BULLS&BEARS

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Impending Flu or Simply Sniffles?

The officials at the Centers for Disease Control and Prevention (CDC) have estimated that, through the middle of March, approximately 30 million people have contracted some form of the flu, including hospitalization of over 400,000 and over 40,000 deaths. It has also been suggested that, even though peak flu season normally ends in February, flu activity this year may extend into May. These results are in spite of increased coverage for vaccinations. Given these statistics, it is somewhat understandable that we become more sensitive to potential flu warning signals. In the workplace, at school, etc., we have an increased tendency to use preventative techniques, such as hand-washing or avoidance, if we perceive that others around us may be infected. Or, we'll increase our intake of vitamin C and even stay home at the first sign of the sniffles. Unfortunately, if we have actually contracted the illness, our only option is to attempt to mitigate the symptoms going forward.

At the last FOMC meeting this March, the Federal Reserve surprised markets by not only leaving target interest rates alone, but by also indicating that it will not raise rates any further this year. Until recently, its assumption was that it would raise rates two times this year. In addition, the Fed also indicated that by September it would stop shrinking its balance sheet through the sales of fixed income securities. These actions were welcomed by equity markets, but are they suggestive of a Fed that is reading some of the recent economic data as more than "the sniffles?"

What Are Some Symptoms?

Concerns "across the pond" have been raised about a potentially bad breakup in the notable Brexit debate. While the end result is still uncertain, the process has the potential to negatively impact not just Great Britain, but the whole of Europe as well. Any negatives caused by Brexit would amplify weaknesses already appearing in European manufacturing data. A similar weakness of manufacturing data is being noticed in the U.S. as well. The addition of these concerns to a more accommodative leaning Fed and other yellow flags have helped lead to a flattening of the yield curve. That is, basically all U.S. Treasury rates up to ten years recently coalesced within a few hundredths of a percent around 2.45%. Some pundits are already suggesting that a flattening or declining yield curve is more than just a canary in the coal mine for an economic recession.

Sanguine or Skittish?

As far as the yield curve/recession debate goes, we're not quite convinced that the yield curve flattening is as predictive as it once was. For one thing, U.S. rates are still pretty attractive to overseas investors… the 10-year U.S. Treasury rate was recently at 2.43% compared to -0.02% (yes, that is a minus sign) for the comparable German government bond. Elevated purchases by international investors would tend to lower rates at the long end of the curve. In any case, if the predictive power is still there this time around, the yield curve indicator has historically "predicted" recessions one to two years in advance. So, at this point, our modest level of caution is based on an economy transitioning from a period of high growth to one of more modest growth. Markets would be expected to be more uncertain/volatile during the transition, but the recession story in the U.S. can be delayed for now. Thanks for reading.

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Market Indicators

3//19	Year-to-Date Change
S&P 500	12.18%
NASDAQ	12.51%
Russell 2000	15.40%

Interest Rates	3/25/19	12/31/18
10-Year Treasury Note	2.43%	2.68%
3-Month Treasury Bill	2.46%	2.45%

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