CABANA WEEKLY MARKET COMMENTARY SEPTEMBER 23, 2019

Fed Cuts Interest Rates Again as We Continue to Keep our Head Above Water

During the past week, major U.S indexes reached resistance at summer highs before pulling back and churning 1.3% lower (S&P 500). On Wednesday, Chairman Powell and the Federal Reserve lowered the target federal funds rate by 25 basis points. This is exactly what bond and equity markets were pricing in, and despite some perceived hawkishness during Mr. Powell's news conference, stocks and bonds ended up flat on the day.

Overall, we have seen some minor improvement in the yield curve inversion, which has been a major topic here and abroad over the past several weeks. Almost all past yield curve inversions have led to a recession within 24 months. The 10-year Treasury bond is now yielding 1.69% and the 2-year Treasury is yielding 1.65%. Obviously not much difference, but at least it is no longer inverted. Other parts of the yield curve still are, but the 2-10 is the area that is most closely watched.

The U.S. stock market continues to significantly outperform everyone else. China and other emerging markets are weak and well below highs reached early in 2018. Part of this is due to trade issues that remain unresolved and part is due to the strength in the U.S. dollar. A strong dollar negatively impacts commodity exporting countries, which make up much of the emerging market complex. The one exception to this is gold, as it has benefited from deflation around the world and political uncertainty. Developed economies are not doing much better. Germany is technically now in a recession and Great Britain is sure to follow, absent a Brexit deal in the next six weeks. The developed world stock index "EFA" (that does not include the U.S. or Canada) is down 13% from its 2018 high. I have commented on the relative weakness around the world many times and will not belabor the point again, other than to say we cannot grow without trading partners. At some point the U.S. consumer will blink and our earnings will fall, without another source of demand. Of course, this reality is exactly what is being conveyed in economic data like the yield curve. It is why we watch the transportation index (IYT) so closely. It is also why we are always concerned with employment and real estate. Without jobs and a strong real estate market, the consumer does not have the financial or psychological means to carry the U.S. economy on its back. Let's not forget that most of the average American's net worth is in their home.

So far, we have kept our head above water in all these important areas, despite lots of clouds on the horizon. Sometimes a strong wind can blow storm clouds in another direction. We will continue to watch for the wind and hope it is a good one rather than a bad one when it comes.

Last week's market commentary can be found here.

G. Chadd Mason
CEO, The Cabana Group

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