Q3 2019: A Story in Three Acts

As any frequent theatergoer knows, a great show contains three essential elements: a hero plus a villain, conflict between these key characters and suspense surrounding the ultimate outcome. Based on that criteria, Q3 2019 would make a great movie, because all three elements showed up in multiple ways.

The quarter opened its run by hitting new records in July, bolstered by renewed optimism surrounding a U.S.-China trade deal. That same month, the Federal Reserve cut rates for the first time in over 10 years. Markets viewed the move as the beginning of an easing cycle intended to bolster a slowing economy.

However, by late July and August, we experienced our first taste of conflict for the quarter. Markets stumbled as trade talks with China turned acrimonious. China devalued its currency, sending global markets into turmoil. The Dow dropped 800 points on Aug. 14, its worst day of 2019. The term "Trump Recession" began to appear in conversation, which I can only define as a growing economy that's not growing as strongly as it was before.

Markets lost close to 7% from their mid-July highs to close out August. However, before the month was out, the yield on the 10-year U.S. Treasury plummeted and the yield curve inverted. We recovered significantly in September, nearly surpassing the highs set in July. Markets responded optimistically to the apparent revival of trade talks with China. Who's the hero in getting the discussion back on track? It's up for debate, but meetings are scheduled to resume in October, and suspense around a final agreement remains high.

The Fed listened to the feedback from its audience and lowered rates again in mid-September. However, divisions exist within the group regarding the need for continuing cuts. Rates around the world are close to zero or even negative — and the U.S. seems to be out of sync. It appears that markets have stolen the initiative from the Fed and driven it toward a reactive response in its approach. President Donald Trump's constant haranguing of Fed Chairman Jerome Powell adds to the drama and undermines the notion of an independent Fed.

It's not far-fetched to call Iran one of this quarter's villains, as they've remained increasingly belligerent after shooting down a U.S. Navy drone at the end of June. (In case you're wondering, the drone was the size of a Boeing 737.) Attacks on oil tankers and Saudi oil production facilities have only added fuel to an already combustible situation.

Finally, nowhere is the drama more intense than in Washington — and it shows no signs of letting up. In September, a whistleblower came forward with allegations that President Trump pressured the leader of Ukraine to investigate Joe Biden and his son in a July phone call. Following the allegations, House Democrats moved from investigating the possibility of bringing up impeachment proceedings to "really" investigating the possibility of bringing up impeachment proceedings. Things are likely to only get worse as we approach the 2020 election.

Equity Performance as of October 1, 2019					
Equity Index	**13-Week**	**YTD**	**1 YR**	**3 YRS**	**5 YRS**
S&P 500	-0.31%	19.08%	2.61%	12.93%	10.86%
S&P MidCap 400	-2.26%	15.72%	-3.55%	8.71%	8.79%
Russell 2000	-4.51%	11.93%	-9.42%	7.52%	8.08%
NASDAQ	-2.26%	19.19%	-1.60%	14.19%	12.33%
MSCI ACWI	-2.08%	13.23%	-1.74%	7.23%	4.59%
MSCI EAFE	-2.01%	12.27%	-1.64%	6.31%	3.35%

Source: Morningstar. Index Performance: Return (%). http://news.morningstar.com/index/indexReturn.html. Accessed Oct. 2, 2019.

Q4: The Drama Continues

It's not time for the curtains quite yet, as Q4 begins with a very similar dynamic to the start of Q3. We have some big questions to answer over the next few months. First of all, how will things go with China? We should get a glimpse of the answer in October as trade talks resume. Anticipation will drive markets as we move closer to a deal, but based on preceding events, negotiations will drag out over several months.

Another big question for Q4: Will the Fed continue to lower rates? It remains unclear about what actions the Fed will take and how the markets will respond, but it is feasible that we'll see another cut of 25 basis points at its December meeting.

Will the U.S. come to blows with Iran? The U.S. may strike at Iranian proxies in Syria, Iraq and Yemen, who said they attacked the Saudis. Strikes would keep tensions high but likely not lead to a shooting war with Iran.

Finally, will the Washington Circus continue to vie for our attention? Absolutely. And it is reasonable that every political plot twist featured on the main stage will create episodic turmoil and volatility in the markets.

Stay for the Credits

So far, the Fed has delivered on the market's demands. As always, China is a wild card; both President Trump and Chinese president Xi Jinping could both use a public relations boost, and a deal could be beneficial for both sides.

No matter what direction the markets take in Q4 and beyond, we believe that the best thing investors can do right now is refill their popcorn, keep their seats and see how the show plays out. Now is a great time to schedule an appointment with your financial advisor, who can review your portfolio and ensure it lines up with your risk tolerance and goals.

Most importantly, remain focused on the bigger picture. There may be conflict in your story along the way, but staying the course can help move you closer toward your happy ending.