Fourth Quarter Report 2019

LUCIEN, STIRLING & GRAY ADVISORY GROUP SM

"Smart Decisions About Serious Money"

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A Message From The President

Thomas G. Twombly

Happy New Year! All of us at Lucien, Stirling & Gray hope 2019 was generous to you in many, many ways, and that 2020 brings you health, prosperity and enough personal challenge and growth to make life interesting and fulfilling.

First, thank you. I feel incredibly fortunate to have been given the opportunity to serve all you clients of this firm who are, to a person, likeable, respectable and friendly. I feel equally blessed to be surrounded by a team of great colleagues who do everything possible to demonstrate just how honest, hard-working, fun-loving, self-effacing and professional they are in caring for your needs. I'm very lucky. It's possible that there are many others out there who feel the same sense of gratitude I do about their professional lives, but I sincerely doubt it. So, thank you all for such a rare and precious gift. I treasure it.

The end of a decade, especially one as disruptive to the apparent order of things as this past one has been, seems like a big moment. It's natural for people to look back and make note of the big events, milestones and turning points that have shaped our collective experience, and you'll find no shortage of reports, articles and opinion pieces being published now that attempt to do just that.

Rather than add to that prodigious pile here, I'd prefer to look forward instead, and with a more personal perspective, to share with you some of the big challenges and opportunities we see coming at us, and at you, over the next 5-10 years. Then we'd like to ask you for your thoughts, your insights, and your candid advice in how we should address them. Your input is very important, so please help us.

Fundamentally, ours is a business about working closely, even intimately, with people. It's about managing expectations, emotions, behaviors and relationships—not just money, investment portfolios and financial plans. There is no automated process, investment algorithm, or software product—no matter how helpful and efficient it might be—that can ever replace the profoundly human need for empathy, trust, confidence and personal connection in doing what we do.

We're acutely aware that to be trusted by others, we must *be* trustworthy. If we are to help our clients move forward in an uncertain world, to make measured decisions in the face of multiple risks and challenges, to endure the inevitable setbacks, and to reap the long-term rewards of diligent planning and investing, we must inspire confidence. To do that, we must have trust and confidence in ourselves. Not the false confidence that we *know* the future, for nobody does—but the authentic confidence that comes from being experienced, battle-tested, prepared to adapt to whatever conditions come our way, and assured that our value is all that it should be going forward. It's here that we'd like your input.

How are we doing? What are we doing well? What are we not doing so well? What should we change? Please give us your candid feedback. If you could offer us just one piece of advice about how to serve your needs, and the needs of other people like you *better* in the coming years, what would it be?

Like many professions, ours is subject to all kinds of on-going disruption. New technologies, artificial intelligence, and aggressive private equity firms with deep pockets are combining in ways not imagined before in efforts to consolidate, streamline and overtake firms without a clear sense of purpose and direction. We're also seeing huge demographic changes in our profession.

Studies I've read indicate that a third of financial advisors in practice today will retire within the next decade. Other studies indicate that half of current advisors have entered the business in the last decade—so they have comparatively little experience, acquired in a largely benign environment. Taken together, these point to a coming shake-up in the expectations and relationships that many clients of advisory firms have today—just when they'll need stability, experience and continuity the most.

We want to provide that stability, experience and continuity—now, and for a long time to come. We're fiercely protective of the fiduciary culture we've built here, and proud of the fact that the senior members of our advisory team have worked together for an average of 16 years. At the same time, we're intent on growing, changing, adapting, bringing new talents and capabilities aboard and making sure we're constantly cross-pollinating between the wisdom of the old guard and the talents of the new.

The famous Irish playwright George Bernard Shaw once said, *"we are made wise not by recollections of our past, but by the responsibility for our future."* I believe we're also made wise by seeking candid advice from trustworthy clients and friends, and by listening carefully to their perspective and counsel, because they care about our well-being and they have a vested interest in our continued success.

In the coming months, as we meet with you and talk over the telephone, we hope to get your considered perspective on some of the issues and questions I've raised above, as well as other insights I'm sure will arise out of thoughtful conversations.

Thank you again for your confidence and trust.

Thomas G. Twombly
President

Investment Commentary

What a difference a year makes. At the writing of this report 12 months ago, investors, business leaders and politicians alike were struggling with deep frustration and anxiety over a government shut-down that seemed to have no definitive end. Due to the furlough of all the government employees that compile and report such things, there was a dearth of reliable financial and economic data on which many of those people rely. In other words, lots of the gauges on many crucial dashboards weren't working well, and the drivers were getting a little worried.

Additionally, rising tensions over tariffs and trade disputes between the U.S. and China at the end of 2018 were rattling nerves around the globe, and the U.S. Federal Reserve had recently completed its third and final announced tightening of interest rates in the United States. All these issues contributed to substantial uncertainty. Interest rates were rising, credit markets were stressed, stock markets sold off quite sharply in the final quarter, and all asset classes except cash, municipal debt and short-term bonds (which collectively offered only meager total returns of between +1.4% and +1.8% for all of 2018) experienced losses for the year. Gloominess was abundant, and both asset flows and anecdotal evidence suggest that not a small number of people reacted fearfully in the final weeks of 2018, fleeing to cash and missing out on many of the gains of subsequent months.

By the end of 2019, by contrast, enthusiasm reigned supreme. All the eight major asset classes rose by margins that ranged between +7.7% and +31.5%. It was extraordinary. In fact, according to one report we read, it was the first time since 1972 that every single one of those asset classes rose by more than +5%, and the median annual gain of +20% was the highest since 1982.

Leading the pack were large-cap U.S. stocks, with total returns of +31.5%. Several other widely held asset classes also turned in above-median results, contributing substantially to overall results for the broadly diversified portfolios our clients own. REITs rose by +28.7%, small-cap U.S. stocks by +25.5%, and Developed Market International stocks by +22.7%.

On the below-median side of results for the year, though hardly to be sniffed at, were Emerging market equities, which provided total returns of +18.9%, High-yield bonds of +12.6%, the Barclay's Aggregate Bond Index of +8.7% and commodities of +7.7% for the year. Again, these resulted in very attractive overall gains for investors in broadly diversified portfolios and proved the value of patience, a disciplined approach and a long-range view in the prudent allocation of capital.

Looking ahead, and given the attention and the flow of assets that the S&P 500 is attracting from many investors in what is now becoming an increasingly ebullient environment, we believe it's worth noting here some of the internal data behind its impressive rise in 2019. We mention this not as a note of alarm, but as a nod towards continued situational awareness and sobriety, and a constant reminder of the wisdom of remaining sufficiently diversified among other asset classes going forward.

The technology sector alone, which currently represents 23.2% of the weight of the index, rose by an astounding +50.3% in 2019, and accounted for fully one third of the overall gains of the index. Apple rose by +88% in 2019; Microsoft by +59%; and Facebook by +57%. The financial sector was also a strong contributor, with gains of +32.1%. JP Morgan Chase provided total returns of +46%; Bank of America +46%; Mastercard +59% and Visa +43%.

As a capitalization-weighted index, additional asset flows will increasingly be directed towards companies and sectors that have the largest weights in the index, resulting in ever more concentration. While exciting on the way up, it can be particularly painful when markets inevitably retreat at some point.

We have, and will continue to maintain, healthy allocations to U.S. stocks. There has always been a very dynamic business environment in this country and there are many companies and industries that continue to innovate and grow at compelling rates. At the same time, we're also conscious that there are many other great businesses domiciled outside the United States too. And as the chart below demonstrates (see page 4), relative to the high valuations now found in the U.S., those markets have never been cheaper than they are now.

Looking forward, the balance of economic and geo-political risks and opportunities is evolving as always. The big trade-related risks between the U.S. and China appear to be abating for the time being, and manufacturing growth is stabilizing. Central banks remain accommodative in their monetary policies, but after three rate cuts in 2019 the Federal Reserve looks much less likely to provide any additional stimulus moving forward. Consumer spending is solid and will likely continue to grow as unemployment stays near record lows of 3.5% and wages continue their gradual rise. But with the top 10% of income earners claiming slightly more than 50% of pre-tax national income, but spending only 69% of their after-tax income, according to JP Morgan, that growth rate will likely remain slow. At the same time, new worries are rising to the surface, including new tensions in the Middle East and on-going drama surrounding impeachment proceedings in the United States – and of course the specter of a very tense political climate and uncertain outcomes as we march steadily towards the November election.

In closing, the first quarter of the year is always a good time to review your overall financial situation. Additionally, there have been some recent changes to retirement plan rules and regulations with the passage of the SECURE Act in the final days of 2019 that are worth discussing with one of us. If you haven't already done so, we encourage you to schedule some time for a review and a conversation sometime soon. We are still housed in temporary space until sometime around the end of February as we await the completion of our permanent home across the hall, but as long as you don't mind cement floors and a somewhat rustic setting, we're fully functional and will happily welcome you in.

We look forward to addressing any issues and concerns you have, and we hope you'll come prepared to share your insights and advice with us, too.

Chart 5: US stocks at 70-year highs versus global stocks

Source: BofA Merrill Lynch Global Investment Strategy, Global Financial Data

General Market Results

	4th Quarter	YTD	One Year	Three Year	Five Year	Ten Year
Barclays Agg Bond	0.18	8.72	8.72	4.03	3.05	3.75
S&P 500	9.07	31.49	31.49	15.27	11.70	13.56
DJI	6.67	25.34	25.34	15.73	12.59	13.40
S&P 400	7.06	26.20	26.20	9.26	9.03	12.72
Russell 2000	9.94	25.52	25.52	8.59	8.23	11.83
NASDAQ	12.47	36.69	36.69	19.86	14.93	16.05
MSCI EAFE	8.17	22.01	22.01	9.56	5.67	5.05
MSCI EM	11.84	18.42	18.42	11.57	5.61	3.68

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