Market Commentary **Fall 2018**

An Irrational Wave?

To help logically process what we may be witnessing today, it is worthwhile to look back over our shoulder at earlier times and experiences. In that regard, October's nasty selloff is reminiscent of last Spring's stock market antics. Remember when, in January, stocks had extended 2017's already outsized gains by another +7.5% before the wheels fell off at month-end on a surprise (10.1%) market retreat to touch correction territory? That happened in just nine days prompting many to believe the bull had finally run its course. Following that frightful early February week, the market promptly reversed course to recover some +8.0% through early March. Then a second whirlwind loss of (7.4%) was imposed on investors by early April. When the dust had finally settled at the end of June, the Russell 3000 broad market index had ended up posting +3.2% on the 1st half year. By the way, it's also instructive to point out that the Federal Reserve had by then imposed (2) additional quarter-point rate hikes including the FOMC's last in mid-June. Notwithstanding the additional tightening, the ensuing summer market shrugged off those hikes to deliver another robust +7.8% performance before September's close - leaving the year to date stock market up almost +10%. Unfortunately, October surprisingly - perhaps irrationally - erased all but 1-2% of those gains.

Having witnessed such erratic, and arguably, untimely market behavior over the last 10 months, it's reasonable to ask what fundamentals have changed in our economy to warrant another surprise and hefty selloff. To our way of thinking, nothing! By all measures, we know that the US economy continues to fire on all cylinders. Unemployment is near 50 year lows, wages are increasing modestly and the dollar is strong: both of which are helping to keep inflation at bay. Consumer spending, personal savings and confidence are at all-time highs. Our leading economic indicators are all pointing in the same direction and corporate earnings remain in double digit territory with healthy profit margins. US GDP growth over the last several quarters has been as strong as it has ever been over the last decade. This includes last Friday's first estimate of 3rd Quarter GDP which revealed that economic growth continued to expand at an annualized +3.5% clip. Despite all this positive real-time data, the market's untimely turbulence seems to suggest that things have simply been too good for too long. Hence there must be a "black swan" out there somewhere ready to do damage to our momentum.

So what speculations belie the market's erratic behavior? Perhaps it's that everyone is reminded daily that the stock market's bull run is now the longest on record with gains having touched heavenly highs (forgetting, of course, that the world's "financial lights" all but burned out 10 years ago). Why wouldn't the market climb back from the deep trough it had dug itself back then? For GDP watchers, perhaps it's the disappointment of this 3rd Quarter's GDP estimate which fell short of the mid-year's +4.2% growth rate - conveniently forgetting that three years earlier most economists rationalized that the US would likely never again see economic growth beyond +2.0%. For the Fed watchers, perhaps it's that "crazy" FED again which has historically been accused of overshooting rate hikes that "assuredly" serve to derail economic growth; or for the yield curve observers who deem the curve's current modest inversion is a sure sign that recession is right around the corner. Why? Because inverted yield curves have always been right! And let's not forget those fiscal policy pundits who reiterate that our current tax reform tailwinds are sure to die off sooner than we expect leaving corporate America no choice but to abandon new business investment and CapEx. Yes, for all these reasons, whether real or imagined, the market absorbs this non-stop data dump to a tripping point, which typically leaves main street investors suffering sudden anxiety while asking themselves "What just happened"?

Meanwhile, what do we sense and see? We see real economic data that confirms that times have not been better in the US over any period in the last decade. The economy is booming hence we continue to remain comforted and encouraged by what we read and observe well into the near-intermediate future. Are there nascent headwinds on the horizon? For certain, because concerns always exist in a stock market, that by nature, forever climbs a "wall of worry".

For now, the most poignant of those concerns is the fear of future inflation and the FED's corresponding policy moves. We, however, don't see anything wrong with the Fed's objective to reach "r-star": the economy's "neutral interest rate" particularly after a decade of mandated accommodation. Next are the upcoming mid-term elections and the toxic political backdrop which underscores them. Some are convinced this election is the most important in our lifetime. Really? Next, is the trade war with China and the speculation that Beijing won't budge, thereby sending global growth into the tank. But, not so fast there Bucky! We've already witnessed amended NAFTA and European trade treaties when most skeptics said the negotiations were doomed to fail. Finally, another less notable - but potential - financial threat is the upcoming Brexit which has garnered very little media attention …. until it finally does! So yes, there's always something to worry about.

So, against this daily cross-current of headline news, what are responsible investors and the investment professionals who serve them to do? To our way of thinking, nothing more than to remain disciplined enough to periodically re-affirm one's investment objectives, monitor and ensure that portfolio allocation appropriately matches one's risk profile, time horizon, income requirements, and liquidity needs. The reward for doing so? Enjoying the comfort of being able to shrug off the daily dump of often contradictory information and the market turmoil it periodically unleashes irrespective of how long it lasts.