OUTLOOK 2020

BRINGING MARKETS INTO FOCUS

LPL RESEARCH

ECONOMY | POLICY
BONDS | STOCKS

LPL Financial

TAKING A LOOK

HINDSIGHT IS 2020, BUT FINDING CLARITY IN FUTURE UNCERTAINTY CAN BE FUZZY.

AT LPL RESEARCH, as we look forward to the year 2020 and a new decade, some key trends and market signals will be important to watch, including progress on U.S.-China trade discussions, an encouraging outlook from corporate America, and continued strength in consumer spending.

Trade risk, slower global growth, and the impeachment inquiry have garnered a lot of the headlines recently, but behind the scenes the U.S. economy has remained resilient. Economic data has been meeting lowered expectations, indicating an expansion that is still enduring. Most recently, third quarter economic growth was consistent with the long-term trend of this current economic expansion, which is now more than 10 years old.

We expect the U.S. economy to continue to grow in 2020 and support gains for stocks, although we are increasingly mindful of our position in the business cycle. At some point in the future, this record-long expansion will come to a close, leaving investors wondering what's next. Against this backdrop, questions about the next potential recession and the 2020 U.S. presidential election continue to be top of mind for many investors. While we can't see into the future, one thing we can predict is that uncertainty in the markets is here to stay. And we are here to help. We offer our *Outlook 2020*, your guide to preparing for this dynamic—and uncertain—market environment.

ECONOMIC FORECASTS

ECONOMY

DOMESTIC: We are expecting 1.75% U.S. GDP growth in 2020. Our forecast reflects the potential for continued trade uncertainty and weak business investment, but a steady consumer [FIG.1].

GLOBAL: Europe and Japan continue to struggle with trade uncertainty, geopolitical concerns, and sluggish growth. We anticipate more opportunities for growth in emerging markets' economies, with countries outside China playing a growing role.

INFLATION: Consumer inflation has picked up slightly, and we believe inflation will continue to grow at a healthy but manageable rate.

EMPLOYMENT: U.S. job growth has been steady, although recently it has started to show signs of moderating. Some cooling down would be expected at this point in the economic cycle.

RECESSION: Prolonged trade uncertainty and a potentially rancorous U.S. election season lead us to believe that recession starting in the fourth quarter of 2020 or first quarter of 2021 could be possible, but we don't think it's probable.

BONDS

Short-lived and shallow yield curve inversions are not worrisome in our view, and we continue to emphasize a blend of high-quality intermediate bonds in tactically oriented portfolios.

STOCKS

We look for solid U.S. equities performance to continue, and we see more potential upside in emerging markets than developed international markets. We continue to prefer cyclical sectors for appropriate strategies as the U.S. economic expansion endures, and a balance of growth and value styles.

FIG 001

REAL GDP YoY%

*LPL ESTIMATES

	2018	2019*	2020*
U.S.	2.9%	2.0%	1.75%
Developed ex-U.S.	1.9%	1.3%	1.5%
Emerging Markets	4.5%	3.9%	4.6%
Global	3.6%	3.5%	3.5%

U.S. MARKETS

*LPL ESTIMATES

	2019*	2020*
10-year U.S. Treasury Yield	1.75–2%	2–2.25%
S&P 500 EPS	$165	$175
S&P 500 Fair Value	3,000	3,250–3,300

Source: LPL Research, Bloomberg, International Monetary Fund (IMF) 10/16/19
2019 U.S. economic data, U.S. GDP estimate, and global GDP estimate are LPL forecasts.
Other GDP estimates are IMF projections.

ECONOMY IN FOCUS

STRONG CONSUMER SPENDING HAS PROPELLED THE U.S. ECONOMY, WHILE CLARITY ON TRADE COULD SUPPORT BUSINESS INVESTMENT.

20/200
20/100
20/70
20/50
20/40
20/30
20/25
20/20
20/15
20/13
20/10

THE U.S. ECONOMY has slowed from 2018's pace, but it is still growing, and we believe it will continue growing through 2020, albeit at a slower rate than our 2019 growth expectation **[FIG.2]**.

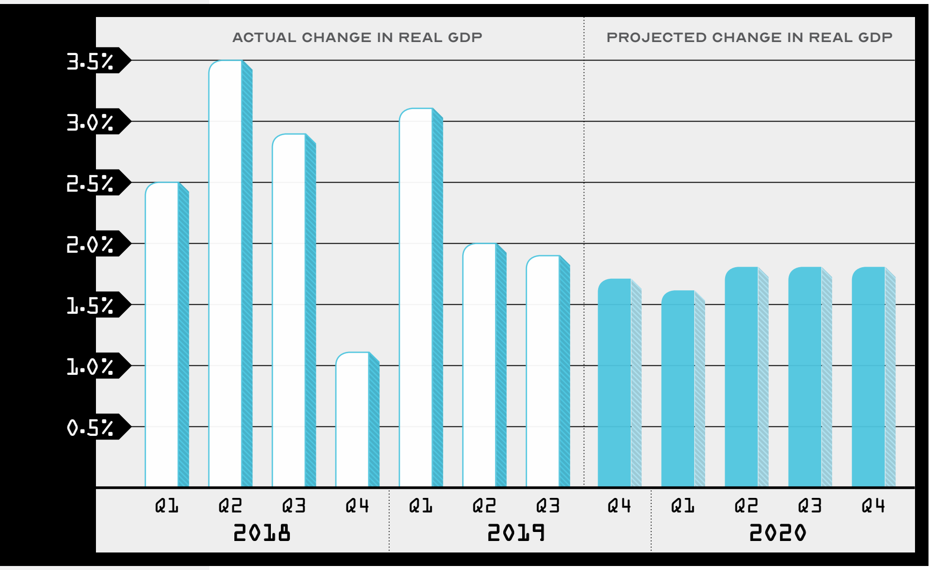
As we looked ahead back in 2018, we expected the combination of more favorable tax rates, repatriation of internationally sourced profits, and immediate capital expensing provisions enacted in the *Tax Cuts and Jobs Act of 2017* to be tailwinds for capital expenditures. Yet it appears these tailwinds have been hindered by the headwind from trade uncertainty. Slower international growth, due in part to the U.S.-China trade dispute, has also added pressure to U.S. economic growth, offsetting some of the impacts of fiscal stimulus and the Federal Reserve's (Fed) accommodative monetary policy.

As we expect these same geopolitical and trade concerns to persist into 2020, we're offering a forecast of 1.75% U.S. gross domestic product (GDP) growth in 2020. The expected slowdown from 2019 reflects the U.S.-China trade dispute dragging into the first part of 2020 and increased odds of recession in the latter months of 2020 or early 2021.

Geopolitical *refers to a combination of political, economic, and geographic (regional or country-specific) factors.*

FIG
002

GDP GROWTH HAS SLOWED, BUT MAY REMAIN STEADY



Source: LPL Research, Bloomberg 11/01/19
Gross domestic product (GDP) projections are median Bloomberg consensus forecasts.
The economic forecasts set forth may not develop as predicted.

CONSUMER INFLATION PICKS UP

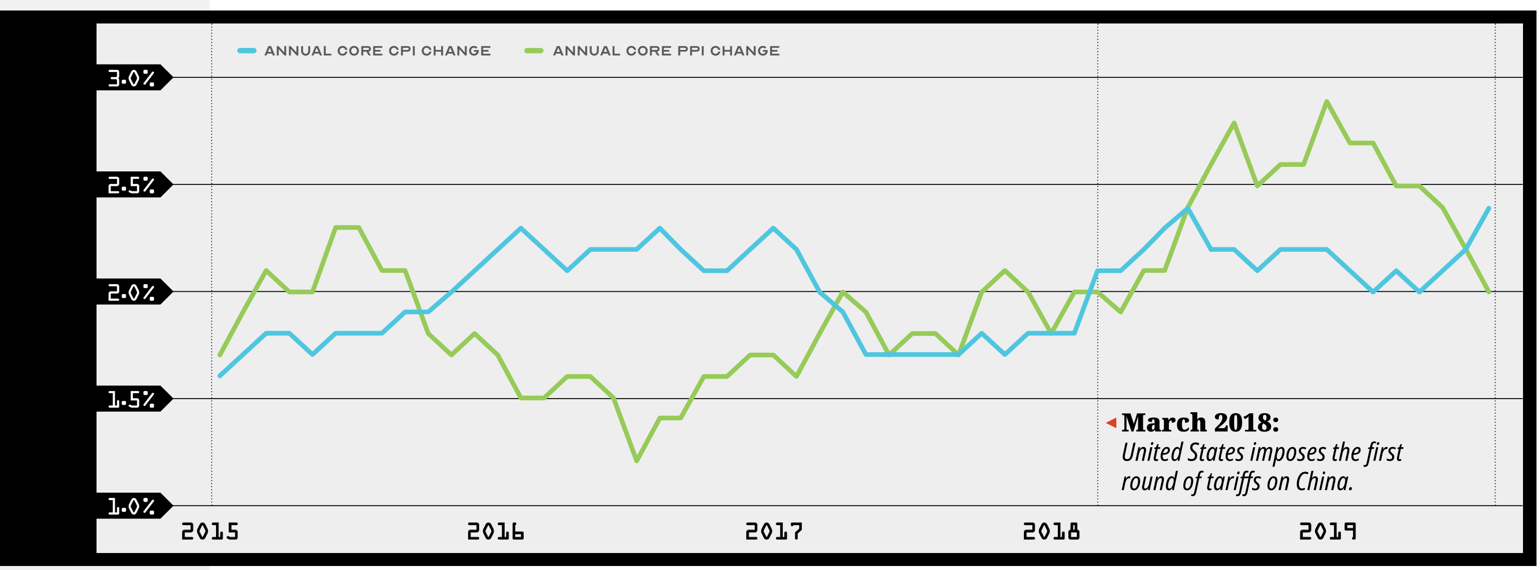
For some of us, inflation is considered a negative word, but some inflation (price increases) is often a sign of economic growth, while a weak economy is often accompanied by very low or even negative inflation. The Fed targets an inflation level of about 2%, which generally indicates a healthy economy that is not growing dangerously fast.

Consumer inflation has picked up recently, even though international trade tensions and slower global growth have had some moderating impact on producer prices. Consumer prices increased at a healthy pace in 2019, growing at the fastest pace of the economic cycle for a second straight month in September, as evidenced by the core Consumer Price Index (CPI), which excludes food and energy **[FIG.3]**. At the same time, year-over-year growth in the core Producer Price Index (PPI), which better reflects costs to businesses, declined. Limited upward pressure on wholesale prices most often reduces the likelihood of an acceleration in consumer prices.

So far, we haven't seen slowing producer price growth translate into lower consumer inflation, likely because U.S. companies still have ample pricing power amid strong trends in domestic consumer spending. Consumer spending, which comprises approximately 70% of the economy, continues to grow at a solid pace and is anchoring the U.S. economy. We believe economic factors currently benefiting consumers and businesses—full employment, moderate wage growth, and low interest rates—will help sustain healthy but manageable inflation going forward.

FIG
003

WHOLESALE PRICES MAY HELP CONTAIN INFLATION



Core Consumer Price Index (CPI) and Producer Price Index (PPI) exclude food and energy prices.

Source: LPL Research, U.S. Bureau of Labor Statistics 11/01/19

JOBS ARE STRONG, PRODUCTIVITY NEEDS IMPROVING

The U.S. labor market has remained strong despite signs of weakness in other pockets of the U.S. economy. Hiring began to slow toward the end of 2019, although job growth has remained near the cycle average. And even though hiring slowed slightly, it still looked healthy, especially considering this economic expansion is in its eleventh year.

Other labor market measures also appeared healthy. The unemployment rate stood at 3.6% in October, near a cycle low, and initial jobless claims continued to be subdued. Clarity on trade could boost business investment, enabling workers to produce more efficiently, thereby supporting future productivity gains. Gains in productivity can help limit the impact of increases in labor costs on companies while increasing the economy's overall economic potential.

It's natural for job growth to slow when the economy is near full employment. Job growth slowing over the course of the year to around 100,000 per month would be consistent with our economic outlook. Even if job growth slowed to 100,000 per month, unemployment would pick up only modestly and could remain near or under 4%.

Wage growth slowed in the third quarter too, hinting that inflationary pressures could be showing signs of moderating. Average hourly earnings growth fell to 3% year over year as of October, lower than the cycle peak of 3.4% in February 2019 but still ahead of inflation **[FIG.4]**. This pace of wage growth should still be enough to buoy personal incomes and consumer spending without driving interest rates higher.

THE U.S. LABOR MARKET HAS REMAINED STRONG DESPITE SIGNS OF WEAKNESS IN OTHER POCKETS OF THE U.S. ECONOMY.

FIG 004

SOLID WAGE GROWTH SUPPORTS SPENDING

Source: LPL Research, U.S. Bureau of Labor Statistics 10/31/19


S Z N
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K C R H N
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WE FORECAST 1.75% U.S. GDP GROWTH IN 2020.

20/200
20/100
20/70
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20/40
20/30
20/25
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20/10

RECESSION WATCH

The U.S. economy remains on solid footing as 2020 approaches, and we continue to see low likelihood of recession in the coming year. After a record-long expansion, though, we are bound to have a recession at some time. For now, economic fundamentals have signaled that the consumer remains sound, and any clarity on trade could potentially boost business investment, possibly supporting productivity growth and elongating the expansion.

A recession is generally taken to be two consecutive quarters of the economy shrinking, although other factors count too. When a recession does settle in eventually, we suspect the likeliest cause may be a convergence of global events, including a highly charged U.S. elections season, prolonged trade uncertainty, and continued weak economic growth in international developed countries. But the key could be the impact these events have on consumer and business confidence. Even if these events continue to weigh on consumer spending and business investment, we would still expect a low probability of recession starting any earlier than the fourth quarter of 2020 or first quarter of 2021.

INTERNATIONAL ECONOMIES STRUGGLING

EUROPE: The U.S. economy, paced by the consumer, has continued to amble along at trend growth near 2%. Meanwhile, in Europe, Germany has teetered on the cusp of recession as its manufacturing sector contracts, Brexit (the United Kingdom's exit from the European Union) indecision continues to cloud the outlook for businesses operating in the U.K., deficit spending remains a challenge—particularly in Italy—and the benefits of monetary policy

GLOBAL ECONOMY

appear to have been stretched to the limit, despite the best efforts by the European Central Bank (ECB).

Europe also has been impacted by trade uncertainty, and there's still a possibility that tariffs on European autos will be imposed. The Eurozone may struggle to deliver even 1% GDP growth in 2020, after similarly lackluster performance in 2019.

JAPAN: The picture has been no better in Japan. The September 2019 trade agreement between Japan and the United States on agriculture, investment, and digital trade was encouraging, but the Japanese manufacturing sector saw several consecutive months of contraction in the second half of 2019. As with Europe, auto tariffs remain a risk. A consumption tax increase enacted October 1 further clouded the outlook for an economy that is not expected to grow more than 1% for the foreseeable future, based on Bloomberg's consensus forecasts. The Bank of Japan has been as aggressive as the ECB in implementing monetary policy, yet has little growth to show for it.

CHINA: Slower growth in China has weighed some on growth in emerging markets' economies overall, but Bloomberg's consensus forecast for emerging markets' GDP is still 4.6% for 2020. These forecasts could be conservative if the United States and China make further progress on trade in the early part of 2020. Nevertheless, with China's economic growth slowing, look for other emerging-market countries and regions, such as India, Russia, and Latin America, to pick up the slack. Overall, policies and demographics remain more supportive for emerging markets' economies than their developed counterparts, including a surprise corporate tax cut in India announced in September 2019.

BREXIT TAKES A BREAK

At its Super Saturday meeting October 19, the U.K. Parliament voted to not vote on the latest Brexit deal, which triggered a request for an extension of the October 31 Brexit deadline to January 31, 2020. The extension made a "hard" or "no deal" Brexit, which is the worst-case economic and market scenario, unlikely, although there are still scenarios in which it is possible. The U.K. will hold elections December 12, 2019, with potential outcomes ranging from the U.K. Parliament approving a plan already approved by the E.U. to a new vote on whether the U.K. should exit the E.U.

CENTRAL BANKS ARE BACK

THE FEDERAL RESERVE IS CURRENTLY IN WAIT-AND-SEE MODE AS IT GAUGES THE IMPACT OF ITS THREE 2019 RATE CUTS.

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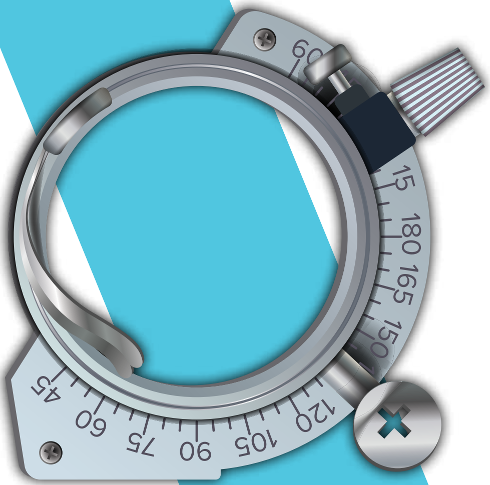


AT ITS MEETING in October, the Fed answered the markets' call and cut interest rates by 25 basis points (.25%) for the third time this year, taking its main policy rate down to a range of 1.5–1.75%, while signaling that its midcycle rate adjustment was likely complete for now. Historically, three consecutive 25 basis point (.25%) cuts have led to continued equity gains and avoided recessions. After three initial quarter-point cuts in 1975, 1996, and 1998, the S&P 500 rose an average of 10% six months later, and 20% 12 months later. The Fed stated in its post-meeting press conference it would have to see a significant pickup in inflation to consider hiking rates, which is probably a good ways off in our view.

POLICY IMPACTS INVESTORS

Policy has played an increasingly important role in investors' outlooks. Over the past several years, a combination of monetary and fiscal initiatives has supported growth in economic output and corporate profits. More recently, the tailwinds of taxes, deregulation, and additional government spending programs (fiscal policy) have been offset by headwinds from global trade uncertainty. This has led to weakness in manufacturing activity around the world, which has required additional responses from global central banks (monetary policy), a majority of which have already lowered interest rates, some into negative territory. The ECB and Bank of Japan both have used monetary policy extensively

to try to stimulate their economies, but without much luck to date.

Other geopolitical stresses have complicated matters. The impeachment inquiry in the United States, Brexit confusion and rising populism in Europe, the increase in consumption taxes in Japan, and escalating tensions in the Middle East and with North Korea have all contributed to investor concerns about heightened policy uncertainty. A highly charged U.S. presidential election also could add to the uncertainty during the latter part of 2020.

While further progress on the stickiest U.S.-China issues and a Brexit resolution may come in early 2020, politics will continue to play a role in the United States and globally throughout the year. We will continue to keep an eye on tensions around the globe as they arise. We remain generally optimistic that even some relaxation in tensions could benefit global economic growth in 2020, potentially spurring reacceleration, even if not to the levels of 2018 and 2019.

TRADE POLICY WEIGHED ON GLOBAL ECONOMIES

Trade uncertainty has weighed on the global economy, and cracks are forming in the United States' economy as well. The biggest impact has been in the manufacturing sector, which has weakened as trade tensions have escalated. According to data from the Institute for Supply Management (ISM), U.S. manufacturing growth reached a 10-year low in September 2019, in step with global manufacturing's steep decline over the last several months.

Companies have stepped back from expansion plans, lowering demand for goods and cutting manufacturing output. Stabilizing manufacturing is critical because of the sector's importance to corporate profits. Corporate profits in turn serve as a leading indicator for employment and investment. Clarity on trade is also important for renewed business investment, which helps boost productivity. The markets signaled their

Fiscal policy *refers to federal taxation and spending actions.*

Monetary policy *refers to decisions by the Federal Reserve and other central banks regarding interest rates and the money supply.*

displeasure with weaker manufacturing reports prior to the positive trade headlines in the fall, highlighting the importance of trade negotiations in supporting global economies.

U.S.-China trade negotiations in October resulted in a verbal agreement on an initial relaxation of tensions that may be signed before 2019 ends. We also believe President Donald J. Trump and China's President Xi Jinping will continue to make incremental progress on hammering out a new trade relationship. Ultimately, we expect further progress in 2020 as the negotiations proceed in phases.

We are also watching for progress on the United States-Mexico-Canada Agreement (USMCA) trade agreement (also known as NAFTA 2.0). Delay could lead to prolonged uncertainty for trade with Mexico and Canada. There is also a chance the United States could implement auto tariffs on the European Union and Japan, adding risk to global economic growth and corporate profits.

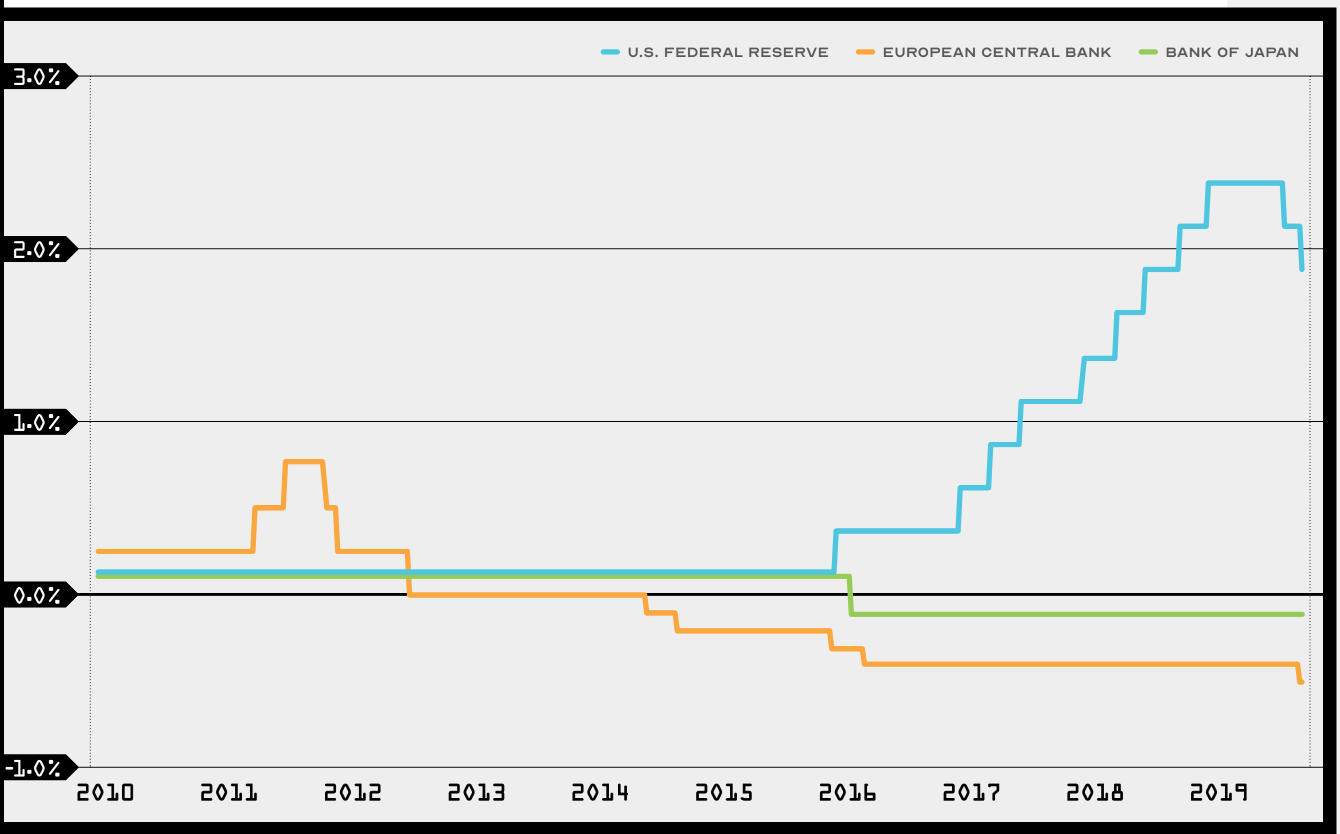
GLOBAL RECOVERY HINGED ON MONETARY POLICY

Most of the global economic recovery has hinged on unprecedented monetary policy programs, and global central banks have recently switched back into easing mode, cutting interest rates to combat trade-related economic weakness. Around the world, negative-yielding debt, in which a lender pays the borrower for the privilege of loaning the borrower money, has become a new type of normal. Negative-yielding debt reached a record $17 trillion in September.

FEDERAL RESERVE: After its meeting in October when it cut interest rates for the third time this year, the Fed announced it would have to see a significant pickup in inflation to consider raising rates. That comment may encourage markets to respond positively to good economic news and to be less fearful that it would lead to a rate hike. If the Fed's three cuts turn out to be enough

FIG 005

FED RATE REMAINS ABOVE OTHER CENTRAL BANKS



Source: LPL Research, Bloomberg, U.S. Federal Reserve, European Central Bank, Bank of Japan 11/01/19

AROUND THE WORLD, NEGATIVE-YIELDING DEBT HAS BECOME A NEW TYPE OF NORMAL. NEGATIVE-YIELDING DEBT REACHED A RECORD $17 TRILLION IN SEPTEMBER 2019.

support to help the U.S. economy navigate its recent slowdown, it may signal increased potential for U.S. stock market gains in 2020.

EUROPEAN CENTRAL BANK: In the third quarter, the ECB took bold steps in cutting its target interest rate further into negative territory (to -0.50%) and restarting bond purchases that will continue until inflation targets are reached, without providing an end date. The ECB is now committed to policy accommodation that could potentially last years, but is also having a diminishing impact.

BANK OF JAPAN: At its October 31 policy meeting, the Bank of Japan elected to keep its target interest rate at 0.1% and maintain bond purchases at existing levels (80 trillion yen, or roughly $736 billion annually). The central bank also strengthened its commitment to providing significant monetary policy support with an "as long as needed" timetable that replaced "at least until spring of 2020." Japanese monetary officials have clearly indicated that they are open to the idea of further reducing interest rates into negative territory in response to weaker global GDP growth, and they likely want to get ahead of any economic weakness that may result from the October value-added tax increase.

CENTRAL BANK INTERACTION: Monetary policy is a coordinated effort between the U.S. Federal Reserve and global central banks right now, but there are complicated dynamics to consider. There is a mismatch between the Fed and other central banks' interest rate policies [FIG.5]. The danger there is that the interest-rate differential between U.S. Treasuries and other sovereign debt could widen further and put more upward pressure on the U.S. dollar. This would make servicing the debt payments on the dollar-denominated debt issued by non-U.S. countries more expensive, which could become an increasing burden on the global economy. A stronger U.S. dollar could also potentially weigh on U.S. exports by making them more expensive and depress international stock returns for U.S. investors. While not an explicit part of U.S. monetary policy, concern about dollar strength may be contributing to the Fed signaling greater flexibility on inflation before it raises rates.

We expect global central banks to keep rates at levels that encourage increased economic activity as the global economy recovers from the impact of trade disruptions, and we see ongoing central bank interventions in international markets as appropriate for now.

EYES ON THE BOND MARKET

WATCHING THE WARNING SIGNS IN THE UNITED STATES AND AROUND THE WORLD.

Yield curve inversion *is when long-term yields fall below short-term yields.*

THE BIG NEWS in fixed income in 2019 was the yield curve. When we talk about the yield curve, we generally mean the difference or spread between the 2-year and 10-year U.S. Treasury yields. In a healthy economy, long-term yields will almost always be higher than short-term yields, which encourages lending and supports economic growth. When a yield curve inverts, short-term yields rise above longer-term yields, lending is typically less profitable, and consumers, businesses, and investors may rein in spending and investment amid recession fears.

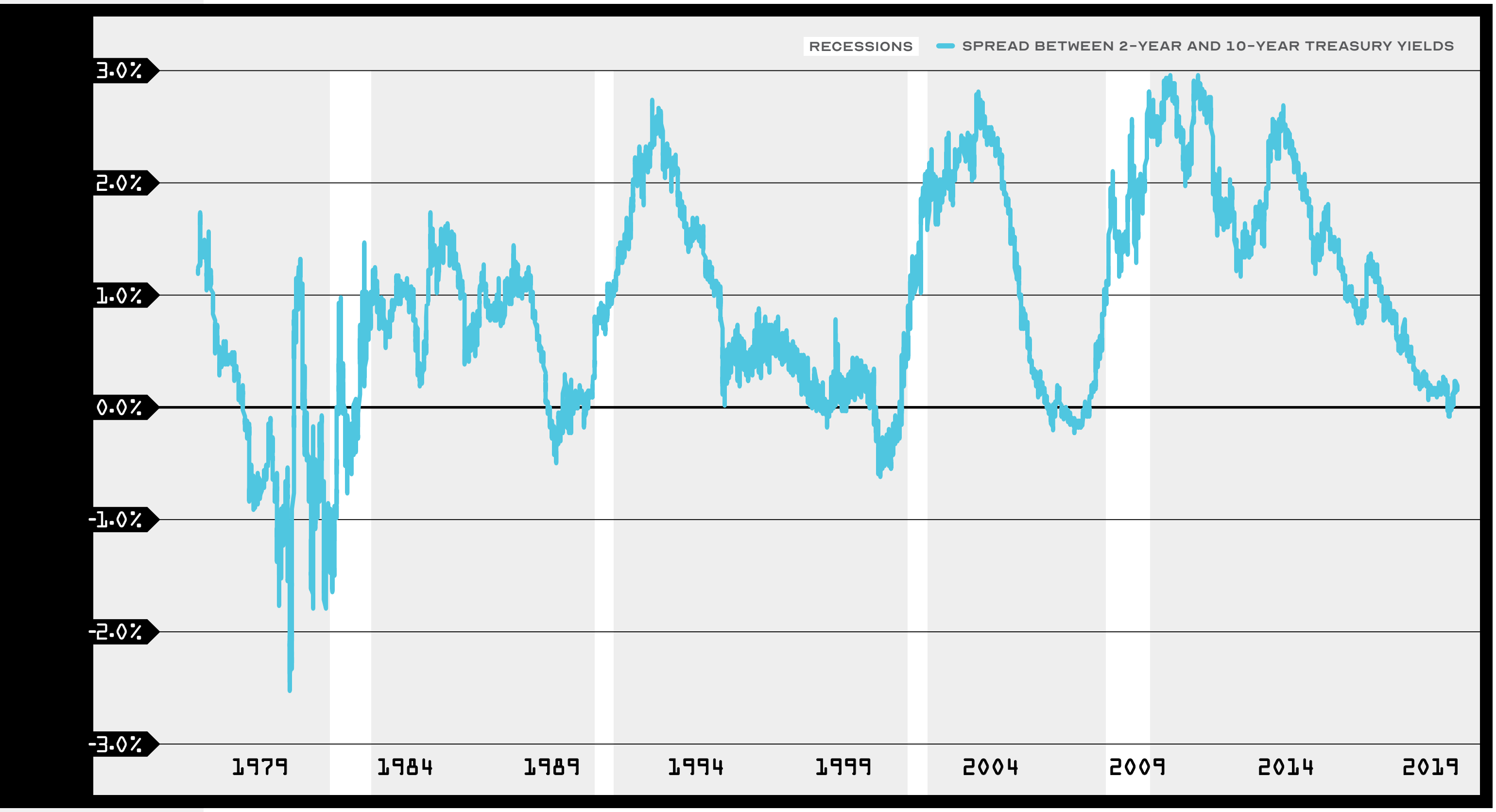
YIELD CURVE SENDS SIGNALS

Typically, economic cycles end as inflation climbs, and the Fed responds by tightening monetary policy, which may lead short-term rates to increase faster than longer-term rates, inverting the yield curve, and threatening recession. In the United States, we've experienced almost the opposite: below-target inflation, an accommodative Fed, a firm U.S. dollar, and falling commodities prices.

Meanwhile, a variety of geopolitical risks have pushed investors looking for a "safe haven" into U.S. Treasuries*, particularly international buyers facing negative sovereign-debt yields, even as U.S. economic fundamentals remain sound and the U.S. budget deficit continues to rise. As a result, recent yield curve inversions have been characterized by long-term rates falling faster

FIG 006

SHORT-LIVED YIELD CURVE INVERSION IS LESS WORRISOME



Past performance is no guarantee of future results.

Source: LPL Research, Bloomberg 11/01/19

* U.S. Treasuries may be considered "safe haven" investments but do carry some degree of risk, including interest rate, credit, and market risk. They are guaranteed by the U.S. government as to the timely payment of principal and interest and, if held to maturity, offer a fixed rate of return and fixed principal value.

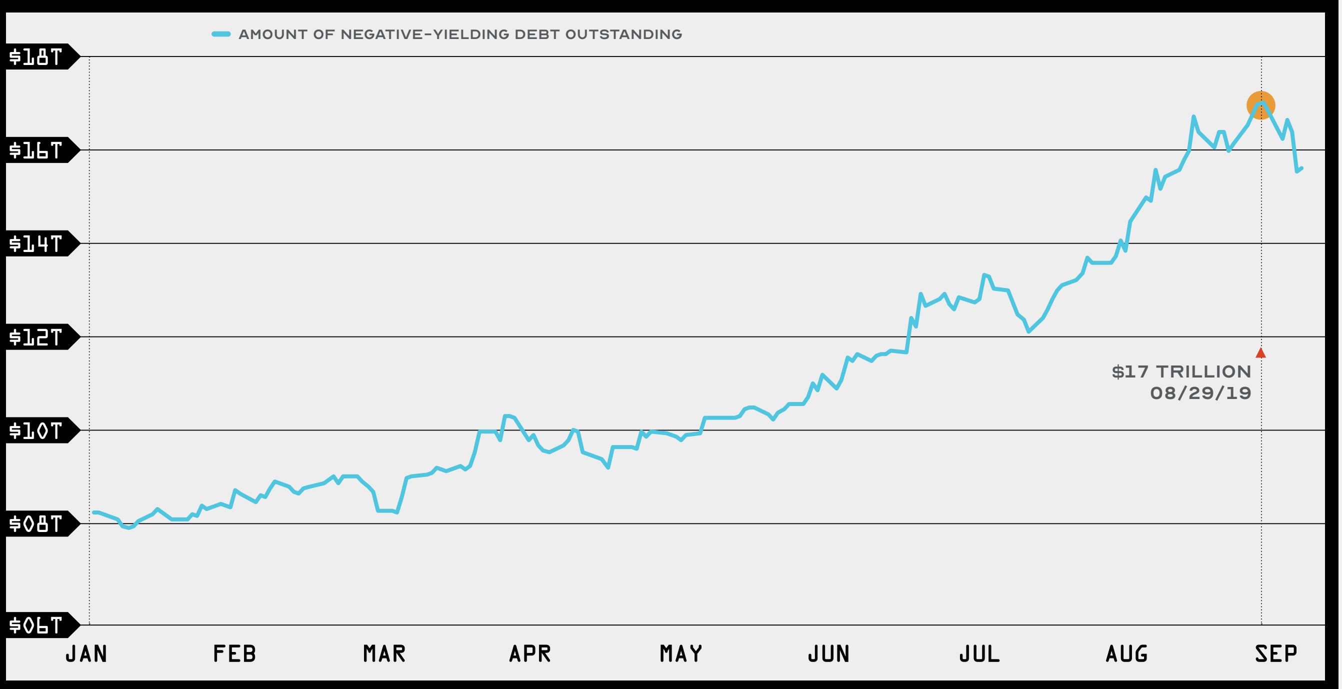
than short-term rates, increasing investor fears of an impending recession **[FIG.6]**.

In the last three economic expansions, a recession began about a year after the 2-year/10-year yield spread inverted for 90 consecutive days. Since the spread between the 10-year Treasury and 2-year Treasury yield has been negative only occasionally in the latter portion of 2019, we suspect the message really was that Fed policy is too tight for ongoing trade uncertainty. An extended inversion, however, would send a different message about expected economic activity. The steepening of the 2-year/10-year yield curve back into positive territory during the fall months is an encouraging sign.

While the August 2019 inversion was due in part to prospects of slowing economic growth, we think the unusual rate environment has made the signal less

FIG
007

NEGATIVE-YIELDING DEBT HAS CLIMBED



Source: LPL Research, Bloomberg 10/31/19
Negative-yielding debt is measured by the Bloomberg Barclays Global Agg Negative Yielding Debt Market Value USD Index.

meaningful than it has been in the past, and we would take even the modest steepening that we expect in 2020 as supportive of continued economic expansion.

GLOBAL RATES GO NEGATIVE

Negative interest rates internationally have been one of the most perplexing developments in the markets in recent years [FIG.7]. When interest rates are below zero, the lender, in theory, pays the borrower for the “privilege” of providing the loan. While we have concerns about how these rates normalize over time, we do not believe that process will begin anytime soon, and we continue to view central bank actions as supportive for markets right now.

European and Japanese rates may stay negative until growth and inflation in those economies pick up; however, with the benefits of monetary policy largely exhausted, that may take a while. The gap between U.S. and international yields likely will remain wide and potentially could get wider, keeping upward pressure on the U.S. dollar. At the same time, further potential rate cuts by the Fed and other economic and market forces may keep the dollar in balance overall.

THE GAP BETWEEN U.S. AND INTERNATIONAL YIELDS LIKELY WILL REMAIN WIDE, KEEPING UPWARD PRESSURE ON THE U.S. DOLLAR.

LOOKING AHEAD

The Fed is currently in wait-and-see mode as it gauges the impact of its 2019 rate cuts, which can take time to flow through to the real economy. Growth in line with our outlook would not necessarily require any further cuts, although muted inflation does give the Fed more flexibility. More than one cut would likely signal more serious concerns about economic deterioration. Continued Fed flexibility should provide enough support to the economy to foster a modest increase in longer-term yields. Our year-end 2020 forecast for the 10-year U.S. Treasury yield is a range of 2–2.25%.

We continue to emphasize a blend of high-quality intermediate bonds in tactically oriented portfolios for fixed income allocations. Despite expectations of modestly higher long-term rates (which can push bond prices lower), the "coupon" income that bonds provide would still leave the broad Bloomberg Barclays Aggregate Bond Index with the potential for low-single-digit gains while providing likely diversification benefits if stocks falter.

Slowing but near-trend economic growth could support corporate profits and companies' ability to service their debt, but moderate inflationary pressure could offset these benefits for corporate bond investors. We continue to recommend a cautious approach to this more credit-sensitive segment, but a "coupon-clipping" environment, where returns are largely driven by bonds' interest payments, may still aid suitable investors, and we are comfortable with benchmark-like exposure to investment-grade corporate bonds.

U.S. Treasuries appear richly valued, but the yield advantage over international government bonds and expectations of only modest rate increases argue against a significant underweight compared with benchmarks for these traditional portfolio diversifiers. For suitable investors, mortgage-backed securities could act as a source of yield that may be better suited for modestly rising rates, and valuations have become more attractive relative to other high-quality bonds.

With the yield curve fairly flat, longer-term bonds do not provide much additional return potential from coupon payments, and we continue to recommend that investors hold fixed-income portfolios with less interest-rate sensitivity than the broad Bloomberg Barclays U.S. Aggregate Bond Index in appropriate strategies.

20/200 20/100 20/70 20/50 20/40 20/30 20/25 20/20 20/15 20/13 20/10

STOCKS WIDE OPEN

PROGRESS ON TRADE COULD HELP STOCKS IN 2020.

CORPORATE EARNINGS GROWTH has slowed considerably in 2019, as the impact of the 2018 tax cuts created a difficult year-over-year comparison, global economic growth slowed, and tariffs and trade uncertainty weighed. Further progress on the U.S.-China trade conflict in early 2020 could help keep U.S. economic growth at or above the trend for the current economic expansion and support corporate revenue growth. We believe any small steps forward on trade could increase business confidence and spark capital investment, lifting corporate profits.

The United States and emerging markets still stand out to us as relatively more attractive investment opportunities than developed international markets, based in large part on relatively stronger outlooks for economic growth and corporate profits.

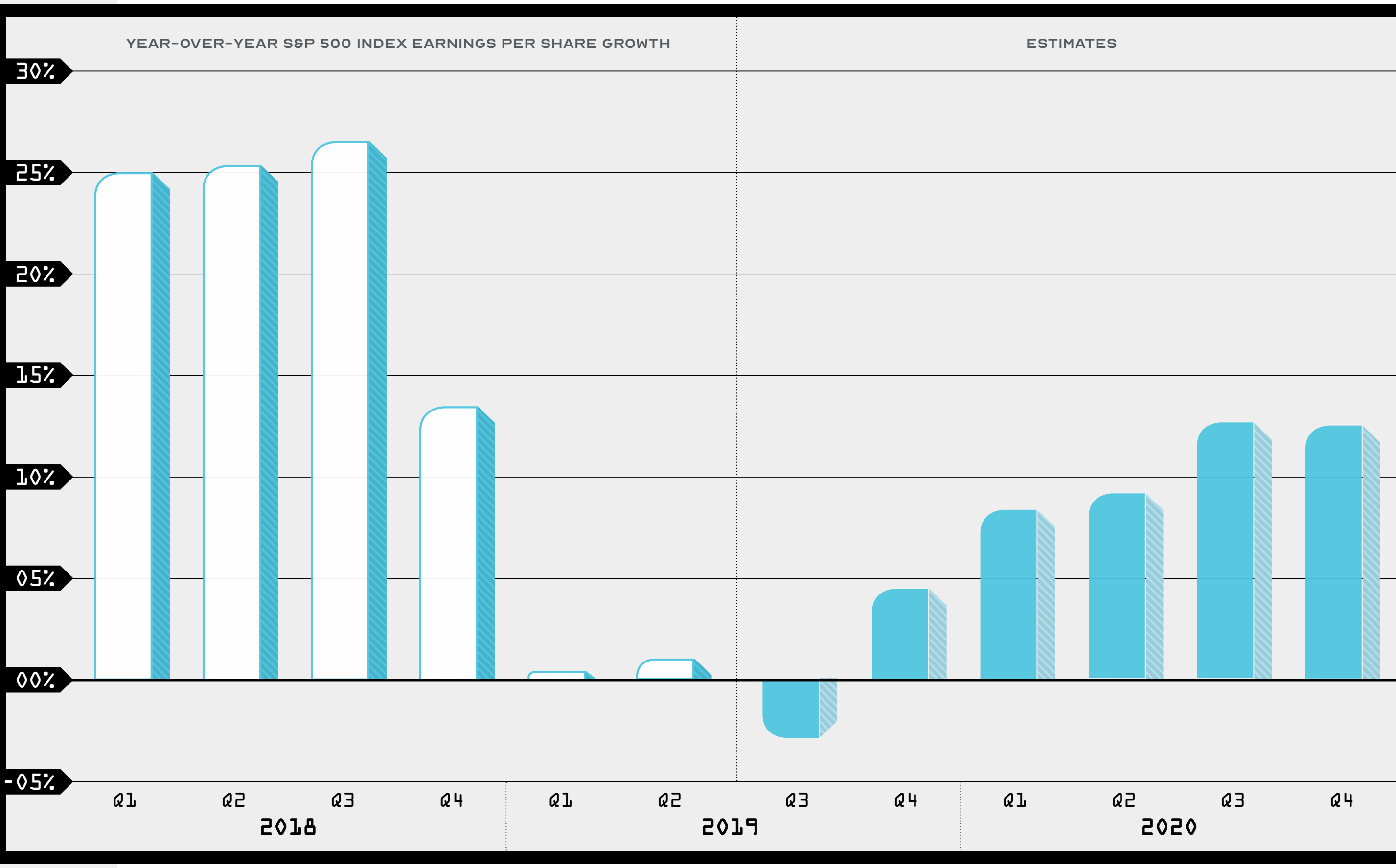
LOOKING AT EARNINGS AND REVENUE GROWTH

Our 2019 S&P 500 earnings per share (EPS) forecast is $165, which we lowered in August due to increased risk to economic growth and profits from the U.S.-China trade conflict **[FIG.8]**.

The current geopolitical environment makes forecasting 2020 earnings very difficult, but our base estimate is $175, which represents a mid-single-digit increase from our 2019 estimate. Roughly $4 below current consensus estimate (Source: FactSet), our forecast assumes further progress on

FIG 008

U.S. EARNINGS GROWTH IS POISED TO ACCELERATE IN 2020



Estimates reflect FactSet consensus. The economic forecasts may not develop as predicted.

Source: LPL Research, FactSet 10/31/19

trade that keeps U.S. economic growth near the trend of this expansion and reduces the tariffs burden. Until we have clarity on trade, we would not expect 2020 earnings to improve meaningfully from 2019 levels.

That said, we expect prospects for better earnings growth in 2020 will help support stocks at current valuations.

Our 2020 year-end fair value target range for the S&P 500 is 3,250–3,300. We base this year-end target on a trailing price-to-earnings ratio (P/E) of 18.75, which we multiply by our 2020 S&P 500 EPS forecast of $175. We believe mild inflation and still-low interest rates support these valuations.

GLOBAL PROFITS

In one sense, the outlook for global profits follows the pattern of economic growth, with the United States and emerging markets

on top [FIG.9]. We expect S&P 500 earnings growth in 2020 most likely will outpace that of Europe (MSCI Europe Index) and Japan (MSCI Japan Index), consistent with FactSet consensus estimates.

EMERGING MARKETS: Assuming there is progress on trade, earnings for the MSCI Emerging Markets Index is expected to rebound solidly in 2020, with the consensus estimate (FactSet) calling for a 14% increase. That pace is nearly triple the forecast for Japan (5%) and ahead of Europe (9%) and the United States (10%). A possible double-digit increase in emerging markets' earnings could be attractive to global investors, although disappointing earnings growth in these regions in recent years has been a concern. We still believe a modest allocation to emerging markets equity makes sense in appropriate strategies.

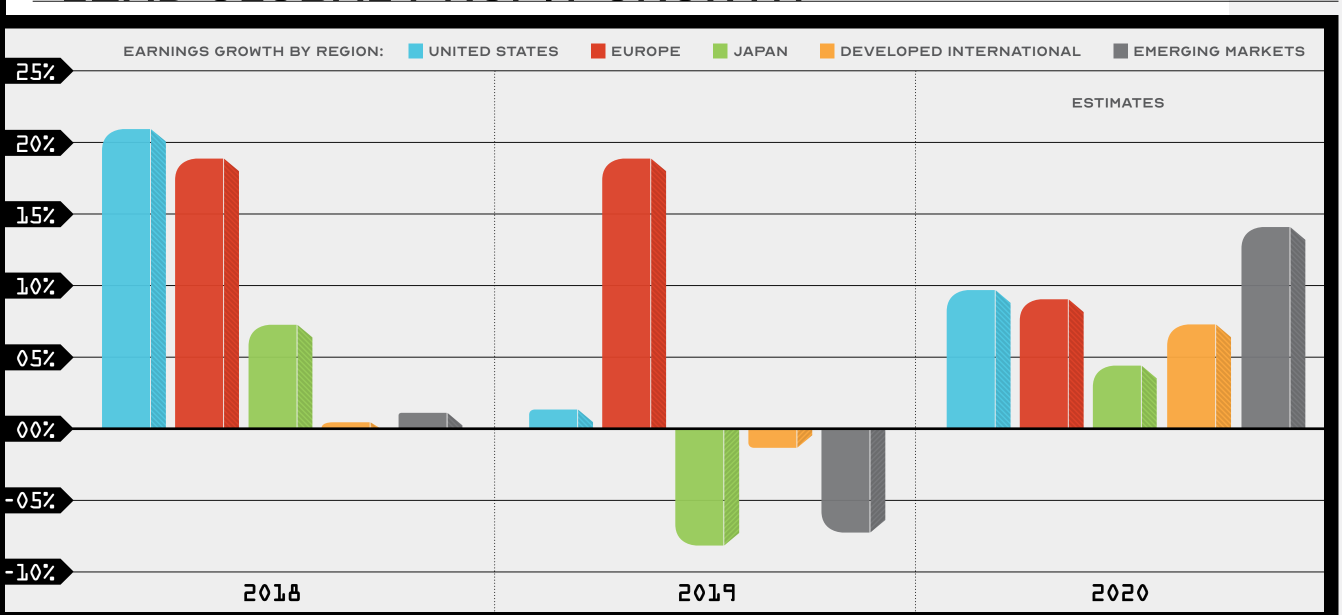
DEVELOPED INTERNATIONAL: Our concerns about global policies, economic growth, and interest rates drive our cautious outlook for developed international equities. Despite relatively attractive valuations, we see a number of challenges in developed markets that lead us to maintain our tactical underweight to the asset class. With the impact of any further monetary policy support likely to be muted, a coordinated move toward pro-growth fiscal policy would be needed for us to become more bullish on these regions.

UNITED STATES: We recommend tactical investors consider focusing the majority of their equities allocations here at home as U.S. economic growth expectations have held up well compared with global trends. We recommend a balance of growth and value styles, with an emphasis on large cap stocks over their small cap counterparts as the business cycle moves into its latter stages.

We continue to prefer cyclical sectors as the U.S. economic expansion continues, and technology still leads this bull market. We expect industrials to benefit from a potential pickup in capital spending if there is further progress on a U.S.-China trade agreement. The challenging interest rate environment prevents us from a more positive view of the financials sector for now. Opportunity may be emerging in healthcare stocks, which have fallen to attractive valuations due to heightened policy risk ahead of the 2020 election.

FIG 009

U.S. AND EMERGING MARKETS MAY LEAD GLOBAL PROFIT GROWTH



Source: LPL Research, FactSet consensus 10/31/19
Data represents S&P 500 Index, MSCI Europe Index, MSCI Japan Index, MSCI EAFE Index, and MSCI Emerging Markets Index.
The economic forecasts may not develop as predicted. 2020 data is based on FactSet consensus estimates.

OUR VIEW

AS 2019 DRAWS to a close, the U.S. economy is still exhibiting some positive fundamentals despite trade uncertainty and slowing global growth. Consumer spending remains strong, supported by low unemployment, steady wage growth, contained inflation, and low interest rates. At the same time, the age of the economic expansion has led to questions about how long it can continue. U.S. manufacturing weakness has become more pronounced. Signals from the global bond market are confusing. Earnings growth has stalled in the United States and internationally, and due to heightened geopolitical risks that must continue to be monitored, companies are lacking the visibility they need to make sound decisions about long-term investments. Clarity on trade needs to come sooner rather than later, as we prepare for a highly charged and likely divisive U.S. presidential campaign. We can't see into the future, but we hope this guide can help improve your view into the new year. Welcome to 2020.

20/200
20/100
20/70
20/50
20/40
20/30
20/25
20/20
20/15
20/13
20/10

Elections

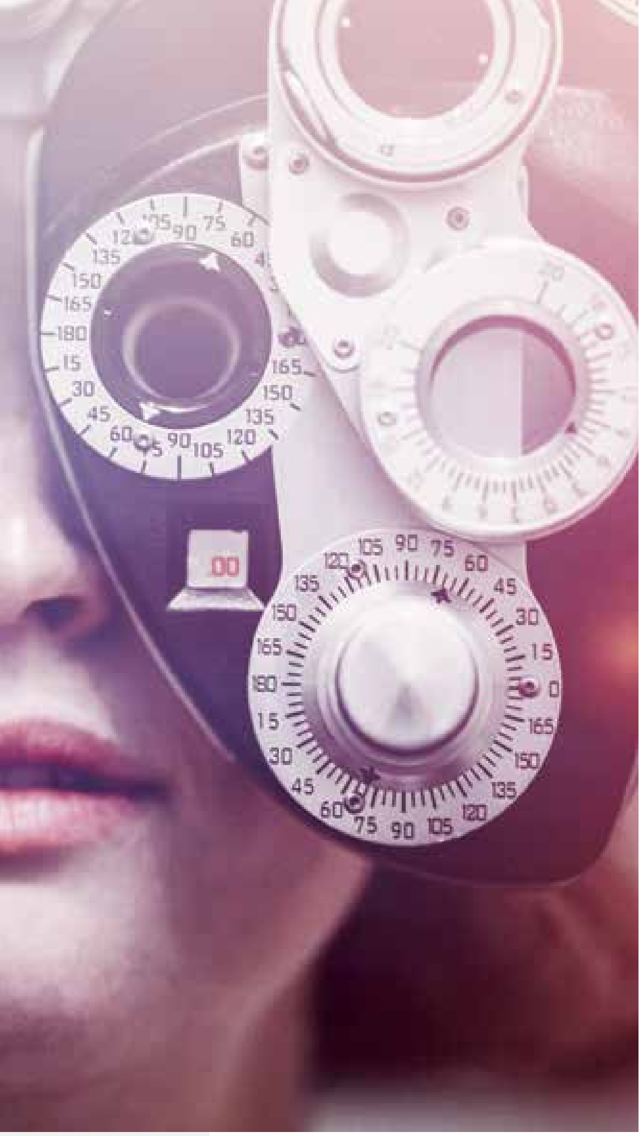
VISION 2020

WE LOOK AT HOW THE MARKETS MAY IMPACT—AND BE IMPACTED BY—THE 2020 U.S. ELECTIONS SEASON.

IT'S EARLY, but policies of the leading presidential candidates are beginning to take shape. We've listed some of the key policy issues that may influence markets in 2020 and beyond.

TRADE POLICY: Resolving trade concerns with China maintains bipartisan support, so we expect any administration to continue to be tough on China. Tensions could de-escalate if tariff threats are pulled back, depending on leadership; however, we would expect trade to continue to be emphasized as a policy tool.

TAXES: The *Tax Cuts and Jobs Act of 2017* has not been popular with all members of Congress, so we expect corporate tax rates could be adjusted and other programs from the law changed, depending on who wins the White House. Individual tax rates on the wealthy also could be targeted, although a "wealth tax" as currently proposed by some candidates would have difficulty gaining



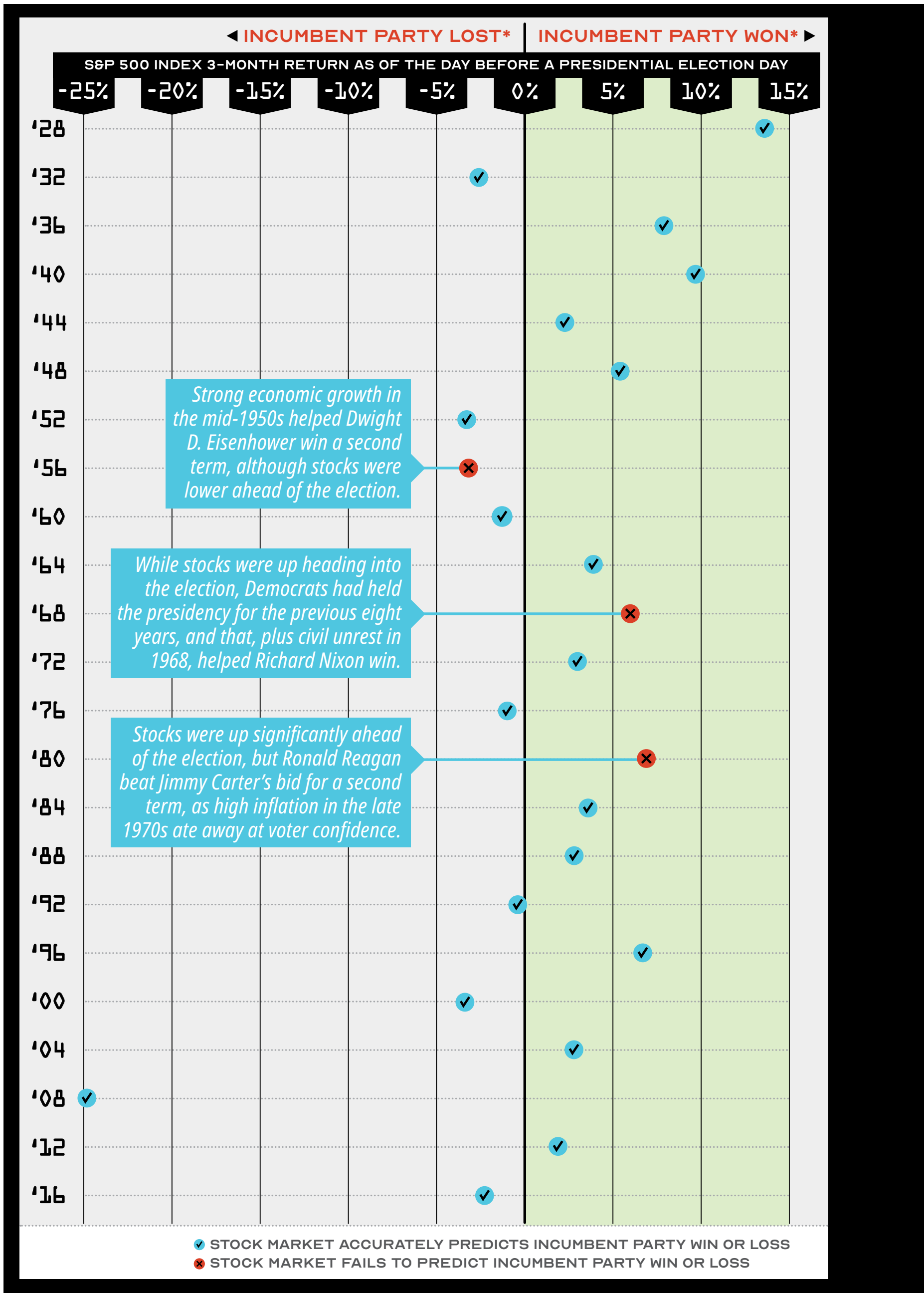
traction in Congress, regardless of who controls the chambers.

HEALTHCARE: A shift in which party controls the Senate could have consequences on healthcare spending and the substance of the *Affordable Care Act*. Drug-price regulation may be coming regardless of which party is in power. We anticipate that Medicare expansion will be a hot topic no matter what, and those debates could lead to increased volatility in the healthcare sector, particularly for health insurers.

FINANCIAL SERVICES REGULATION: It's possible we could see additional government regulation of the financial services industry after the elections, depending on the winners, with the potential for new proposals to raise capital requirements or to put pressure for more reforms on regulatory agencies. Proposals for more regulation would cause an increase in compliance costs for many financial services firms.

CAN STOCKS PREDICT THE NEXT PRESIDENT?

Our 2020 elections chart shows S&P 500 Index performance for the three months prior to every presidential election all the way back to 1928, when Herbert Hoover was elected. The chart shows that when the S&P 500 was in the green three months before the election, the incumbent party tended to stay in the White House. If stocks were down, this potentially signaled an upcoming change in power in the White House. The track record isn't perfect—it missed in 1956, 1968, and 1980—but in 20 of the last 23 presidential elections, stocks have been correct.



Source: LPL Research, Strategas Research Partners 07/15/19
The modern design of the S&P 500 stock index was first launched in 1957. Performance back to 1928 incorporates the performance of predecessor index, the S&P 90. All indexes are unmanaged and cannot be invested into directly. Past performance is no guarantee of future results.

*EXCEPT IN 1956, 1968, AND 1980

IMPORTANT DISCLOSURES

The opinions, statements, and forecasts presented herein are general information only and are not intended to provide specific investment advice or recommendations for any individual. It does not take into account the specific investment objectives, tax and financial condition, or particular needs of any specific person. There is no assurance that the strategies or techniques discussed are suitable for all investors or will be successful. To determine which investment(s) may be appropriate for you, please consult your financial professional prior to investing.

Any forward-looking statements including the economic forecasts herein may not develop as predicted and are subject to change based on future market and other conditions. All performance referenced is historical and is no guarantee of future results.

References to 'Markets,' 'Sectors,' and 'Stocks' herein are generally regarding the index tracking the corresponding asset class. All indexes are unmanaged and cannot be invested into directly. Unmanaged index returns do not reflect fees, expenses, or sales charges. Index performance is not indicative of the performance of any investment.

All information is believed to be from reliable sources; however, LPL Financial makes no representation as to its completeness or accuracy.

RISK DISCLOSURES

Investing involves risks including possible loss of principal. No investment strategy or risk management technique can guarantee return or eliminate risk in all market environments.

Investing in stock includes numerous specific risks including the fluctuation of dividend, loss of principal, and potential illiquidity of the investment in a falling market. Because of their narrow focus, sector investing will be subject to greater volatility than investing more broadly across many sectors and companies. Value investments can perform differently from the market as a whole. They can remain undervalued by the market for long periods of time. The prices of small and mid-cap stocks are generally more volatile than large cap stocks.

Bonds are subject to market and interest rate risk if sold prior to maturity. Bond values will decline as interest rates rise and bonds are subject to availability and change in price. Bond yields are subject to change. Certain call or special redemption features may exist which could impact yield. Government bonds and Treasury bills are guaranteed by the U.S. government as to the timely payment of principal and interest and, if held to maturity, offer a fixed rate of return and fixed principal value. Corporate bonds are considered higher risk than government bonds but normally offer a higher yield and are subject to market, interest rate, and credit risk, as well as additional risks based on the quality of issuer coupon rate, price, yield, maturity, and redemption features. Mortgage backed securities are subject to credit, default, prepayment, extension, market, and interest rate risk.

Investing in foreign and emerging markets debt or securities involves special additional risks. These risks include, but are not limited to, currency risk, geopolitical risk, and risk associated with varying accounting standards. Investing in emerging markets may accentuate these risks.

There is no guarantee that a diversified portfolio will enhance overall returns or outperform a non-diversified portfolio. Diversification does not protect against market risk.

DEFINITIONS

Gross Domestic Product (GDP) is the monetary value of all the finished goods and services produced within a country's borders in a specific time period, though GDP is usually calculated on an annual basis. It includes all of private and public consumption, government outlays, investments, and exports less imports that occur within a defined territory.

The P/E ratio (price-to-earnings ratio) is a measure of the price paid for a share relative to the annual net income or profit earned by the firm per share. It is a financial ratio used for valuation: a higher P/E ratio means that investors are paying more for each unit of net income, so the stock is more expensive compared to one with lower P/E ratio.

Earnings per share (EPS) is the portion of a company's profit allocated to each outstanding share of common stock. EPS serves as an indicator of a company's profitability. Earnings per share is generally considered to be the single most important variable in determining a share's price. It is also a major component used to calculate the price-to-earnings valuation ratio.

The Standard & Poor's 500 Index is a capitalization-weighted index of 500 stocks designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries.

Cyclical stocks typically relate to equity securities of companies whose price is affected by ups and downs in the overall economy and that sell discretionary items that consumers may buy more of during an economic expansion but cut back on during a recession. Counter-cyclical stocks tend to move in the opposite direction from the overall economy and with consumer staples that people continue to demand even during a downturn.

A growth stock is a share in a company that is anticipated to grow at a rate significantly above the average for the market due to capital appreciation. A value stock is anticipated to grow above the average for the market due to trading at a lower price relative to its fundamentals, such as dividends, earnings, or sales.

Large-cap stocks are issued by corporations with a market capitalization of $10 billion or more, and small-cap stocks are issued by corporations with a market capitalization between $250 million and $2 billion.

Credit Quality is one of the principal criteria for judging the investment quality of a bond or bond mutual fund. As the term implies, credit quality informs investors of a bond or bond portfolio's credit worthiness, or risk of default. Credit ratings are published rankings based on detailed financial analyses by a credit bureau specifically as it relates the bond issue's ability to meet debt obligations. The highest rating is AAA, and the lowest is D. Securities with credit ratings of BBB and above are considered investment grade.

The Bloomberg Barclays Aggregate US Bond Index represents securities that are SEC-registered, taxable, and dollar denominated. The index covers the U.S. investment-grade fixed rate bond market, with index components for government and corporate securities, mortgage pass-through securities, and asset-backed securities.

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