Madison FUNDS®

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UPDATE

FALL 2019

ECONOMIC REVIEW

Witnessing daily stock market action this past summer was a bit like being stuck in stop-and-go traffic. To extend the metaphor, the constantly changing tariff situation was like a randomly switching stoplight. Take August, for instance. Half of the month's trading days ended with an up or down move of more than 1%; ten days were negative and twelve were positive. Despite an August dip of -1.6%, the year-to-date return remained a robust 18.3% on August 30. (Market data is quoted for the S&P 500® Index)

The overall mood of investors was cautious, with investment flows into the relative safety of bonds pushing down yields to recent lows. One marked result was the inversion of the 2-year to 10-year yield curve in August, with the shorter end out-yielding the longer end, a relatively unusual situation which can presage a recession. However, this type of inversion is a notoriously unreliable predictor of recessions. Balancing the yield curve concerns were the positive signs from early economic indicators, with the exception of the Purchasing Managers' Index (PMI), a manufacturing index which dipped just below 50, the tipping point for an economic slowdown. However, the manufacturing sector is particularly sensitive to the tariff situation, and the on-again, off-again promises of settlement produced widespread uncertainty and suppressed business sentiment and capital spending in general. The signs of an economic slowdown were stronger overseas, where PMIs have been below 50 for some time despite pedal-to-the-metal central bank policies in Europe and Japan.

The Federal Reserve (Fed) seemed to be committed to working against these trends with a quarter-percentage rate cut in July. The consensus belief was that another cut was almost a sure thing in September, with more cuts likely over the next six months. With inflation under control, the Fed's action is seen as a preemptive move to keep the economy moving forward against the drag of tariffs and soft international economies, which include a tariff-scarred China and a Europe stealing for the uncertain consequences of Britain's scheduled October 31 exit from the European Union.

Stock investors gravitated towards safe harbors in August, with the only positive sectors coming from the defensive Consumer Staples, Utilities and Real Estate Sectors. As a possible harbinger of risk-conscious markets ahead, high-quality stocks had a considerable performance advantage over more speculative issues in August.

Consumer sentiment and spending was one of the bright spots these past months, although affluent spending showed weakness, as seen in soft luxury sales and an increase in inventory in high-end housing. Meanwhile, the rest of the U.S. consumer market seemed unaffected by the jittery markets or the percolating price increases that follow increased tariffs. While consumer spending remains a critical part of domestic GDP (Gross Domestic Product), at around 70%, there are reasons to question its staying power. While wages ticked up at a rate slightly higher than inflation so far this year, and overall unemployment remained low, the quality of these jobs has been diminished by the steady shift from higher-paying industrial and manufacturing jobs to those in the service sector. Median wage growth increased only 0.3% a year between 2007 and 2018, while household expenses have not been contained – healthcare premiums are up 55% over the same period. One result has been the rising trend line of consumer debt, with the sobering statistic that the average net worth of the bottom 50% of American households by wealth is now negative. Another suggestion of the strain at this level is the boom in dollar stores, which provide household items in smaller quantities, producing a lower check-out bill. All of which suggests that any sort of economic shock would leave a large number of Americans in difficult straits.

While the headlining of the inverted yield curve created a wave of concern, the fact is that even when a recessionary period followed an inversion, it was typically only with a considerable delay. History shows that this latent period has been strong for stocks. As a result, it seems imprudent for us to make any precipitous allocation moves at this time. Stock investors have benefited from a considerable, long-lasting bull market since 2009 and we keep those gains in mind as we remind ourselves that over time the stock market has produced positive returns two-thirds of the time (for the S&P 500, since inception).

The Purchasing Managers' Index (PMI) is an index of the prevailing direction of economic trends in the manufacturing and service sectors. It consists of a diffusion index that summarizes whether market conditions, as viewed by purchasing managers, are expanding, staying the same, or contracting.
Past performance is no guarantee of future results.

NEWS YOU CAN USE

Individual Retirement Account (IRA) and Education Savings Account (ESA) Annual Fee.

If you are an IRA or ESA account holder, a payment coupon is included with your quarterly investor statement to remit your annual administration/custodial account fee.

This fee supports the additional services required by the custodian to maintain such accounts (e.g. tracking of contributions and mandatory reporting to the Internal Revenue Service). If you have not already paid your fee for 2019, please return the enclosed payment coupon with your check no later than December 2, 2019. If we do not receive your payment by the due date, we will automatically redeem sufficient shares from your account to pay the fee in mid-December.

Individual Retirement Account (IRA) Required Minimum Distributions (RMD).

The Internal Revenue Service requires you take an annual distribution from your IRA account(s) once you reach the age of 70½. The deadline for the first distribution is delayed until April 1st following the calendar year in which you reach age 70½. Consequently, if you will be 70½ on or before December 31, 2019, you must take your 2019 required distribution no later than April 1, 2020. If you are already taking required distributions, the deadline to take your RMD for 2019 is December 31. If you have any questions regarding your distribution status, or need assistance calculating your RMD amount, please contact your financial adviser or call Shareholder Services at 1-800-877-6089.

Capital Gains.

Just a reminder that mutual funds are required to distribute fund capital gains annually to shareholders. Distribution rate projections will be available on madisonfunds.com in early December. If there are distributions to be paid, they will be declared to shareholders of record in December.

Notice Regarding Escheatment.

What does "escheatment" mean?

The term relates to unclaimed property that transfers over to the state in which the property owner lives. Besides the term escheatment, the phrases "abandoned" or "unclaimed" property may be used.

Prevent your account(s) from being deemed "abandoned" by periodically maintaining contact with us. State unclaimed property laws require Madison Funds to turn over an account's assets to the state it's registered under if one or more of the following occurs over a period of time (typically three to five years):

- You have an invalid address on your account
- You have not initiated contact with us
- You have an uncashed check

Establishing contact with Madison Funds is easy.

Call us at 1-800-877-6089 or visit madisonfunds.com and access your account online. We will capture this activity and consider it "contact". You can learn more about abandoned property and "escheatment" in the Funds' prospectus.