Hughes Investment Advisory Service LLC

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Dear Clients and Investors,

Happy New Year and welcome to the new decade! US stocks closed out trading in 2019 on a very positive note – the complete opposite from 1 year ago when the markets ended the year in a 20% downside route. At this time last year, it was a black hole of selling created by fears of Federal Reserve interest rate hikes boosted by the lack of liquidity that sometimes accompanies end-of-year trading. What a difference a year makes. For those of us keeping score, the S&P 500 was up + 10% in the 4th quarter and gained 28.9% for 2019. It wasn't an easy year despite the final results. After a ripping rally that saw the S&P 500 gain 18% during the first four months of 2019, the market ran into a wall of worries that included an inverted yield curve,, an earnings recession, the Trade War and of course Impeachment, or whatever that was, of President Trump. Essentially, all the gains occurred in the first and last quarters of the year while the middle 6 months were flat to negative.

Each year at this time I like to reflect back on last year's predictions to see how they turned out.

Where was I correct in 2019?

- The S&P rose strongly, up %28.9 - higher than my optimistic prediction of %16 but clearly in the right direction.
- Consumer confidence remained strong ending at a reading of 126 as predicted.
- Oil prices ended the year around $62.00 close to the $60.00 predicted.
- Corporate profits did rise to a new record with S&P 500 earnings at $164.00 though not quite the $170 predicted.
- GDP Growth looks like it will finish the year at approximately 2.37% below 2.87% predicted.

Where was I off the mark in 2019?

- Unemployment rate dipped to 3.7% below the 4.3% predicted.
- Interest rates dropped with the 10-year T-Note ending the year at 1.92% The Fed cut the Fed Funds rate 3 times in 2019 to 1.25-1.50%
- Inflation remained subdued ending the year at 2.1% below the 2.5% predicted.
- The US dollar did strengthen but not as much as predicted versus the Euro ending at .90 versus the .95 predicted.

The good news about my incorrect predictions is that although four were slightly off the mark, they could all be construed as generally market positive – so we will take it!

Last year there were two big calls that an investor needed to get right. First was to dismiss signals of an impending recession and stay long stocks. Second, was to recognize that the Federal Reserve had accepted the signals of slowing growth and that it's sudden reversal at the start of 2019 meant that it had become significantly more dovish. We did stay invested, buying the dip in Q4 2018 and also recognized the Fed's dovish turn, remaining cautiously invested throughout 2019 participating in the

rally. All this said, it was pretty hard to lose money in 2019 unless you were sitting in cash, bitcoin or short the market. The 10-Year Treasury was up almost 10%, gold up 15%, crude oil up 34%. The equity market favored our corner of the market with value and dividend focused stocks like United Tech, JP Morgan and Coke performing well as did our tech plays like Apple, Microsoft and Google.

One sign of over exuberance and a "bubble" occurred in the IPO market. My deep-rooted skepticism about IPO's in general and expensive "unicorn" stocks in particular proved right and the year terrible for UBER, Lyft and the deservedly failed IPO of WeWork. I consider these money-losing, hyped companies to be a threat to equity markets. I just don't buy the idea that revenues matter more than profits – that model seems to have worked for Amazon and may work for Netflix but I'm generally skeptical of the market share/revenue only focused companies currently being hyped by certain corners of Wall Street.

So where are we today as we head into the new decade? The yield curve is no longer inverted and negative yielding global bond totals are currently shrinking. Trade tensions are abating with USMCA finally passed, China Phase 1 Trade deal ready for signing on 1/15/20 and a finalized Brexit vote completed. These three trade related problems are all moving solidly forward and removes most of the Macro headwinds experienced during the last two years. Additionally, the Federal Reserve remains market friendly with the Fed currently on hold until excessive signs of inflation appear in the economy. S&P 500 earnings appear headed 10% higher to $179.00 in 2020. For the year ahead I must say that my concern is that my economic and market outlook is currently in the consensus. This is not where I usually stand and the consensus is usually wrong so as always, being flexible, watching the economic statistics, political developments and market signs will be the plan in 2020. What is the consensus? The economy will be fine, bond yields will rise, and US stocks will deliver unspectacular but positive returns.

What am I looking at that could go wrong for the economy and markets? As always it's usually the unexpected that causes the greatest harm but on my radar would be the US Election, War and on the longer term big picture front – excessive corporate and Government debt as it relates to quantitative easing and current ultra-low interest rates in view of the enormous future obligations for Medicare, Social Security and other unfunded government obligations both here and around the globe – admittedly the debt problems could still be years or decades in the future but also potentially close ahead. Enormous debt service requires low interest rates. Lastly, the S&P 500 is now currently expensive or fairly priced based on earnings projections which means we will need better than expected earnings growth or additional P/E multiple expansion for any outsized gains, neither of which I currently expect.

Some predictions for 2020:

- The S&P 500 will rise 6%. GDP Growth of 2.5% Unemployment rises to 4.0% as discouraged workers continue to re-enter the workforce.
- Interest rates will rise – 10-year T- note averages 2.25%.
- Consumer Confidence softens, 125 now.
- Inflation moves higher but stays muted at 2.5%
- Oil prices remain stable and average around $55 for the year.
- Dollar remains strong relative to most currencies, and strengthens versus Euro to .95
- Corporate profits hit another record high - S&P 500 earnings at $180 up 10%

At this time, I continue to favor large-cap, dividend paying, US based multi-national companies with strong balance sheets. We love businesses with irreplaceable brand names, high barriers to entry, wide margins, grow their dividends and have modest debt. Emerging markets in general are inexpensive and we will be looking for good entry points. Risk/reward continues to favor equities over fixed income. Select MLP's, REIT's and specialized bond and income funds continue to look good as income producers.

Sincerely,

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