



VIEWPOINTS

4TH QUARTER 2019

ADVISORY NEWSLETTER

MARKET COMMENTARY

FREDRIC W. WILLIAMS

Why Two, Kaye?...

Not only did the most recent New Year's Eve usher in the passing of 2019, but it also marked the end of a decade, the first score of the 21st century, and the twentieth anniversary of the millennium – which gave us the angst-ridden build up to the end of 1999, eponymously referred to as Y2K. One can recall the dire warnings surrounding the concern about how computer script might misinterpret the step from 1999 to 2000 as being instead to 1900 (given the coding convention of just noting the last two numbers in a given year), and thereby impacting everything from electrical power grids, to airline and other transportation systems, along with the more mundane calculation of bank interest, and rates, on loans and savings. Fortunately, there was very little disruption, and somewhat surprisingly, the simplest of solutions worked the best: the date covenant was merely expanded from two digits to four...as my oldest grandson frequently says to me: “Duh, Grampy!”

In an ever more complex world where techno-this and robo-that have become the proxies for measuring society's progress, sometimes simplicity is that old-school approach that provides the most effective path through the clutter. And although it's important to embrace the leading-edge and the opportunities it may provide going forward, we shouldn't lose sight of the lagging-edge, and its attributes, merely because of the appearance of a “shiny new toy”. The investment world, for example, is replete with smart people espousing the virtues of algorithms, correlation analysis and momentum strategies (all of which can be helpful at times), but it was an “antiquated” strategy that won the race during the last decade.

The admittedly unglamorous Dogs of the Dow, which focuses on relative dividend yields, beat both the Dow and the S&P 500 over the ten years that ended in December.

“The Dogs of the Dow simply calls for buying the 10 highest-yielding stocks in the Dow 30 at the beginning of each year. It is a contrarian strategy. It favors the beaten-up stocks of companies that may have issues such as new competition or declining demand. To have a high yield means a stock has a low price relative to the dividend paid.”

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"It shouldn't be this easy to beat the broader index with a simple investing strategy, but it is – or at least it was over the past decade."

- Ben Levisohn, Barron's 1/6/2020

Having considered iterations of this concept over the years (OPA incorporates the inclusion of P/E ratios as an additional metric) we find that "The Dogs" also offers some basic investment disciplines that can cut through the cacophony of what spews forth from the financial media's talking-heads on a daily basis:

- ✓ **Buy low** – rather than chasing momentum stocks, these shares tend to be lower priced, on a relative basis, which is what creates their higher dividend yield
- ✓ **Buy value** – often times these shares are from companies facing headwinds that may be temporary, so the relatively lower share price could be temporary as well
- ✓ **Buy cash flow** – these "critters" pay dividends that can be twice what the overall index is paying – an attribute OPA has favored since the '90s.

With the globe continuing to be embroiled in trade disputes, regional geo-political tensions and a relatively subdued economy that even low, and sometimes negative, interest rates can't seem to stimulate, this focus on investment income is always a timely approach for long term investors.

"The other part of the Dogs strategy is a recognition that dividends are important. Over the past decade, dividends contributed, very roughly, 20% of the total return earned by the Dogs. That percentage, of course, is much higher in years like 2015 and 2017, when total gains were small or non-existent."

"It is possible to view history in a lot of different ways. The stock market is one of those lenses. Looking for stocks with the highest dividend yields tells a story of what industries are falling out of favor and what issues investors see as worrisome for coming years."

"Sometimes investors overreact to the day's news, which is another reason these dogs run."

- Ben Levisohn, Barron's 1/6/2020

Considering these types of more mundane investment guidelines may be the prudent thing to do given where the domestic equity markets have come over the last year.

The run up from the holiday-2018 lows has the S&P 500 trading at over 18 times forward earnings, has the options speculation index with 30% more bullish than bearish trades, and shows the CNN Fear & Greed index going from last December's "Fear" reading of 31, to a recent "Extreme Greed" peak of 97. All of which suggests that the indices are priced to perfection and are offering investors little cushion should something come up not quite so rosy.

OPA will continue to look for risk-adjusted opportunities in all asset classes, both domestically and overseas, that resemble the Dogs income-oriented criteria, while still offering attractive valuations.

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CAPITAL MARKETS OVERVIEW

Index Returns			
Equities	Percentage Change for the 4 th Quarter	Percentage Change for the Year	Annualized 10-Year Returns
S&P 500	9.07%	31.49%	13.56%
Bloomberg Commodity Index	4.42%	7.69%	-4.73%
MSCI EAFE*	8.17%	22.01%	5.50%
MSCI Emerging Markets*	11.84%	18.42%	3.68%
FTSE NAREIT Equity REIT Index	-0.76%	26.00%	11.94%
Fixed Income			
Bloomberg Barclays U.S. Aggregate Bond	0.18%	8.72%	3.75%
Bloomberg Barclays U.S. Treasury Inflation-Linked Bond	0.79%	8.43%	3.36%
Source: BlackRock, Bloomberg, FTSE™, NAREIT®. *Returns are calculated with net dividends in USD Index returns are for illustrative purposes only and do not represent actual performance of any investment. Index performance returns do not reflect any management fees, transaction costs or expenses. Indexes are unmanaged and one cannot invest directly in an index. Past performance does not guarantee future results.			

Domestic and Global Market Recap...

FRANCIS J. DAVIES, III

The financial markets ended 2019 on a high note. It was a great year to be invested as stocks charged upwards and fixed income also provided substantial total returns. Markets were reassured as geopolitical risks faded (before the current Mid-East actions), optimism about the economy rose following potential trade developments and, most importantly, central banks continued to support economic activity. For context, 2019 saw the largest amount of central bank easing since 2008, a time of global economic catastrophe. The easy money allowed investors to move funds into riskier investments.

In the US, the S&P 500 rose 9% in Q4 to finish with a 31.5% gain for the year. Investors' appetite for risk was shown by continuing preference for growth stocks over value, and the outperformance of both smaller cap stocks and emerging market equities. Microcap growth stocks gained 13.5% and small-cap growth rose 11.4% while emerging markets grew 12%, outpacing the US for the first time all year. Technology was again the leader in 2019, returning 48% despite increasing concerns about the global influence wielded by the huge tech leaders.

The Federal Reserve cut rates once in the quarter, steepening the US Treasury Yield Curve and correcting its inversion. With the curve no longer inverted, fears of recession were diminished for the time being. Government bonds responded to the weaker economic data, with bond yields broadly following the manufacturing surveys lower. The 10-year Treasury yield ended the year at 1.92% with the latest figures showing the US economy expanding at slightly better than 2% annual rate. There was also demand for riskier investments in the

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fixed income markets as junk had its best year since 2016. High yield corporates, emerging market debt, and leveraged loans all outperformed investment grade paper in Q4.

The improved global economic data and advancement in trade negotiations sparked a rally in international equities. The Eurozone had a strong quarter with Germany producing better than expected economic data. The Euro Stoxx 50 returned 27% in dollar terms, the most since 2013. London's FTSE 100 added 17% in local currency and 22% in dollar terms. Japanese stocks gained 8.6% for the quarter. Tech heavy Taiwan gained almost 18%, while India rose just 5% as the country faced economic and political turmoil. As mentioned above, emerging markets did well with oil dependent Russia and Columbia having particularly strong quarters. Emerging market bonds also had solid returns.

The Bloomberg commodities index zigzagged to a 5.4% gain in 2019. Crude oil prices saw the biggest rise in three years, gaining 34%, and they rallied early in 2020 as U.S.-Iran tensions flared. The dollar index ended December little changed from where it started 2019. Precious metals were out of favor in the risk on environment, gold up 3.3% and silver 5%. Less than robust growth held down the price of industrial metals.

A new research paper from Yale professor Paul Schmelzing throws new light on the issue of low and negative interest rates. He examined real interest rates in developed markets for the last 600 years. Despite the belief that negative rates are temporary aberrations, his work shows they have always been around. The data shows a definitive downtrend in rates, falling roughly 1% every 60 years to near zero today. The study indicates that developed economies should experience negative real rates about a quarter of the time during the next few decades. A new wrinkle in valuing future cash flows.

Sector Highlights...

RICHARD "CHIP" HARLOW

After a rather flat 3rd quarter, the 4th quarter resumed the march higher, with positive trade news helping. The S&P500 rose 9.1% during the most recent quarter and once again gave us a Santa Claus rally. On the year, the S&P 500 rose 31.5% with the Technology sector leading the way, up a whopping 50.3%. All sectors finished the year in positive territory with Energy picking up the rear at 11.8%

Technology

The tech sector regained its leadership position during the 4th quarter, tying Healthcare with a 14.4% return for the quarter. Favorable news on trade negotiations helped. 2019 was also the best year for Technology stocks since 2009. Semiconductors helped lead the way but other big players like Apple and Microsoft also helped. While technology valuations may be stretched, there are positive fundamentals that are behind technology's strong upward trend. A key to watch in the coming year is how the fight for technological dominance will play out between the US and China.

Health Care

Healthcare was up 14.4% during the 4th quarter and ended the year up 20.8%. Health care has risen on solid fundamentals, but concern over potential changes in US healthcare laws and policies, due to upcoming presidential election, has put a dampener on the sector. Health care

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is considered a “late-cycle” sector, where economic growth rates start to slow, and as such could be a reason for the in-flows and performance.

Financials

Financials were the third best performing sector during both the 4th quarter as well as for the year. Financials were up 10.5% for the 4th quarter and 32.1% for the year. While the sector was held up in the beginning of the year, domestic economic growth along with continued clarity with Brexit, the trade deal with China, and Fed monetary policy allowed the sector to end the year strong. Further, the recent phase-one U.S.-China agreement and the Fed’s announcement of no change in interest rates and a pause, following three interest-rate cuts this past year, have revived optimism in the sector.

Real Estate

Real Estate was the worst performing sector during the 4th quarter, giving back -.5%. Interest rates stabilized during the 4th quarter and so along with some profit taking, the sector took a breather. Real Estate ended the year up 29.0%, close to the middle of the sectors in terms of 2019 performance.

FIDUCIARY CORNER

STEPHEN L. EDDY

2020 Regulatory Limits for Retirement Plans

In October 2019 the IRS announced cost-of-living adjustments affecting dollar limitations for retirement plans in 2020. Most limits for 2020 will change because the increase in the cost-of-living index hit the statutory thresholds that would trigger Cost-Of-Living-Adjustments (COLA). These adjustments, if any, are typically in \$500 increments for contribution limits and \$5,000 increments for compensation limits. Below is a chart of some of the more important plan limitations.

Important Limits	2020	2019	2018	Notes
402(g) Deferral Limit <i>(401k, 403b, & most 457 plan elective deferrals)</i>	\$19,500	\$19,000	\$18,500	The maximum amount a participant can annually contribute through salary deferral.
Salary Deferral Plan Catch-up Contribution <i>(401k, 403b, & most 457 plan elective deferrals)</i>	\$6,500	\$6,000	\$6,000	The maximum amount a participant 50 and older can <u>additionally</u> contribute through salary deferral each year.
IRA Deduction Limit <i>(add \$1,000 catch-up contribution if you're over 50)</i>	\$6,000	\$6,000	\$5,500	The maximum amount a participant can annually contribute to an Individual Retirement Account.
Annual Compensation Limit	\$285,000	\$280,000	\$275,000	The maximum amount of compensation allowed for contribution calculation purposes.
Highly Compensated Employee	\$130,000	\$125,000	\$120,000	The compensation threshold at which an employee becomes defined as highly compensated. Important salary deferral and contribution allocation testing.
Limit on Annual Additions: Defined Contribution Plan	\$57,000	\$56,000	\$55,000	The maximum annual amount allowed to be contributed for an employee from all contribution sources (employee, employer).

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Social Security Wage Base	\$137,700	\$132,900	\$128,700	The maximum earnings level allowed to be taxed under the OASDI program. Important for calculations integrated with social security.
Key Employee Officer Comp	\$185,000	\$180,000	\$175,000	The compensation threshold at which an employee can be considered a potential "key" employee. Important for "top-heavy" calculations.

OPA NEWS & COMMUNITY EVENTS

OPA OUT & ABOUT:

The start of a new year is when a variety of non-profit organizations further their annual fundraising efforts so they can continue to enhance the fabric of our community. Although by no means complete, the events below are but a sampling of the organizations that our firm, employees, colleagues and clients are involved with, should you want to consider supporting their missions.

UPCOMING EVENTS

PORTLAND HARBOR HOTEL'S ICE BAR BENEFIT – This annual event, running this year from January 23rd to 25th, features ice carvings and an outdoor venue, and provides funds for area non-profits. Additional information, and tickets, can be found at <http://www.portlandharborhotel.com/portland-harbor-hotel-ice-bar.php>

CENTER FOR GRIEVING CHILDREN'S LOVE REALLY COUNTS – Their annual benefit auction and dinner gala will be at Brick South on Thompson's Point, Friday February 7th. Tickets and more information can be found at <https://www.cgcmaine.org/event/2020-love-really-counts-auction-and-dinner-gala/>.

MAINE PRESERVATION'S 9TH ANNUAL GALA – This year's gathering will be held Wednesday March 5th at The Portland Club, 156 State Street – additional information and tickets can be found at <https://www.maine Preservation.org/gala>

AMERICAN HEART ASSOCIATION'S GO RED LUNCHEON – Will be held March 19th at Holiday Inn By the Bay, and will raise funds for the battle against cardiovascular disease and stroke. Additional information can be found at <https://ahascarborough.ejoinme.org/MyEvents/20182019MaineGoRedForWomen/tabid/982189/Default.aspx>

THE TELLING ROOM'S 3RD ANNUAL SHOW & TELL: A LITERARY SPECTACULAR – This year's performance will again be at The State Theater on April 7th and the show will celebrate the power of writing and storytelling. Additional information and tickets can be found at <http://showandtellportland.com/>

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Lastly, a thank you to all who were able to attend our *Gather Together* 25th anniversary event on December 11th at The Portland Country Club. It was great to see the ballrooms filled with clients, colleagues and friends – and to celebrate all that we’ve been through together over the last two and a half decades.

Jeff Kleintop’s presentation on the globe’s economic issues and opportunities going forward was very insightful, and it was nice to highlight the various OPA Team members in the video that Kast Branding produced. Thank you all for the feedback and support – we will be doing events similar to this going forward.

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