Argent Capital Management LLC

RE: **INVESTMENT COMMENTARY FOR PERIOD ENDING SEPTEMBER 30, 2019**

FROM: **ARGENT CAPITAL MANAGEMENT**

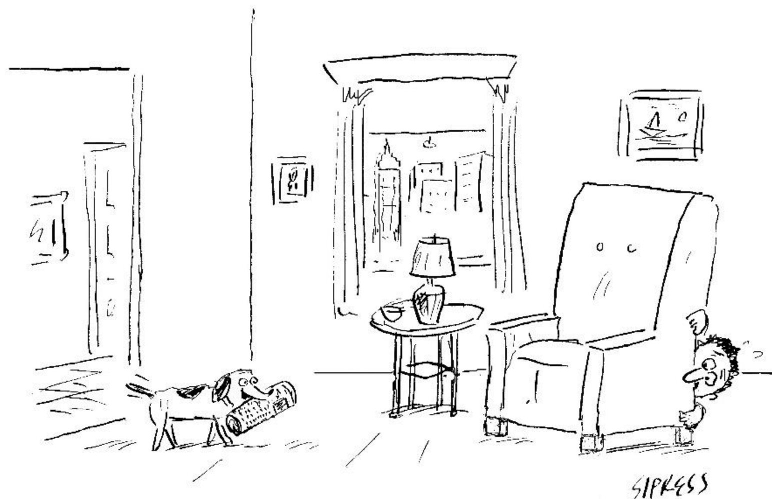
DATE: **OCTOBER 9, 2019**

"I have approximate answers, and possible beliefs, and different degrees of uncertainty about different things, but I am not absolutely sure of anything."

- Richard Feynman

Richard Feynman, a noted physicist, would be pleased that *uncertainty* was the only *certainty* in the third quarter of 2019. The S&P 500 Index surged to an all-time high in July, faded in August on a flare-up of U.S.–China trade tensions, then improved again in September as a more conciliatory tone took hold. The result was an uneventful quarter for most U.S. stocks. Year-to-date, however, returns are very good, with virtually all stock indices reporting solid gains.

Four newsworthy themes are poised to dominate headlines this fall and upcoming winter, all with economic and financial ramifications, and some with political consequences as well.



Low Interest Rates: Global interest rates continue to fall to unprecedented levels. The thirty-year Treasury Bond fell *below* two percent for the first time ever in the third quarter, while the interest rate (yield) on a two-year Treasury Note rose *above* the interest rate on a ten-year Treasury. Such an occurrence creates what is known as an inverted yield curve, implying that bond investors have very pessimistic views of future economic growth. (Why else would bond investors accept such low returns on their bond investments?) An inverted yield curve has preceded *all* recent recessions, although it is also worth noting it has predicted a few downturns that did not materialize.

Partially in reaction to a *negative* interest rate environment overseas, the Fed cut its benchmark interest rate in September by 0.25 percent – its second such reduction of the third quarter. The Fed's latest rate reduction followed closely on the heels of aggressive action by the European Central Bank, which further cut its interest rates (most of which were already negative!) and implemented new monetary stimulus. The Fed's cut, therefore, was partially in reaction to this, and to help cushion the economy against a deeper global slowdown amplified by trade disputes. There are, of course, benefits to lower rates – mortgage rates have been declining all year and, in August, we saw a significant uptick in housing starts and building permits. In addition, refinancing is surging again, putting more money in consumers' pockets.

"Your previous provider refused to share your electronic medical records, but not to worry—I was able to obtain all of your information online."

High Employment: The jobless rate fell to 3.5 percent in September, its lowest level in 50 years. New monthly jobs in the U.S. have averaged 161,000 this year, a healthy clip considering that we are now in the eleventh year of an economic expansion. Falling unemployment helps allay fears of a recession, although there is no question that we are in a slower growth mode. The Institute for Supply Management (ISM) had their manufacturing index recently fall to 47.8, signaling a *contraction* in manufacturing activity. This does not, however, on its own signal a recession, as the all-important consumer spending figures remain strong. Nonetheless, soft manufacturing indicators combined with low interest rates overseas keep open the possibility of another Fed interest rate cut later this month.

Trade/Tariffs: There is little debate that trade uncertainties reduce business confidence and investment. Quite simply, it is hard for business executives to make major decisions about investing in projects and employees when they do not know what future costs they might reasonably expect. Recently, the World Bank stated the average U.S. tariff was below 2.0 percent from 2000 to 2017. They estimate that this number will approach 6.0 percent if President Trump's remaining tariffs go into effect as scheduled. Whether good or bad for the U.S. over time, tariffs *do* increase costs of doing business, some of which are absorbed but hurt profit margins, and some of which are passed on to consumers.

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As good as the economy has been in recent years (and it has been good), we believe it would have done even better if the U.S. and China had been able to reach a truce regarding trade. It would also help if Congress would ratify the revised NAFTA agreement and if trade negotiations with European leaders could be resolved. Our hope is that some sort of *détente* will occur, and perhaps the upcoming election cycle can provide the catalyst needed to make that happen.

Impeachment/Election: We have learned over the years, both with experience and by studying history, that making investment decisions on the basis of possible election outcomes or political events rarely works to an investor’s advantage. Markets are unpredictable in the short-run, and businesses adapt quickly to changing circumstances.

As we see things, impeachment hearings will unquestionably cause much venom to be spewed by both parties, but an impeachment drama, on its own, seems unlikely to derail investment markets any more than the Clinton hearings did 20 years ago. The election, however, has the potential to have a greater impact, particularly if it seems likely a much higher tax and more stringent regulatory environment is coming. Even so, and to paraphrase Calvin Coolidge, if you see ten troubles coming down the road, nine of them will almost certainly head to the ditch before reaching you.

Using 20/20 vision for next year (get it - 2020?), and given all this, where do we see investment markets heading? Our expectation is that interest rates will remain very low and corporate earnings will grow, albeit at a modest pace. Employment will stay strong, and inflation muted. (Indeed, housing activity may actually increase in this environment.) These positives should be enough, particularly when combined with the stock market at reasonable levels, to offset political headline risks and ongoing trade disputes. While we, like Richard Feynman, have different degrees of uncertainty about any number of different things, we do have confidence the economic recovery now in its eleventh year should have durability into year twelve.

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