

July 10, 2019

WHAT WEIGHS MORE — A POUND OF FEATHERS OR A POUND OF LEAD?

Dear Clients and Friends,

How does one make sense of seemingly conflicting information? Is it best to rely on one's gut or to evaluate the available data and come to an educated conclusion?

While this appears to be an existential question that should be pondered within the ivy-covered walls of academia, in reality, it is a practical one that investors face every day. We are continuously weighing information. From a micro perspective, we balance our technical analysis and industry outlooks with information we receive from the companies in which we invest. We are challenged to interpret macro-economic data that can stand in stark opposition to what the markets appear to be saying. Even asset classes, bonds compared with stocks for example, can telegraph divergent views about the future.

The second quarter of this year was particularly ripe with this type of conflicting information, yet lacking the wild rollercoaster ride of the preceding six months. After two quarters where the stock market demonstrated bipolar behavior based mainly upon the Federal Reserve's outlook for the future of interest rates, the most recent quarter's activity was more muted. This was despite continuing concerns surrounding the outlook for global trade, earnings, GDP and government policy.

More broadly, investors turned much more conservative, with global cash flows chasing the safety of high-quality bonds. This demand has driven yields in the safest of assets to levels we last observed in early 2017. A recent poll of money managers concluded that investors haven't been this bearish since 2008. They highlight the second biggest drop in stock allocations on record and the growth in cash positions not seen since the 2011 debt-ceiling crisis.

Is this bearish or bullish? There is still underlying strength to the market - the S&P 500 closed the quarter bumping up against all-time highs - notwithstanding the headlines. With bonds as expensive as they have ever been, many stocks should provide a better total return over the intermediate period. Most importantly, many companies continue to see their businesses thrive. Therefore, we would conclude that pessimism is overblown and that prudent and thoughtful security selection is a better strategy than building a cash hoard in one's mattress. The market certainly has areas where valuations would cause us anxiety if we had to own them. Fortunately, we don't!

The path over the near-term is likely to be bumpy - but this isn't out of the ordinary for the stock market. While these periods of stress can provide wonderful investment opportunities, as they have so far this year, we realize that they can also trigger concerns with respect to one's personal circumstances. As always, we are available to help you interpret what it all means for you individually.

We hope you enjoy the balance of the summer and thank you for your continued trust in our firm.

Best regards,

The Partners of CANNELL & CO.