA Wealth Strategies
A Beautiful View To Your Financial Future℠

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Fourth-Quarter 2019 Market Review ~ On the Rebound

January 2020 - New year, new format:

- Both stocks and bonds advanced across the board in 2019.
- Domestic stocks had their best year since 2013.
- But 2019 was more of a rebound year from a severe December 2018 sell-off.
- Interest rate shifts largely drove market sentiment and returns.
- Read on for more details:

Stocks and bonds rallied across the board in 2019, with all major equity asset classes posting double-digit returns. Although investors contended with trade tensions, recession concerns, and political drama, as measured by the Standard & Poor's 500-stock index, it was the best year for domestic stocks since 2013.

However, some perspective is necessary, as the S&P 500 finished 2019 only about 10% above 2018′s peak, which is close to the average return of 9.8% for the S&P 500 over 90 years. A steep sell-off in December 2018 left the S&P 500 near bear market territory (defined as a drop of 20% or more from a recent high) after the Federal Reserve raised interest rates four times in 2018, including a December hike that took its key rate to a range of 2.25% to 2.50%.

Stocks started 2019 rebounding from the December 2018 slide, advanced further in the second quarter, mostly paused in the third quarter, and leapt ahead in the final quarter. For the fourth quarter, the Dow Jones Industrial average rose 6.0%, the S&P 500 (total return) climbed 9.1%, and the NASDAQ Composite index swelled 13.5%.

As the closing bell rang for 2019, the Dow Jones had jumped 22.3%, the S&P 500 (total return) vaulted 31.5%, and the NASDAQ surged 35.2%. International stocks also generated double-digit gains, with developed large caps expanding 22.7%, developed small caps soaring 25.5%, and emerging markets picking up 18.9%.

Declining interest rates in 2019 led to universal gains for bonds. All broad bond sectors had mid to high single-digit returns, while U.S. Corporate High Yield and International Emerging Markets stepped up 14.3% and 13.1%, respectively.

Interest rates sank in the third quarter after central banks unexpectedly cut rates and trade deliberations continued to simmer. Yields on long-term U.S. Treasuries tumbled by more than one-half percent (50 basis points). The 10-year U.S. Treasury note slipped below 1.50% to levels not seen since 2016, while the 30-year U.S. Treasury bond fell below 2.0% for the first time ever.

When the Treasury yield curve slightly inverted at the end of the first quarter, investors began to speculate that an economic recession may be on the horizon. (The yield curve is the relationship between short-term and long-term interest rates, usually measured by comparing the yield for three-month U.S. Treasury Bills with 10-year Treasury Notes. Normally, long rates are higher than short-term rates due to the risk of loaning money for longer periods. The exception is an "inverted" curve, when short-term rates are higher than long-term rates.) An inverted yield curve has been highly predictive of recessions. It has correctly signaled all nine recessions since 1955, with only one false positive in the 1960s (the inversion was followed by an economic slowdown, but not a recession). It was the first time the yield curve inverted since 2007.

Interest rates somewhat normalized for the first half of the second quarter, but then turned and remained inverted through the beginning of the fourth quarter. Short term rates finally dropped after the Federal Reserve cut interest rates by a quarter percent twice during the third quarter and once during the fourth quarter, resulting in a range for the federal funds rate of 1.50% to 1.75%. It was the central bank's first reduction in rates since 2008 when the Fed moved to near zero during the financial crisis. The Fed expects to remain neutral for 2020.
At year end, the yield on the three-month Treasury bill was 1.56%, plummeting 90 basis points for 2019. The 10-year U.S. Treasury note closed at 1.92%, sinking 76 basis points, while the 30-year Treasury bond finished at 2.39%, shedding 63 basis points for the for the same period.

Below are rates of return for selected market indices for the fourth quarter of 2019, full-year 2019, and the three, five, and 10-year compound annual returns as of December 31, 2019.

Equity (Stock) Indices	**4Q:2019**	**2019**	**3-Year**	**5-Year**	**10-Year**
Domestic					
Russell 1000 - Large Cap	9.04%	31.43%	15.05%	11.48%	13.54%
Russell Midcap	7.06%	30.54%	12.06%	9.33%	13.19%
Russell 2000 - Small Cap	9.94%	25.52%	8.59%	8.23%	11.83%
Real Estate (FTSE NAREIT Equity REITs)	-0.76%	26.00%	8.14%	7.21%	11.94%
Commodity (Dow Jones Commodity Index)	5.22%	10.12%	1.54%	-2.40%	-2.88%
International					
MSCI EAFE Developed Large Cap	8.21%	22.66%	10.11%	6.18%	6.00%
MSCI EAFE Developed Small Cap	11.56%	25.47%	11.35%	9.25%	9.12%
MSCI Emerging Markets	11.93%	18.88%	11.99%	6.01%	4.04%
Global - MSCI All Country IMI	9.16%	27.04%	12.68%	8.92%	9.47%
Fixed-Income (Bond) Indices					
Bloomberg Barclays					
Global Aggregate - Unhedged	0.49%	6.84%	4.27%	2.31%	2.73%
Global Aggregate - Hedged	-0.49%	8.22%	4.30%	3.57%	NA
U.S. Aggregate	0.18%	8.72%	4.03%	3.05%	3.75%
U.S. Treasury TIPs	0.79%	8.43%	3.32%	2.62%	4.09%
U.S. Corporate High Yield	2.61%	14.32%	6.37%	6.13%	7.18%
Municipal	0.74%	7.54%	4.72%	3.53%	4.65%
International Emerging Markets	2.09%	13.11%	6.07%	5.84%	7.20%

Source: ftserussell.com, reit.com, us.spindices.com, msci.com, bloomberg.com