THIRD QUARTER 2019 REPORT

ENTERPRISE
WEALTH MANAGEMENT
A division of Enterprise Bank

IN THIS ISSUE

The Wall of Worry…

The old Wall Street adage has reappeared in recent months. Many market participants have used the phrase to describe the increasing number of bricks being stacked in the way of the U.S. bull market that has surpassed its tenth year. The following pages describe several developments globally that can turn even an optimist's mood sour. More recently, the political climate in Washington and weak manufacturing statistics serve as an additional weight on sentiment. These developments have fueled market volatility in the weeks preceding the end of the third quarter.

Yet despite the Wall of Worry, the major domestic equity indices continue to trade near record levels. The S&P 500 Index has provided participants a 20.2% total return through September, the best start to the year since 1997. All asset classes highlighted on the next page have seen positive returns for the year. Thus, while there is cause for consideration, these developments don't necessarily foreshadow the imminent end of the bull market.

For the market to move forward in the coming quarters, investors and businesses would like to see progress on the two major issues discussed on the next page.

Continued inside

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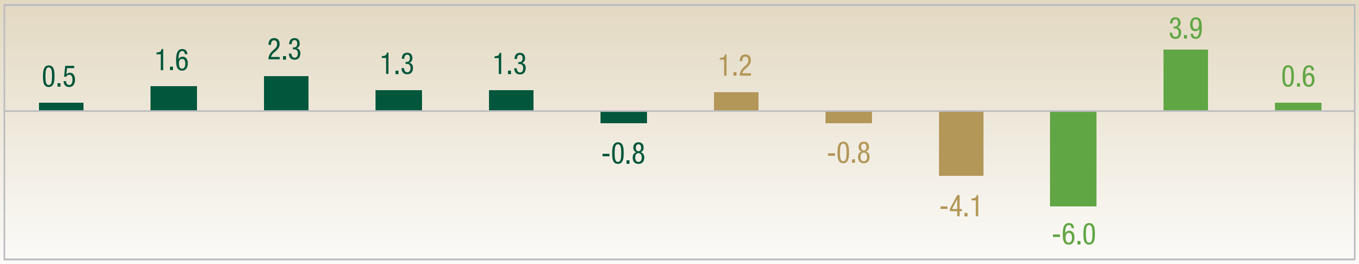
The U.S.-China Trade War. Tensions between the U.S. and China ratcheted up in the third quarter as each side accused the other of not living up to their end of the deal that was reportedly close to being finalized. As a result, companies doing business in China have been focused on rerouting existing supply chains while companies everywhere are holding off on new investment until more clarity is provided on U.S.-China relations and the resulting impact on the U.S. and global economy.

The Downward Sloping Yield Curve. Historically, a downward sloping yield curve, also referred to as an inverted yield curve, has portended economic recession. Simply put, the yield curve is a graph of U.S. Treasury interest rates across maturities from short-term to thirty years. The combination of global growth fears and a slow-to-cut Federal Reserve briefly pushed the 10-year Treasury yield lower than its two-year counterpart, ending the quarter just 0.04% away from the much dreaded inversion. While credit markets remain well-behaved, a yield curve inversion risks creating a self-fulfilling prophecy of economic gloom. As such, the markets want more easing. The Fed has stated it will "act as appropriate to sustain the expansion."

The current economic expansion is now also the longest in U.S. history (10 years and three months old at the end of the third quarter). Its ability to break through the bricks in the Wall of Worry will be dependent on companies' ability to navigate increased trade tensions and the Fed's ability to manage interest rates to sustain the expansion. Should we see progress on these issues, this expansion will continue into the foreseeable future and prolong the bull market.

THIRD QUARTER 2019 TOTAL RETURNS (%)

Fears over the effects of an extended trade war and yield curve inversion weighed on equities in the third quarter.



	RISK CONTROL			RISK ASSETS								
	FIXED INCOME						EQUITIES			REAL ASSETS		
	Cash	Muni	Inv. Grade	TIPS	High Yield	EM Debt	U.S.	Dev. Ex-U.S.	EM	NR	GRE	GLI
Q3	0.5	1.6	2.3	1.3	1.3	-0.8	1.2	-0.8	-4.1	-6.0	3.9	0.6
YTD	1.8	6.7	8.5	7.6	11.4	7.9	20.2	14.0	5.7	7.0	19.8	20.8

Source: Northern Trust Global Asset Allocation, Bloomberg. NR = Natural Resources; GRE = Global Real Estate; GLI = Global Listed Infrastructure. Indexes are gross of fees and disclosed on last page.

Key Developments

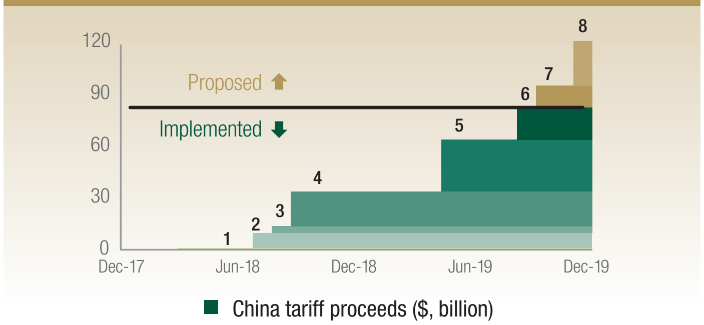
Trade Tensions: Taking Inventory

Keeping up with all the tariffs enacted on China can be hard work. Here's a cheat sheet of all tariff actions thus far and the proceeds accrued to the U.S. government (an annual $82 billion currently). The numbers 1 to 5 in the chart below depict the date and the size of each round of tariffs implemented since June 2018. #1 for example was the initial tariff on steel and aluminum exports to the United States. The axis at the left shows the cumulative dollar amount of the proceeds to the U.S. from the tariffs, in billions of dollars. Number 6, 7, and 8 represent tariffs proposed in recent months that have not yet been implemented. Who is paying for the trade war? That is not a simple answer. Both sides are incurring costs – as is the global economy.

The Oil Crisis That Wasn't

Drone strikes on a major Saudi Arabia production facility temporarily knocked half of the country's, and 5% of the world's, oil production offline. Thirty years ago this event, the largest production disruption in history, would have consumed this entire quarterly review. Today it barely made the cut as a key development. Oil prices spiked by 15% the following day but fell back below pre-attack levels within two weeks. Global stock markets barely flinched highlighting the reduced economic sensitivity to oil supply shocks.

U.S. TRADE WAR ON CHINA ESCALATION



BIGGEST DROPS IN OIL PRODUCTION

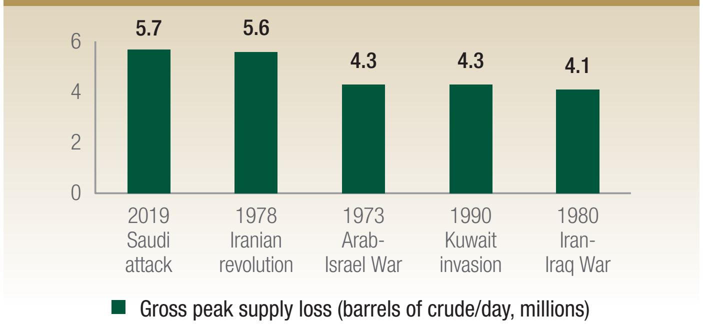


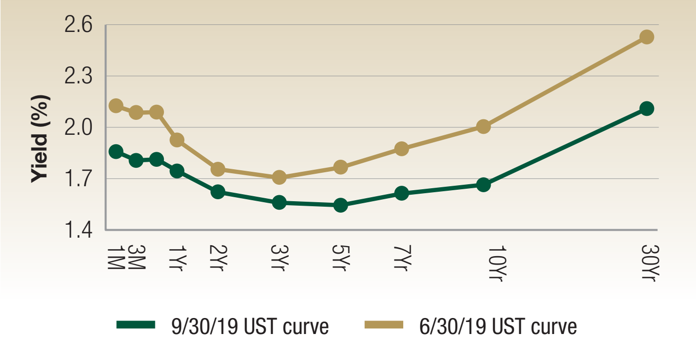
Chart Sources: Northern Trust Investment Strategy, Bloomberg. Indexes are gross of fees. Past returns are no guarantee of future results.

Market Review

Interest Rates

The yield curve moved lower on both the front and back ends as the Fed played catch up to what was priced into the middle of the curve in terms of rate cuts. All said, the Fed cut rates twice in the third quarter and has indicated that it will "act as appropriate to sustain the expansion." Given global growth pressures — including manufacturing purchasing manager indices now solidly in contraction territory (albeit with services still fairly healthy) — the Fed may need to provide more accommodation in the fourth quarter.

U.S. TREASURY YIELD CURVE



Wild Ride in the Rates Markets

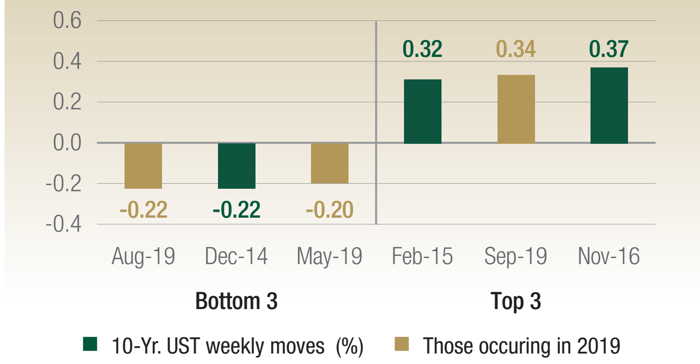
The fixed income markets are supposed to be mostly drama free. But the third quarter was a different story as market participants weighed trade wars and persistently low inflation against still-positive U.S. economic growth dynamics. In mid-September, the 10-year Treasury yield rose by 0.34% — second only to the week of Trump's election in terms of upward movement over the past five years. This was on the back of the largest rate reduction over the past five years in August. Since the September spike, the 10-year yield has settled back below 1.70%.

Yield Wanted

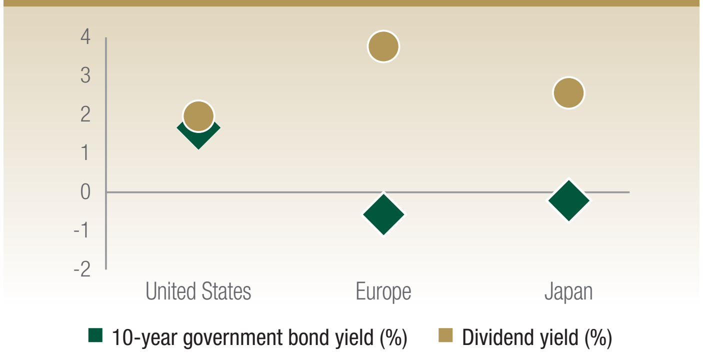
Low and volatile interest rates are prompting many to question the merits of holding fixed income instruments. Fixed income certainly isn't for the income anymore. Across the three biggest economic regions, the local stock market index is providing better yields than the local 10-year government bond — especially the case in Europe and Japan. Other, more income-oriented asset classes such as global real estate and infrastructure have even better yields. That said, fixed income still plays a role in the portfolio for diversification purposes.

Source: Northern Trust Global Asset Allocation, Eurasia Group, Cornerstone Macro, MSCI, Bloomberg.
*Europe 10-year yield is proxied by Germany.

TOP/BOTTOM WEEKLY RATE MOVES (LAST 5 YEARS)



STOCK DIVIDEND YIELDS VS. BOND YIELDS



Credit Markets

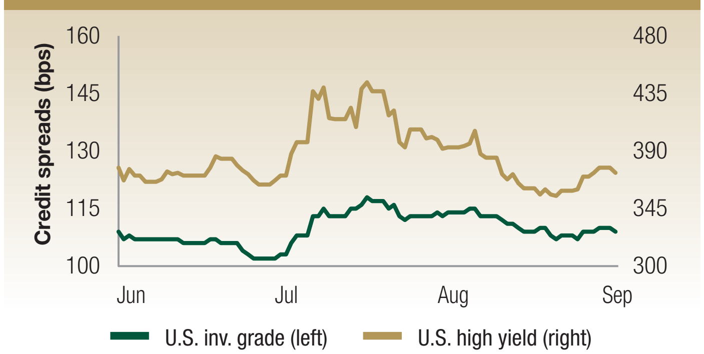
Credit markets remain well-behaved, with investment grade and high yield spreads mostly unchanged and near decade lows. Despite yield curve inversion concerns, healthy credit markets suggest the economic expansion can continue. Spreads are supported by both fundamental and technical drivers. Fundamentals remain sound, with interest coverage ratios high. At the same time, technicals are supportive with great investor demand for yield and new issuance mostly limited to refinancing to take advantage of low interest rates.

Equities

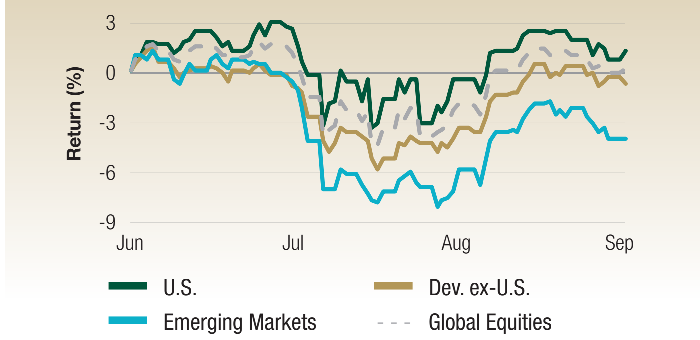
Global equities managed to squeak out a 0.1% gain for the quarter, shrugging off global growth pressures (driven by increased trade tensions) thanks to the interest rate relief valve (with lower rates putting a floor under valuations). U.S. equities once again proved most resilient against trade war concerns, gaining 1.2% for the quarter, while developed ex-U.S. and emerging market equities were both in negative territory. Year-to-date, U.S. equities have far outpaced their international counterparts with a 20.2% gain.

Source: Northern Trust Global Asset Allocation, Bloomberg. UST = U.S. Treasury. Indexes are gross of fees.

CREDIT SPREADS



REGIONAL EQUITY INDICES



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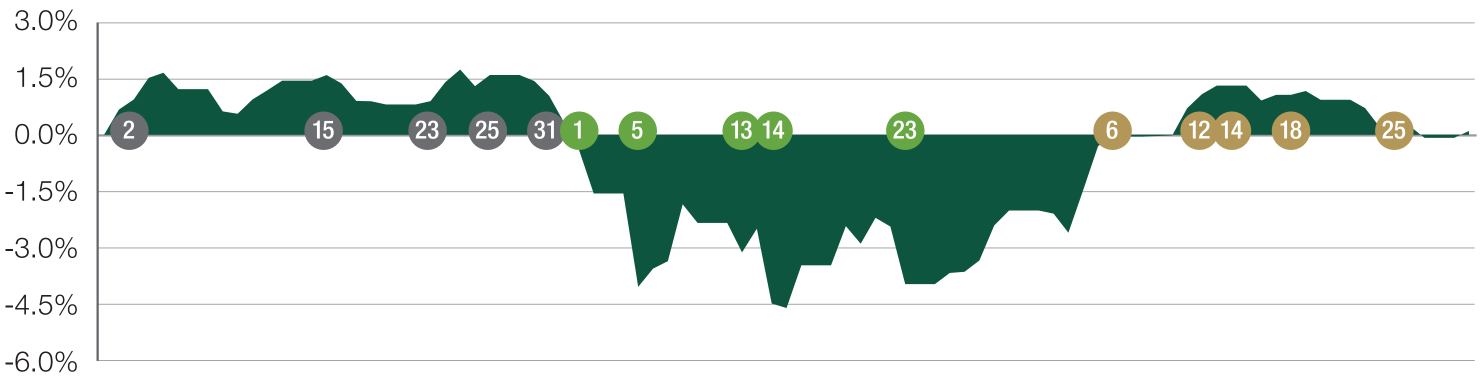
Market Events

3Q 2019 global equity total return: 0.1%



JULY	AUGUST	SEPTEMBER
2 Christine Lagarde receives nomination to succeed Mario Draghi as European Central Bank president.	1 President Donald Trump tweets plans for a 10% tariff on an additional $300 billion in Chinese goods starting September 1.	6 China announces $126 billion stimulus package and reduction of the required reserve ratio.
15 China's 6.2% annualized quarterly growth represents the country's slowest quarterly growth in nearly three decades.	5 China allows the yuan to reach its lowest level since 2008, weakening to slightly above 7 per dollar; the U.S. labels China a currency manipulator.	12 ECB cuts interest rates by 0.1% (to -0.5%), and plans to buy €20 billion in bonds per month starting in November.
23 Boris Johnson wins leadership contest to succeed Theresa May as the next U.K. prime minister.	13 The Trump administration delays tariffs on some Chinese goods (mostly consumer goods) until Dec. 15.	14 Drone attack on Saudi Aramco wipes out about 5% of global oil supply; oil prices surge by over 10%.
25 ECB leaves rates unchanged; Draghi indicates significant monetary stimulus may be needed going forward.	14 The U.S. yield curve inverts at the two-year and 10-year tenors for the first time since the global financial crisis.	18 Fed cuts Fed funds rate by an additional 0.25%, now targeting a range of 1.75 to 2.00%.
31 Fed cuts interest rates for first time since the financial crisis by 0.25% and concludes its balance sheet reduction earlier than planned.	23 China announces new tariffs on $75 billion of U.S. imports; Trump responds with an additional 5% of tariffs on $250 billion of goods (Oct. implementation).	25 Democratic Speaker of the House Nancy Pelosi launches impeachment inquiry on President Donald Trump.

Indexes used: Bloomberg Barclays (BBC) 1-3 Month UST (Cash); BBC Municipal (Muni); BBC Aggregate (Inv. Grade); BBC TIPS (TIPS); BBC High Yield 2% Capped (High Yield); JP Morgan GBI-EM Global Diversified (Em. Markets Fixed Income); MSCI U.S. Equities IMI (U.S. Equities); MSCI World ex-U.S. IMI (Dev. ex-U.S. Equities); MSCI Emerging Market Equities (Em. Markets Equities); Morningstar Upstream Natural Resources (Natural Res.); FTSE EPRA/NAREIT Global (Global Real Estate); S&P Global Infrastructure (Global Listed Infra.)

From the Managing Director

Dear Friends and Clients,

Another summer has quickly passed, and we are now blessed with cooler temperatures and the wonderful fall foliage. I hope you enjoyed your summer and had time to rest with family and friends. The wealth management team stayed quite busy through the summer, as the magnitude of the events in the global financial markets was quite extraordinary.

Reading through this commentary you may be thinking there is a lot going on! The Federal Reserve cut interest rates twice in the period, the UK named a new leader and despite many Parliamentary maneuvers, the future of Brexit is still uncertain, the administration announced additional tariffs on China in early August, an important Saudi oil facility was bombed which reduced global oil supply for several weeks, and at the end of September, House Speaker Pelosi announced the impeachment inquiry of President Trump. We could mention several other events that are noteworthy, but they were crowded out of the headlines.

The investment staff commented these market moving events would be substantial for any one year, but all happened within just three months! You would suspect these events would equate to significant volatility in the markets, and while the equity and fixed income markets did move sharply, the major domestic equity and fixed income index returns were all positive during the third quarter.

Our message is that despite the turbulence in the financial markets and the news media that focuses incessantly on "Breaking News," it's important to maintain your long-term perspective and not be swayed by the events of the day or the quarter or even a year. Thus, we continue to encourage you to disregard the short-term noise and focus on your goals and asset allocation as the best way to build wealth over a long period of time. As always, please contact a member of your team if there is any financial matter you'd like to discuss.

As I'll next be in touch through this column early in the New Year, I wish you and your loved ones a beautiful fall, Happy Thanksgiving, and joyful December holidays.

Sincerely,

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Chief Operating Officer, Enterprise Bank

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