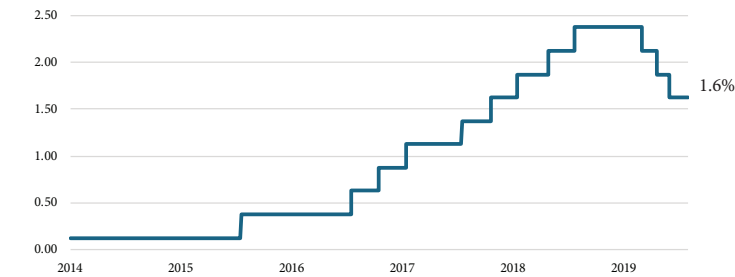


Rarely is there such dramatic change in one quarter. The fourth quarter of 2019 was the exception, with major policy developments in several arenas providing at least partial relief from the tensions festering in the summer. Domestically, the Federal Reserve Board (Fed) reduced its federal funds rate by one quarter of one percent during October, the third reduction since July, cementing the reversal of its raise one year prior. The Fed also committed to redefining its balance sheet once again, allaying fears of a credit crunch in short term investment funding circles. The uncharacteristically bold actions by the Fed signaled that they understood clearly the threats to the financial markets from higher rates and economic slowdowns in Europe and China.

Fed Funds Rate 2014-2019



Source: Factset

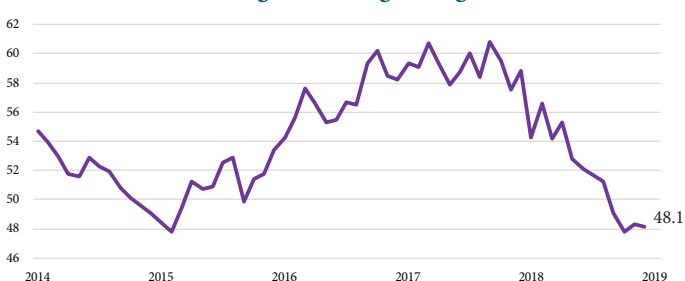
The relaxation of trade tensions signaled that both the United States and China realized spiraling trade restrictions dampen sentiment and elevate uncertainty, hindering capital investment. Whether the détente lasts through the new year remains to be seen but a spirit of cooperation broke out in North America with the recently passed USMCA trade deal between the U.S., Mexico, and Canada.

Foreign governments and central banks took their cues from the Fed. To combat the economic pause experienced in 2019, central banks began expanding their balance sheets again, pumping money into the banking system to induce more investment. In addition, over the past few months, over 60 central banks cut interest rates including Mexico, Russia, Turkey, and Brazil. Interest rate and short-term funding arrangements are perceived to be the quickest method to shore up sagging economies.

The uncoordinated policies had a salutary effect on U.S. markets. Stocks and bonds had their biggest simultaneous gains in over two decades. The S&P 500 returned about 30% for the year and bond prices rose, pushing the yield on the benchmark 10-year Treasury to under 2%. Oil and gold also returned over 10% for the year.

The U.S. economy will remain the primary driver of global growth in the new year, but we anticipate the aggressive central bank actions undertaken in 2019 will bolster growth globally in 2020. Additionally,

U.S. ISM Manufacturing Purchasing Managers Index 2014-2019



Source: Factset

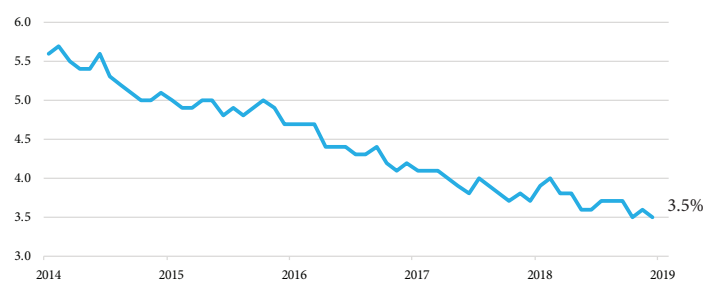
Economic and Market Outlook

First Quarter 2020

low rates and trade policy clarity should benefit the domestic manufacturing sector which surged after the Tax Cut and Jobs Act passed in December 2017 accelerated depreciation timetables. Manufacturing slowed considerably in 2019 as the initial depreciation effects waned and trade policy uncertainties intensified.

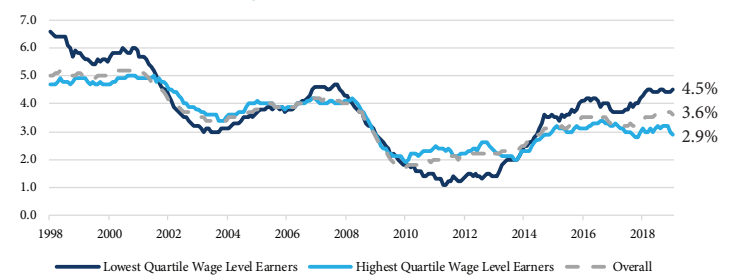
The U.S. consumer has been stalwart throughout the recent slowdown and should continue to provide a solid base from which growth can expand. Robust job creation has thinned the ranks of unemployed and attracted those formerly disengaged back onto the employment rolls. In a rarity, wage growth for the lowest earners has exceeded the growth rate for the top quartile for an extended period of time, reflecting the worker shortage. It is no coincidence that consumer sentiment readings remain at highs with a recent CNN poll reporting 76% of Americans feel the economy is good, the highest reading since 2001.

U.S. Unemployment 2014-2019



Source: Factset

U.S. Wage Growth Tracker 1998-2019



Sources: Current Population Survey, Bureau of Labor Statistics, and Federal Reserve Bank of Atlanta

U.S. Consumer Confidence Index 2009-2019

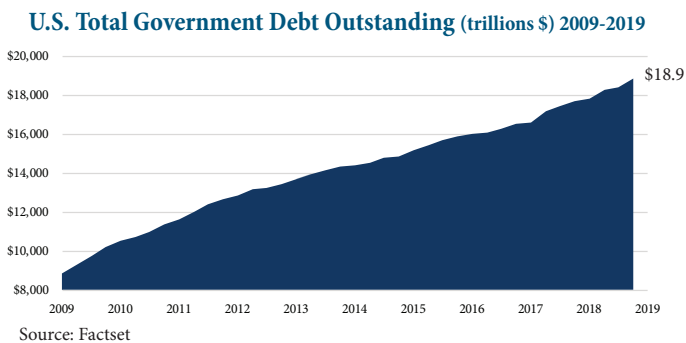


Source: Factset

The extent of central bank interventions would have been unheard of 15 years ago. Certainly, in the U.S., the Federal Reserve Bank is walking a tight rope between a level of growth deemed acceptable to the public and politicians and stubbornly low inflation. The federal government, on the other hand, is not constrained in the same fashion as we head into an election year. In a rare show of cooperation, the government passed the fiscal 2020 budget with

little regard for balancing the budget. Deficits will likely register over \$1 trillion annually over the next two years and should be viewed cautiously looking out a few years.

In addition to fostering growth, low interest rates make accepting debt easier. U.S. corporations remain well capitalized with manageable levels of debt supported by positive cash flow. The U.S. government, on the other hand, is using debt at levels unseen since World War II. Low rates make this possible, but how we manage our public debt in an era of rising rates may well set the tone in five years' time.



As government debt expands, the outlook for interest rates takes on added significance. The Fed's ability to control the federal funds rate does not extend to market controlled longer rates. Inflation, currency fluctuations, and comparative rates play a large part in setting longer rates. For now, inflation remains in check and comparative rates remain lower outside the U.S., maintaining the attraction of the domestic bond market. As 2020 progresses, we expect longer term rates to rise gradually, reflecting an economy growing at a slightly higher level.

In our opinion the outlook for equities is positive. After a strong 2019 however, it is not difficult to postulate a decline in equity values. At the very least a corrective phase seems a reasonable expectation, and inflammatory headlines constantly offer a rationale for things going dreadfully wrong. Headlines make very poor investment strategy. The gain in stock values in recent years reflects fundamental developments, many of them positive for equity valuations. These include the declines in interest rates and inflation, the best job market since the 1960s, technology induced capacity increases and productivity gains, and an improving housing market. Stock values will increasingly

follow their individual company and industry fortunes within a generally favorable overall environment for financial investments.

As we view the worldwide financial condition, we find the view of some that the rise in the price of financial assets represents a bubble about to burst, improbable. At virtually full employment, with rising real income wages, stable interest rates, and placid inflation conditions, the forces underpinning the rise are impressive. Despite political controversies, the United States remains an island of stability and a paragon of growth and opportunity in a destabilized world. This does not mean the coming year will be free of crises and just as in the past three years, sudden and steep corrections will occur. A focus on fundamental and a longer-term horizon will serve investors best in this environment.

Investment Oversight Committee
Daniel A. Lagan, CFA
President & Chief Investment Officer

January 2020



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