The Long Run

INVESTMENT LETTER | JULY 2019

No more hurting people. Peace.
-Martin Richard

Six years ago, 8-year old Martin Richard was the youngest victim killed in the 2013 Boston Marathon bombing. This past month, a new park was opened in his memory a short walk from our office. Combining a playground, 350 trees, 700 shrubs and 4,400 daffodils with a view of the water and downtown Boston, it has quickly become my favorite spot to sit and think. Five cherry trees commemorate the five individuals whose deaths were connected to the bombings.

The Richard family, which helped to design the park, sees it not as a memorial, but as a spot that will bring life and kindness to the city. As they have accomplished something special with the park, they hope we all will contemplate what we can accomplish with our lives.

As we reflect upon the performance of financial markets and the economy during the past quarter, we note that, despite widespread disbelief, both achieved major milestones. Stock prices recently reached all-time highs, with the S&P 500 increasing by 4.30% in the second quarter and 18.54% for the first six months of the year. As of June 30th, the current, ten-year economic expansion became the longest in U.S. history.

Though these accomplishments may seem like something to celebrate, a majority of investors remain dubious. As of this writing, a survey by the American Association for Independent Investors found that only 33.2% of investors were bullish, while 34.5% were neutral and 32.4% were bearish[1]. A survey by Bankrate found that 40% of Americans believe a recession has already begun, or will start in less than a year.

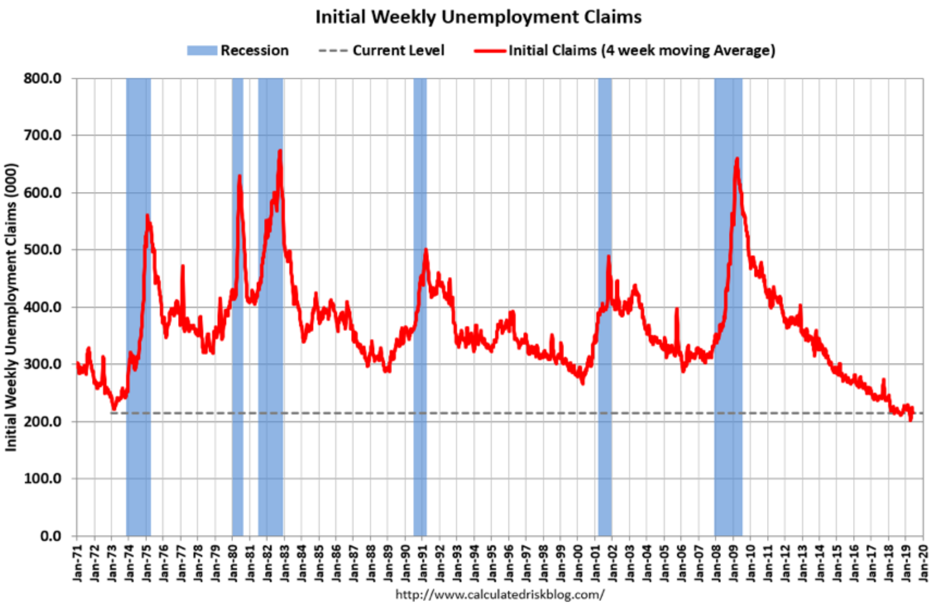
How can one explain this seeming disparity? While this has been the longest economic expansion in our country's history, it certainly hasn't been the strongest. Signs of economic slowing, largely due to trade tensions with China, have become more evident of late. As the following chart shows, the gap between the stock market's gains this year versus disappointing economic data is the widest in U.S. history.

The arguments that this expansion is at record length – so it must be about to end – and the inversion in the yield curve, a solid predictor of impending recession, are not to be easily dismissed. We put some faith in these indicators – and they are reflected in the asset allocation in accounts we manage.

Our favorite indicator, though, of an imminent economic slowdown has not yet given any early warning signals. Initial unemployment claims almost always are the first indicator of when a recession is brewing. When companies experience the first signs of a slowdown, they tend to let workers go, as they are a variable cost that can quickly be pared in order to protect profits.

1. AAII Sentiment Survey Results for Week Ending 7/4/2019. https://www.aaii.com/sentimentsurvey/sent_results

As the following chart shows, initial unemployment claims are near a 50-year low. The previous low was reached in December 1969. If one adjusts for the fact that our population is 60% higher now than it was in 1969, this chart would show companies are doing all they can to keep employees.



With the labor market looking fairly healthy, consumer spending relatively strong, productivity growth accelerating and corporate capital expenditures better than expected, the economy appears like it will continue to grow, though at a slower rate than last year. Trade negotiations with China could certainly disrupt what the economy is accomplishing, so we will likely continue to raise some cash in accounts as valuations rebound.

As we look ahead to the second half of 2019, may we continue to be inspired by the generosity of the Richard family, and others, and reflect on what we can accomplish in the days ahead and the difference we can make in the lives of those around us.

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We would also like to make you aware of some of our firm's accomplishments over the past month. We have just added two new portfolio managers to our staff, Abby McCoy and Katherine O'Brien. Our 17-member senior management, research and portfolio management teams are now balanced with eight men and nine women. We also welcome Hazie Ghazali-Cho, who joined our Fresh Pond Capital division in April as Client Service Associate.

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