Trust, it's our last name.

American National Bank & Trust™

Generally Optimists, Worriers by Nature

May 2, 2019

What a great start to 2019: we just witnessed the best 1st quarter performance in 20 years. The S&P 500 rose 13.65%, erasing the -13.53% decline experienced in the 4th quarter of 2018. In fact, since 1959, a period of 60 years, there have only been six times when the 1st quarter had better performance. The fears about higher interest rates, slowing corporate profits, and trade wars seemed to fade with the New Year. Even bond prices improved as interest rates declined. The yield for the 10-year Treasury dropped 28 basis points to yield 2.40%. The super ball bounce back in growth expectations and the dovish swivel from the Federal Open Market Committee (FOMC) resulted in a Goldilocks environment which has allowed most assets to rally year-to-date.

For the moment, the FOMC is on hold for a possible rate increase and has suggested that any change in the Fed Funds target rate will be data dependent. The economy continues to grow albeit at a slower pace, but still remains positive. Even a possible trade deal with China looks to be moving forward. Low inflation, economic growth and the low unemployment rate continue to point to a strong economy.

Unfortunately we are worriers by nature and it is hard to see how the market can maintain this level of returns for the remainder of the year. The 2nd and 3rd quarters are traditionally uneventful. The 4th quarter is typically the wildcard. Ultimately further asset performance this year will be determined by growth in the US, Europe and Asia. With interest rates relatively low, it still makes sense to lean into equities. With inflation running at or below 2.0% and the 10-year Treasury's yielding 2.40%, it is hard to overweight bonds until we see the yield curve invert (short term rates higher than longer term rates).

Speaking of inverted curves, at the end of the 1st quarter of 2019, the spread between the 3-month T-bill and the 10-year Treasury note was less than 2 basis points. In 2000 and 2001 and again in 2006 and 2007, the yield curve inverted and the economy subsequently went into a recession. The difference between negative spreads was 50 to 100 basis points during those periods. We won't say this time is different but with negative 10-year yields in Switzerland (-0.347%) and Japan (-0.06%) and Germany paying only 0.01%, it is difficult for foreigners not be buyers of US debt, thereby increasing demand and keeping a lid on US interest rates.

As we review current portfolios we are primarily looking for positions that have appreciated significantly over the initial position target. In some cases we will selectively reduce the exposure to individual equities in order to reduce portfolio risk. The decision to reduce or sell assets is not something to be taken lightly, as it often creates a taxable event.

So far the month of April has been positive. However as I mentioned, we are worriers by nature. We will be looking for cracks in the markets, until then we will continue to press the equity position and still maintain a fixed income allocation per each accounts individual objective. Please let us know if you have any questions or concerns regarding your portfolio. We truly appreciate the confidence you have placed with American National Bank & Trust.