

To say that the past six months have been a bit of a roller coaster for investors, is quite an understatement. While Q4 of 2018 produced the worst quarterly result in the S&P 500 since the Great Recession over a decade ago, the first quarter of 2019 was conversely the best since 2009. From negative 13.5%, to positive 13.65%, the ride was stomach-churning and anxiety-ridden, but (like all roller coaster rides) pretty much ended up in the exact same spot as before.

When we examine the economic conditions that persist, it is unsurprising that the market has rallied recently, as not a whole lot has changed in the actual data between the beginning of the downturn in October 2018 and today. Despite a gloomy February (owing partly to the government shutdown), the labor market remains robust, with the unemployment rate holding steady below 4 percent and wage gains running above 3 percent for the sixth straight month, roughly double the inflation rate. Similarly, though manufacturing activity in the US has deteriorated slightly, it remains above expansionary levels and when measured against the global backdrop of slowing growth, the US shines.

Perhaps the biggest change in the last six months is the Fed's reversal, or at least halting of, their projected interest rate policy. The Fed's January meeting revealed their expectations to hold rates steady and removed language indicating further near-term rate hikes. This was a significant development, buoying the anxious equity markets and driving long-term bond yields sharply lower. The Fed's move significantly diminishes the chances of a near-term slowdown, as credit conditions remain healthy and economic visibility for businesses and investors is improved.

One headline that has garnered much attention recently is the so-called yield curve inversion: the outcome of the yield on the 10 year US Treasury being lower than that of the 2 year. Typically, this scenario has been a fairly reliable indicator of a pending recession, as it signals that investors have more confidence in growth in the short-term, than they do in the long run. While it is absolutely true that we have enjoyed an extraordinarily long period of economic expansion and that there are signs of softening in consumer spending, manufacturing activity, housing and global growth, we see this current yield curve inversion as an artificially created condition. Short-term rates have been anchored at levels set by the Fed, yet long-term rates are reflecting a technical and fundamentals driven trade, as investors search for yield in the fixed income markets, where, on a global scale, yields on US debt remain attractive. Among the world's main developed economies, only Italy offers higher rates on their long-term debt and several nations, including Germany, Japan and Switzerland, actually offer negative current yields.

Therefore, in surveying the outlook for the remainder of 2019, we just don't see the necessary indicators for a recession. Instead, we continue to believe that the US economy will grow at a modest rate (perhaps decelerating slightly) and now that the equity markets have recovered to pre-Q4 levels, we expect that returns will be in line with this pattern. Do not mistake this outlook as complacency, as there are certainly developments that we will be watching closely which could change our view. However, if anything, these past two quarters have reaffirmed our confidence in the long-term, methodical approach that we have long advocated for.