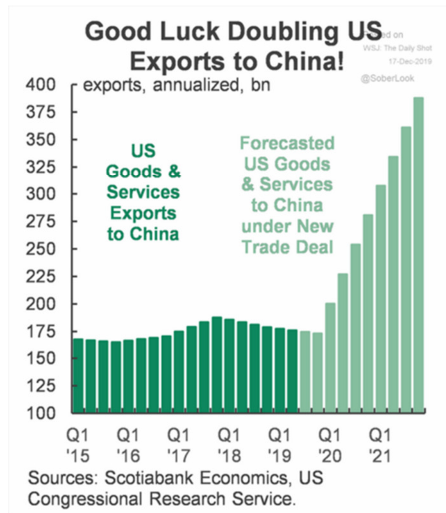
PeoplesBank Wealth Management
Economic & Investment Strategy Outlook
January 14th, 2020

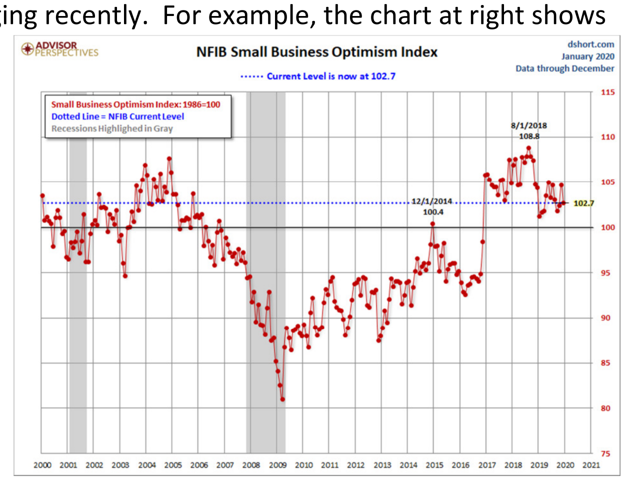
Economic Outlook

Television game shows have been part of American culture since the 1940s. In fact, the first US TV game show, *Truth or Consequences*, aired on NBC in 1941. The format of these shows has evolved over time. When game shows started to take off in the 1950s, quiz shows became the dominant format. This lasted until the end of the decade when it was revealed that many of the shows were rigged to increase ratings. Large-prize quiz shows didn't really make a comeback until 1999's *Who Wants to Be a Millionaire.* In the years that followed the quiz show scandals of the fifties, many of TV's most famous and longest running game shows were created such as *Jeopardy!*, *The Price is Right*, and *Wheel of Fortune.* This month, the Investment Strategy Committee was reminded of another famous game show: *Let's Make a Deal*. President Trump's "Phase One" trade deal with China was set to be signed on January 15th, and the Committee discussed its contents and its potential effect on the global economy and financial markets.



In looking at the high-level details of the trade deal as far as they have been released, China gets a reduction of some tariffs in exchange for agreeing to both import more US goods and purchase more US agricultural products. The finer details though are interesting. Specifically, the US agreed to indefinitely postpone the tariff on Chinese-made consumer goods that was set to be implemented on December 15th and cut in half to 7.5% the tariff imposed in September of last year on $120 billion of Chinese goods. Not reduced though was the 25% tariff on $250 billion of Chinese imports put in place in early 2019. In return, China agreed to increase its purchases of US agricultural products to $40 billion annually and increase its imports of other US goods by $200 billion annually. Both targets are to be met by 2021. As the chart at right from Scotiabank Economics shows, these purchase figures seem quite unrealistic. China will have to increase their US imports at a rather quick rate to meet their obligation under the trade deal. The same can be said for their agricultural purchases too. Also, under the terms of the trade deal, the US reserved the right to "snap back" tariffs if China does not comply with these terms. The skeptic in me thinks that by the end of 2021, it is likely that tariffs will again be discussed when China fails to meet these extremely ambitious targets.

In the shorter-term though, the trade deal should ratchet down some of the uncertainty pervading the economy. This in turn should help to bolster business confidence, which has been sagging recently. For example, the chart at right shows a survey measure of US small business confidence. Notice that by this measure, small business confidence peaked in the summer of 2018, just as the trade war began to ratchet up. While business confidence has leveled off, it remains well below its high. To the extent that business confidence does increase, that should lead to more hiring and more capital investment, which should lead to faster economic growth.



Looking more globally, reduced trade tensions should have other positive effects. For example, both global manufacturing and export growth also peaked in mid 2018. It appears likely that these measures bottomed in late 2019, and a reduction in trade war rhetoric should help these positive economic trends continue. Also, the US dollar tends to appreciate during periods of increased global uncertainty, as has been the case over the past two years. This is because the dollar is considered a “safe haven”, and increased global demand for US assets pushes up the price of the dollar versus other currencies. If the global markets perceive less uncertainty after the trade deal has been signed, this should help the dollar to weaken some. A weaker dollar would be positive for global growth as it makes it easier for non-US borrowers to pay down their dollar denominated loans. A weaker dollar would also help bolster the earnings of large US companies which have global sales and be a tailwind to the returns of non-US stocks.

Over the next several months, we continue to expect that the US economy will remain in an expansion. The leading economic indicators we follow suggest this outcome, as do easy credit and financial conditions. Also, as was discussed in our prior two outlooks, we are watching for signs that the global economy outside of the US is starting to accelerate. If we do become convinced that both faster economic growth outside of the US is taking hold, and the US dollar has begun a sustainable weakening trend, we would feel more favorable to non-US investments. As always, we will follow the weight of the evidence and change our recommendations accordingly.

Investment Strategy

Given our view that the US economy will remain in an expansion for the foreseeable future, and given the potential for economic growth outside of the US to begin to accelerate this year, we remain more favorable to stocks than bonds. While we are looking for the appropriate time to begin to reduce our large recommended overweight to US stocks, we have not yet arrived at that point. Therefore, we continue to recommend that clients have more US stock exposure than they normally would, particularly US large cap. On the bond side of portfolios, we continue to favor areas of the bond market that we expect to outperform during economic expansions such as high yield bonds and preferred securities.

We made no changes to our recommendations this month. The astute reader may notice though that some of our relative asset class recommendations have changed. Specifically, US Mid/Small Cap has moved from neutral to slightly attractive, Emerging Markets has moved from slightly unattractive to unattractive, and Real Estate has move from slightly attractive to slightly unattractive. The reason for these changes is that we updated our strategic or long-term allocation recommendations in late December as part of our annual review process. The strategic allocation targets are meant to be the neutral starting point from which we make our tactical or shorter-term allocation recommendations. Based upon our outlook for potential returns in various financial markets over the next ten years, we decreased our neutral starting point for US stocks both large and small. We also increased our neutral starting point for International Developed and Emerging Markets stocks and US Real Estate (REITs). This means that we have a larger US overweight versus neutral than before and a larger international equity underweight. Please see our overall recommendations on the next page.

Michael Haun, CFA, CFP ®
Vice President, Investment Strategist

PeoplesBank Wealth Management
Relative Asset Class Recommendations
As of 01/14/20

	Unattractive	Slightly Unattractive	Neutral	Slightly Attractive	Attractive
Stocks				X	
US Large Cap					X
US Mid/Small Cap				X	
International Developed		X			
Emerging Markets	X				
Energy Infrastructure MLPs			X		
Bonds		X			
US Investment Grade		X			
Inflation Protected Securities (TIPS)		X			
High-Yield				X	
International Bonds	X				
Municipal Bonds				X	
Preferred Stocks					X
Real Assets					
Real Estate		X			

As of 01/14/20. Recommendations subject to change at any time without notice.

Investment Process

PeoplesBank Wealth Management's asset allocation process develops both long-term (strategic) and shorter-term (tactical) recommendations. The strategic recommendations are based upon how the Investment Strategy Committee believes investment portfolios should be positioned in a generally neutral market environment over the next ten years. The tactical recommendations are meant to highlight opportunities over the next one to two years where the Committee sees either increased opportunity or risk.

The Wealth Management Investment Strategy Committee (ISC) is responsible for establishing and updating both the strategic (long-term) and tactical (short-term) asset allocation for Wealth Management's investment management and trust relationships. The committee is comprised of the senior members of Wealth Management and is chaired by Michael Haun, our Investment Strategist. The committee is also responsible for monitoring and updating strategies, managers, and funds within client portfolios. The ISC meets on a monthly basis.

If you have any questions or would like to discuss PeoplesBank Wealth Management's outlook further, please call Michael Haun at 717.747.2419 or email him at mhaun@peoplesbanknet.com.