THE MARKET'S GOT ISSUES (it often does)

It's been a bit of a wild ride since the end of September, and this week's sell-off has been ugly, but in our view, just another week of trading in a choppy market seeking direction - by bulls and bears…and computers. Not to downplay the messiness, as there's certainly a faction that believes we're tipping towards recession, and at times recent market action has had that feel. But before we get into any longwinded explanations, let us simply say: **we don't see it**. We believe the next recession lies beyond next year, at least, but there's no doubt the market is taking stock. And what's top of mind for the market is the recently inverted bond market yield curve. Our apologies for the jargon - upside down yield curve. Generally speaking, and as briefly as possible, bonds with longer maturities pay higher interest (yield) than bonds of shorter maturities - the longer out you lend, the greater risk, the more you demand. So a graph of those yields should be upward sloping. The Fed controls the shorter maturities, and when it is raising rates like now, and the longer maturities (controlled by investors' expectations for growth) don't follow, the graph flattens and investors get concerned that economic growth will slow. When it inverts, well, let's just say, they get concerned(er). Recessions have followed inversions. Though, it's important to note that an inversion is not a perfect or even particularly timely indicator of recession or subsequent market movements.

But there has been more to it than just the bond market.

"… Tariff Man shouldn't go to war with the laws of economics. He'll lose." That's a quote from the editorial board in Wednesday's Wall Street Journal in response to the President's Tuesday tweet "remember….I am a Tariff Man…." Markets had rallied on Monday after hopeful Chinese trade news came out of the G20 meetings over the weekend. But when pressed, administration officials mostly babbled and then we got that tweet - like having the winning touchdown reversed on illegal procedure. #$&%!. As we've written before, we don't know where the Chinese trade confrontation will lead, but we assume the president would rather have a second term than a recession. Nothing said or tweeted so far has changed our view on this.

We believe growth will be slower next year, but that's relative to a 2018 goosed by foolhardy increases in deficit spending. And slower isn't necessarily bad. Most of the data we see suggests an intact expansion, with the exception of housing, which has stalled out on higher prices, and, until very recently, higher mortgage rates. Employment appears strong; wages are rising, but inflation is tame. There's little in the way of excess that we can point to, so our view is the Fed fully recognizes the warning coming from the bond market and will stop raising rates, and the flattish, sometimes inverted, yield curve will be just another curious artifact of this unusually long economic cycle.

As for stocks, valuations in general are average by historical measures, and this year's churning has turned up some exciting values. We've been patient with portfolio construction, but far from perfect - definitely human. Hindsight is a miserable master. And while the cooling of the FAANG stock frenzy might be hitting some investors hard, the rotation away looks quite normal and healthy to us. Just remember, the economy's overwhelming natural tendency is to grow, and the markets will meander along, eventually and fairly reflecting this.

We hope you have a wonderful holiday, and try not to pay too much attention to the short-term action of the markets - it's not good on the digestion.

The Arrington Building
1802 Bayberry Court
Suite 400
Richmond, Virginia 23226

804.288.0404
800.787.7414
FAX 804.288.7872
www.lowebrockenbrough.com