FIRST QUARTER 2020 MARKET OUTLOOK

Our Outlook

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<tbody>
<tr>
<td>GDP Growth (1)</td>
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<tr>
<td>Change in Consumer Prices (2)</td>
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<tr>
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<td>5-Year Treasury Yield (3)</td>
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<td>10-Year Treasury Yield (3)</td>
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<tr>
<td>S&amp;P 500 EPS</td>
<td>$133</td>
<td>$161</td>
<td>$164</td>
<td>$171</td>
<td>$181</td>
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</tbody>
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(1) 4th quarter/4th quarter (2) December/December (3) Year-end rates

Security National Bank’s Wealth Management Department maintains an economic forecast that provides our Investment Committee and the Bank’s Funds Management Committee background assumptions for use in investment decisions. We are pleased to share our economic outlook with you. Please be advised our crystal ball is just as clouded as other prognosticators and that all forecasters have a poor track record.

2019 was a turbulent year: the Federal Reserve Board (FRB) raised interest rates four times in 2018 and promised to continue raising them at the start of 2019, the global economy continued to slow, the trade war with China intensified, Brexit became even more messy, protest erupted against the political establishment in Hong Kong, Lebanon, Chile, Ecuador and other places, and climate change became a major investing and social issue. Recession worries dominated the airwaves. The stock market experienced a mid-year swoon of seven percent. Despite all the bad news, both equity markets and bond markets had a stellar year.

We believe 2020 will also be turbulent. Every year is turbulent. The 24-hour news cycle demands and creates turbulence. At Security National Bank we attempt to look past the noise and hype. While the U.S. will eventually experience a recession, it is unlikely to enter into one in 2020. As seen in the chart above, we remain cautiously optimistic.

Markets in Review
The fourth quarter of 2019 was almost a mirror image of the previous year’s final quarter. In 2018’s final quarter, the S&P 1500 posted a 13.97% loss with small-capitalization stocks falling over 20%. In 2019’s fourth quarter, the broader index posted an 8.92% total return.

Prepared by Damian Howard

January 10, 2020

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The turnabout was primarily driven by a pronounced pivot by the Federal Reserve Board. In 2018, the FRB raised rates four times and promised additional rate hikes. In 2019, the FRB reversed course and cut rates three times and has promised to keep rates steady for the foreseeable future.

The stock market is probably in an overbought condition. We would not be surprised to see a 5% to 10% sell-off, especially after the FRB stops its overnight lending operations. We anticipate that this sell-off could happen sometime early in the second quarter. A 5% to 10% market correction is standard and occurs almost every year. Excess liquidity and rebounding global growth should limit the correction to historical ranges.

The U.S. stock market, as measured by the S&P 1500 SuperComposite, rose 8.92% in the fourth quarter bringing the 2019 total return to 30.90%. As evident from the chart below, the stock market has had a great decade with a total annualized return of 13.52%. This is well above the long term average of 10.68% total return (Jan 31, 1928 to Jan 7, 2020).

| Annualized Total Return for S&P1500 SuperComposite |
|---------------------------------|---------------------------------|---------------------------------|---------------------------------|---------------------------------|---------------------------------|---------------------------------|---------------------------------|
| One Year                        | Three Year                     | Five Year                       | Seven Year                      | Ten Year                        | Fifteen-Year                    | Twenty Year                     |
| 30.90%                          | 14.65%                         | 11.46%                          | 14.52%                          | 13.52%                          | 9.07%                           | 6.44%                           |

Financial Services was the best performing sector last quarter, posting a 10.47% total return. Financials were closely followed by Healthcare and Information Technology, posting total returns of 14.37% and 14.40% respectively. The worst performing sector last quarter was real estate which lost 0.54%.

Value stocks underperformed growth stocks during the quarter, 9.93% versus 8.32%. Year-to-date, value stocks are slightly ahead of growth stocks performance-wise 31.93% versus 31.13%.

Emerging markets posted a solid 11.84% return for the quarter, followed by 8.17% of non-U.S. developed market stocks. 2019 was a great market for just about every asset class, including cash with U.S. large-capitalization stocks leading the way.

| Asset Class Returns |
|---------------------|---------------------|---------------------|---------------------|---------------------|---------------------|---------------------|
| Large Cap US Stocks | Small-Cap US Stocks | Developed Market Stocks | Emerging Market Stocks | High Yield Debt | Investment Grade Debt | Commodities |
| 2019 31.5%          | -11.0%             | 22.7%               | 18.9%               | 12.6%             | 8.7%               | 7.7%               |
| 2018 -4.4%          | -13.4%             | -14.2%              | -4.1%               | 0.0%              | -11.2%             | 1.8%               |

Security National Bank’s Outlook at a Glance

US economic growth remains steady. Economic growth is likely to be 1.9% in 2020. This is slightly less than the 2.2% estimated growth for 2019. Monthly job growth is likely to slow from the current pace of 200 thousand new jobs per month to about 125 thousand per month by the end of the year. The housing sector is improving, thanks to lower rates. Corporations continue to invest in intellectual property. The consumer remains strong with solid income growth and a stable balance sheet. All of this will continue to produce modest economic growth. We believe the odds of a recession in 2020 are less than 25%.
The Federal Reserve will remain on hold in 2020. The current Fed funds policy rate is 1.50% to 1.75%. Inflation will remain under control. Interest rates will remain low and accommodative. Global interest rates may rise, but only marginally. Bonds should provide modest coupon like returns. U.S. fiscal and monetary policies are on hold until 2021 at the earliest. Outside of the U.S., monetary and fiscal policies remain supportive of faster growth.

Global disruptions from trade disputes have likely peaked. The marginal benefit to further escalation is minuscule. The mini-trade deal with China will not provide material relief or change Chinese behavior. The majority of tariffs will remain in place. US importers will continue to alter supply chains to deal with this new reality, a bi-polar global economy; a U.S. centric global economy and a Chinese centric one. Europe will unsuccessfully try to straddle the two.

During periods of modest economic growth, investors pay a premium for stocks that can generate company-specific growth in excess of modest economic growth. We believe 2020 will again be a period of modest economic growth. Value stocks have historically outperformed during periods of very strong or very weak economic growth. The current economic environment favors our investment philosophy.

Our equity investment philosophy is best characterized as growth at a reasonable price which searches for companies that are showing consistent growth in sales and earnings and consistently earn a return on capital greater than their required return. We also seek to buy these companies at a reasonable discount to estimated fair value. We focus on secular stock picking versus cyclical stock picking and invest in companies that can prosper through the economic cycles. We target companies that we would be willing to hold for a decade or more.

The stock market is trading at 18.7 times our 2020 earnings estimate. This is two and a half points above the long term average of 16.1. The low rate environment and a possible bottoming of global growth support a higher than normal market premium. Stocks are expensive but that does not mean a correction is imminent. There is little correlation between the market P/E and subsequent short term results. However, the current premium gives us pause. In addition, technical indicators point to an overbought market.

Earnings for the S&P 500 are likely to remain flat year over year in 2019. For 2020, we think earnings will grow by about 4%. Current Wall Street estimates call for earnings to grow about 10% next year. This is too high. Expectations are likely to be reset after companies announce fourth-quarter results and give forward guidance. This expectation is widely held and unlikely to cause major market disruption.

Investors should expect modest returns for 2020 of mid-single digits. This is below recent results and the long term average. We would not be surprised to see a 5% to 10% market sell-off around April. The FRB has been adding extra liquidity to stabilize the overnight lending market. As they wind up this temporary support, the stock market may experience some volatility. A 5% to 10% correction is normal and happens most years. Please don’t be surprised to see one early in the second quarter.
Since 1977, the Federal Reserve has operated under a mandate from Congress to “promote effectively the goals of maximum employment, stable prices, and moderate long-term interest rates” – what is now commonly referred to as the Fed’s “dual mandate.” For this reason, we always start our economic review with employment followed by inflation. We then review other factors that drive our economic outlook.

Employment
The December Jobs Report was somewhat weaker than expected. The headline number was below consensus and the two prior months were revised down. The unemployment rate held steady, matching the lowest level since 1969. The average hourly earnings growth rate rose less than 3% y/y. The report will have a limited impact on FRB policy.

The Labor Department released its latest Employment Situation (Jobs) Report on January 10th. The labor market added 145 thousand jobs in December compared to expectations of 160 thousand new jobs. Wages
First Quarter 2020 Market Outlook

grew 2.9% y/y. The unemployment rate held steady at 3.5%. The broader U-6 rate fell to 6.7% and the participation remained at 63.2%.

The U.S. economy added 145 thousand jobs last month. The previous two months total was revised down by 14 thousand jobs for a net 131 thousand jobs added. The household survey showed a gain of 267 thousand jobs. In total, 158.8 million people are working versus 156.8 million last year at this time. The working-age population is 260.2 million. There remain 5.8 million people unemployed versus 7.3 million job openings according to the JOLT report.

To smooth out some of the revisions, we also looked at the trailing three-month averages. The trailing three-month average job growth was 184,300 versus a revised 200,300 last month and 233,300 last year. The broader U-6 measure fell to 6.7% from 6.9% last month and is down from 7.6% last year. This measure includes part-time workers who would prefer a full-time position and people who want a job but are not actively looking for one (so-called “discouraged workers”).

Both the establishment and the household survey estimated that the economy added about 2.0 to 2.1 million jobs over the last twelve months. The number of employed individuals has increased by 1.3% over last year. At the same time, the working-age population has grown by 1.3 million or 0.5%. New entrants into the labor pool account for less than half of new jobs. The remainders of the new jobs are filled by people re-entering the labor market. The participation rate (percent of working-age people in the labor market) has increased from 62.7% to 63.2% in the last two years. A one percent increase in the labor force participation rate equates to 2.6 million jobs. Currently, the economy is creating 1.2 million jobs per year more than the growth in the working-age population. This allows for faster economic growth than would otherwise be possible and is a highly efficient way to grow.

Last month’s average hourly earnings (wages) grew at a 2.9% y/y rate down from the revised 3.1% last month and down with a 3.3% last year. This is the first time wage growth slipped below 3.0% since September of 2018. There is a good possibility that this number will be revised higher in the coming months.

The average work-week held steady at 34.3 hours versus last month but is down from last year’s 34.5 hours. Average weekly earnings are up 2.3% from last year to $971.40 ($50,512 annualized) versus $949.80 ($49,389 annualized) last year. Wage growth remains remarkably under control. Studies have
shown that wage growth is tightly tied to inflation expectations. As seen below inflation expectations remain well contained.

The labor market is in good shape. Job growth continues to exceed growth in the population as more people re-enter the labor force or enter it for the first time. Wage growth is controlled in the 3.0% to 3.5% channel. Job growth above this baseline is proof of the flexibility in the U.S. labor market, accommodative monetary and fiscal policy and a strong economy.

**Inflation**
The consumer price index was up 0.3% in November following a 0.4% increase in October, led by gains in energy, medical care (especially health insurance) and housing. The price index is up 2.0% y/y and the trailing six month period. This indicates inflation has stabilized at the FRB’s 2.0% target. Core inflation is 2.3%. The main driver of inflation is shelter. Shelter inflation is 3.3% y/y. All items less shelter inflation is 1.4%.

Owners’ Equivalent Rent (OER) is up 3.3% y/y. This category has been remarkably steady at 3.1% to 3.5% for the last couple of years. Based on housing data, OER is likely to be the chief source of inflation for the foreseeable future. Changes in the supply and demand for housing occur at a glacial pace. Small changes in interest rates are not going to slow rent increases dramatically. In those markets hit by a housing shortage, changes in land use and zoning will make a bigger impact.

The FRB prefers the Personal Consumption Expenditure (PCE) as its measure of inflation. Due primarily to differences in how health care costs are allocated between employers and consumers, the PCE tends to run 0.25% to 0.50% below the CPI. In November, the PCE was up 0.2% and is up 1.5% y/y. The core PCE was up 1.6% y/y. The PCE excluding energy was up 1.6% y/y.

Consumers and investors base their financial decisions on what they expect inflation to be in the future. We can measure inflation expectations from the difference between a 10-year Treasury security and the ten year Treasury Inflation Protection security (TIPS). The difference implies what market participants expect inflation to average over the next ten years. As evident in the chart above, inflation expectations stabilized at 1.7% +or- 0.1% since August 2019. Currently, market participants expect inflation to average 1.74% over the next ten years. This is right in line with current inflation, indicating a steady inflation outlook.
Inflation is currently at the FRB’s inflation target and looks to remain there for an extended period of time. An inflation overshoot or deflationary spiral is not evident. The primary driver of inflation is now housing cost. Lower interest rates may marginally increase the supply of apartments by reducing an already low cap rate, but the constraining factors of labor availability and land use laws cannot be changed by interest rate policy. We look for PCE inflation to hover around 1.5% to 2.0% for a while. The FRB has a symmetric target which means inflation has to run above target to make up for the decade of low inflation before it will raise rates to combat it.

The Consumer Sector

Personal income growth was strong in November, up 0.5% versus the consensus estimate of 0.3%. Personal income is up 4.9% over the past year. Private sector wages were up 0.4% in November and are up 5.7% from last year. Disposable personal income is up 4.6% y/y. Disposable personal income per capita is up 4.0% y/y. Real disposable income per capita is up 2.5% y/y. Growth at this level significantly enhances the overall standard of living. It is doubtful that the economy will fall into a recession with such strong income growth.

Consumer spending on goods and services is up 3.9% from last year. Consumers saved 7.9% of disposable income. Consumer credit is up 4.8% y/y. Consumer credit is growing slightly faster than nominal GDP (3.6%) but in-line with disposable income (4.6%). At this controlled rate of growth, consumers can handily service the additional debt. Overall, the consumer’s balance sheet remains in good shape.

In general, consumers continue to feel pretty good about their current situation. They are growing a bit apprehensive when looking at the future, in part, due to ongoing trade tensions and political wrangling.

Consumer confidence as reported by the Conference Board fell slightly in December. The headline index fell to 126.5 from a revised 126.8 the previous month. November’s report originally pegged consumer confidence at 125.5. The slight downtick may have more to do with timing. The cut-off date for the survey was December 13th. This was prior to an announced Phase 1 trade deal averting a host of tariffs on consumer goods. The index has remained essentially flat for four straight months. For reference, the average reading over the last twenty years has been 93.
The present situation component, based on consumers’ assessment of current business and labor market conditions, rose to 170.0 from 166.6 the previous month. It remains significantly above its twenty-year average of 101. Clearly, consumers are feeling good about how the economy is today. Consumers have a slightly dimmer view of the future.

The expectations component, based on consumers’ short-term outlook for income, business and labor market conditions, fell to 97.4 from a revised 100.3 the previous month. The reading, while down, is well above its twenty-year average of 87. The expectations component is most sensitive to market sell-offs, trade tweets, dower economic forecast, and political theater.

The sub-components of the present situations component fell modestly. The net appraisal of current employment opportunities being plentiful (easier to obtain) rose to 33.9 from 31.6 the previous month. Consumers continue to feel good about the labor market. Consumers’ net perception of current business conditions (good less bad) also rose to 27.6 from 25.2 the previous month.

We look for consumption to mirror the growth of disposable income, about 3.5% to 5%. It does not appear that consumers have an appetite to significantly lever-up their balance sheets. This is good. Excesses are not building in the consumer sector. It is highly unlikely that the consumer will be the source of the next downturn. Look for consumer-related stocks to outperform stocks of companies that rely on corporate spending for growth.

The Business Sector
The Institute for Supply Management’s (ISM) non-manufacturing index rose 1.1 points to 55.0 from 53.9 the previous month and was better than expected (54.4). The reading marks the 119th consecutive month of economic growth in the service sector. The Index indicates growth in the service sector in December quickened a bit and is indicative of a 2.2% GDP growth rate. The Institute for Supply Management stated “(t)he respondents are positive about the potential resolution on tariffs. Capacity constraints have eased a bit; however, respondents continue to have difficulty with labor resources.”

Business activities/production and supplier deliveries are growing at a faster rate. New orders and employment are growing at a slower rate. The inventory sentiment index increased 1.5 points to 60.0. This indicates inventories are still too high and getting worse. Prices for purchased materials and services held steady at 58.5 indicating input prices are rising at a steady pace. The backlog of orders index contracted for the fourth time in the last five months. Eleven of eighteen industries indicated growth in December. Six industries contracted.

As a frame of reference, a reading above 50 indicates expansion; a reading below 50 indicates contraction. Readings approximating 50 indicate the same level of activity. A manufacturing PMI above 42.9 generally indicates an expansion of the overall economy.
The U.S. manufacturing sector continues to contract. Manufacturing is the sector most exposed to slower global economic growth, trade frictions, and a pause in non-intellectual property capital spending. Non-U.S. manufacturing appears to have bottomed. Non-U.S. manufacturers entered the downturn earlier than U.S. counterparts and appear to have turned the corner a bit sooner than domestic manufacturers. The global supply chain is slowly shifting production of U.S. bound products out of China into Vietnam, Mexico and other Southeast Asian countries.

The Manufacturing Index fell to 47.2 from 48.1 the previous month. This marked the fifth consecutive month of contracting activity and was well shy of consensus of 49. It also marks the ninth straight month of a weakening industrial sector and was the lowest reading since June 2009. New orders, production, employment, and inventories are contracting.

Out of the 18 manufacturing industries only three reported growth and 15 reported contraction. Comments from the survey panel were consistent with the prior month “Global trade remains the most significant cross-industry issue, but there are signs that several industry sectors will improve as a result of the phase-one trade agreement between the U.S. and China. … Overall, sentiment this month is marginally positive regarding near-term growth.” The manufacturing continues to contract. The manufacturing index generally corresponds to 1.3% GDP growth, slower than our forecast but in line with our cautious view of the industrial sector.

Industrial production was up 1.1% in November, its largest monthly gain since 2017. Automotive production was up 12.7% as General Motors recovered from the recent strike. Even excluding automotive production, manufacturing was up 0.5%. Year over year, industrial production is still down 0.8%, automotive production is flat and production of high tech goods is up 7.4%.

The NFIB Small Business Optimism Index rose 2.3 points in November to 104.7, historically a very solid reading. 7 out of 10 Index components expanded. “November reflects a stark departure from the previous clatter months earlier about a possible recession that dampened owners’ economic outlook. The constant drumbeat of news reporting on the topic generated some concern among small business owners reflected in September’s drop in optimism. But as in the late 90s, a strong economy appears to prevail political disruptions when there is little effect on policies impacting the economy or small business sector. What really matters to small business owners are the issues that directly impact their business. And right now, the biggest problem is finding qualified labor to fill open positions for 26 percent of owners, far more than those citing taxes or regulations. Two years ago, Congress and the President provided real,
significant tax relief to small business owners. Now owners are anxious to have their tax cuts made permanent, so Congress needs to get back to work.”

The JPMorgan global all-industry PMI moved up 0.2 points to 51.7 in December, a level consistent with 2.6% global GDP growth. The December service PMI moved up 0.5 points to 50.1. The manufacturing PMI fell slightly to 50.4 from 51.0 the previous month. The manufacturing PMI is consistent with weak global industrial production growth.

Overall, it appears the global business sector is on the mend. The U.S. economy should grow about 2.0% + or - 0.2%. Global economic growth should quicken slightly next year.

The Housing Sector
The housing sector has returned to being a source of economic strength and growth. With mortgage rates down a full percent and income up strongly, the housing sector should continue to be a positive catalyst for economic growth.

New single-family home sales rose slightly in November to a 719 thousand annual rate up 17% from the prior year’s 615 thousand pace. The single-family home sales report is based on small samples, tends to be volatile, and is often revised significantly. This makes it unwise to rely on data from any single month for the big picture. To even out the volatility, we use a rolling three-month average. November’s trailing three-month trend was also up a strong 21% y/y. Single-family housing starts have also increased at a healthy pace.

The median selling price rose 7% to $320 thousand with the trailing three-month average down 1% y/y. New home construction has shifted from the expensive coastal regions to the more affordable South and Midwest. In addition, home builders are selling more cheap models and entry-level homes in an effort to boost affordability. Existing home price appreciation has been decelerating, mirroring new home prices.

Higher incomes, moderating home prices and lower mortgage rates have combined to increase affordability. With better affordability, the housing market has returned to growth mode. Economics continues to hold true: left to its own devices, markets self adjust. When prices were too high relative to income, consumers pulled back.
Now that prices are more in line with income, housing has gone from a detractor from growth to a contributor to growth. During the third quarter, residential construction increased economic growth by 0.2%, marking only the second quarter in the last ten quarters that residential construction added to economic growth. We look for housing to continue to add to economic growth in the coming quarters.

Oil
The U.S. trade deficit fell in November to $43.1 billion, the smallest since 2016. Buried in the details of the report is that for the third month in a row, the dollar value of U.S. petroleum exports exceeded the dollar value of petroleum imports. The U.S. is once again a net petroleum exporter. Horizontal drilling and fracking has transformed the global oil markets.

The U.S. Energy Information Administration (EIA) expects U.S. crude production to average 13.2 million barrels per day (mbpd), an increase of 0.9 mbpd from the 2019 levels. Despite a lower rig count, U.S. production continues to grow as rig efficiency and well-level productivity rises. Increased non-OPEC production, led by the U.S., will more than offset any planned OPEC production cuts. In order to keep prices from crashing, OPEC + Russia will concede additional market share to the U.S. The EIA continues to expect inventory to build as global production outstrips consumption. In the U.S. gasoline stockpiles have built for nine straight weeks and are 5% above the five-year average.

Despite ever-increasing production, not all is rainbows and butterflies in the oil patch. The significant improvement in efficiency is weighing on employment growth. The Federal Reserve Bank of Dallas doubled its estimates for job losses this year through Oct in the oil and gas industry of Texas. The FRB Dallas now expects job losses of around 8,100.

After briefly hitting $63 per barrel following the missile attack on the Iranian General Soleimani, oil prices have returned to their recent range. Research has shown that the most accurate forecast for oil prices is no change in prices. This forecast significantly outperforms the collective effort of professional oil forecasters. The average target price as tracked by FactSet is for WTI to end 2020 at $56.99. This is a bit lower than the current price of $59.97. The futures curve supports a $54.00 to $58.00. We have a no-change forecast of $58.00 for year-end 2020.
The Yield Curve and International Interest Rates
The current Fed Funds policy range is 1.50% to 1.75%. Fed Funds futures are pricing in no change for the next six months. We contend that the FRB is on hold for an extended period of time. The traditional measure for recession watching has been the 10-year minus the 2-year yield curve. After a brief flirtation with an inverted curve, the curve is slightly positive (29 basis points). The yield curve points to slow economic growth.

While still negative, German bond yields have risen since early September. The differential between German and U.S. yields has also narrowed by about 0.50%. The narrowing will take some of the downward pressure off U.S. rates and also help lower the dollar.

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<th>GDP Growth</th>
<th>Inflation</th>
<th>Unemployment</th>
<th>Interest Rate on Government Debt</th>
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<tr>
<td>United States</td>
<td>2.1%</td>
<td>2.0%</td>
<td>3.5%</td>
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<tr>
<td>United Kingdom</td>
<td>1.1%</td>
<td>1.5%</td>
<td>3.8%</td>
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<td>Germany</td>
<td>0.5%</td>
<td>1.5%</td>
<td>3.1%</td>
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<tr>
<td>Japan</td>
<td>1.9%</td>
<td>0.5%</td>
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<tr>
<td>China</td>
<td>6.0%</td>
<td>4.5%</td>
<td>3.6%</td>
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Trade Weighted Dollar
The index is down 0.31% over the last six months but up 1.6% over the last year and up 5.7% over the last five years. At the end of 2019, the U.S. dollar traded below its 50 day and 200-day moving average. We are not technical traders but have been advised this is a bearish signal for the dollar. Technical indicators and a narrowing of yields differentials do set the stage for a weaker dollar. Some market commentators have forecast a significantly lower dollar for 2020. We are not in that camp. We look for the dollar to remain stable to weaken slightly. The dollar’s value should not be a material factor in S&P 500 earnings or in our asset allocation decisions. We do not foresee a dollar weak enough to cause us to increase our allocation to non-U.S. assets. We are mindful that it is a risk we bear.

We welcome your comments and suggestions. Please feel free to contact me at dhoward@snbomaha.com. Also, please see the obligatory disclosures listed below.

Prepared by Damian Howard
January 10, 2020
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