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No Recession Yet

For most investors, the stock market and the economy are inextricably linked. This idea can be forgiven because the financial news media goes to great lengths, on a daily basis, to tie the movements of the market to economic events. But the fact of the matter is, there is little relationship between the health of the overall economy and that of the stock market. This current expansion (2009-2019) has been the slowest in history, averaging only ~ 2% growth per year.3 But has this impeded stock market performance? No, the S&P 500 has fared quite well, averaging ~ 14%, greater than that of historical norms.2

For one thing, stocks tend to be a leading indicator of the economy.3 That means in years like 2009 when growth was negative, stocks were looking ahead to better growth to come. It also means that in years like 2000, when growth was positive, stocks were looking ahead to weaker growth (recession began in March 2001).1,3

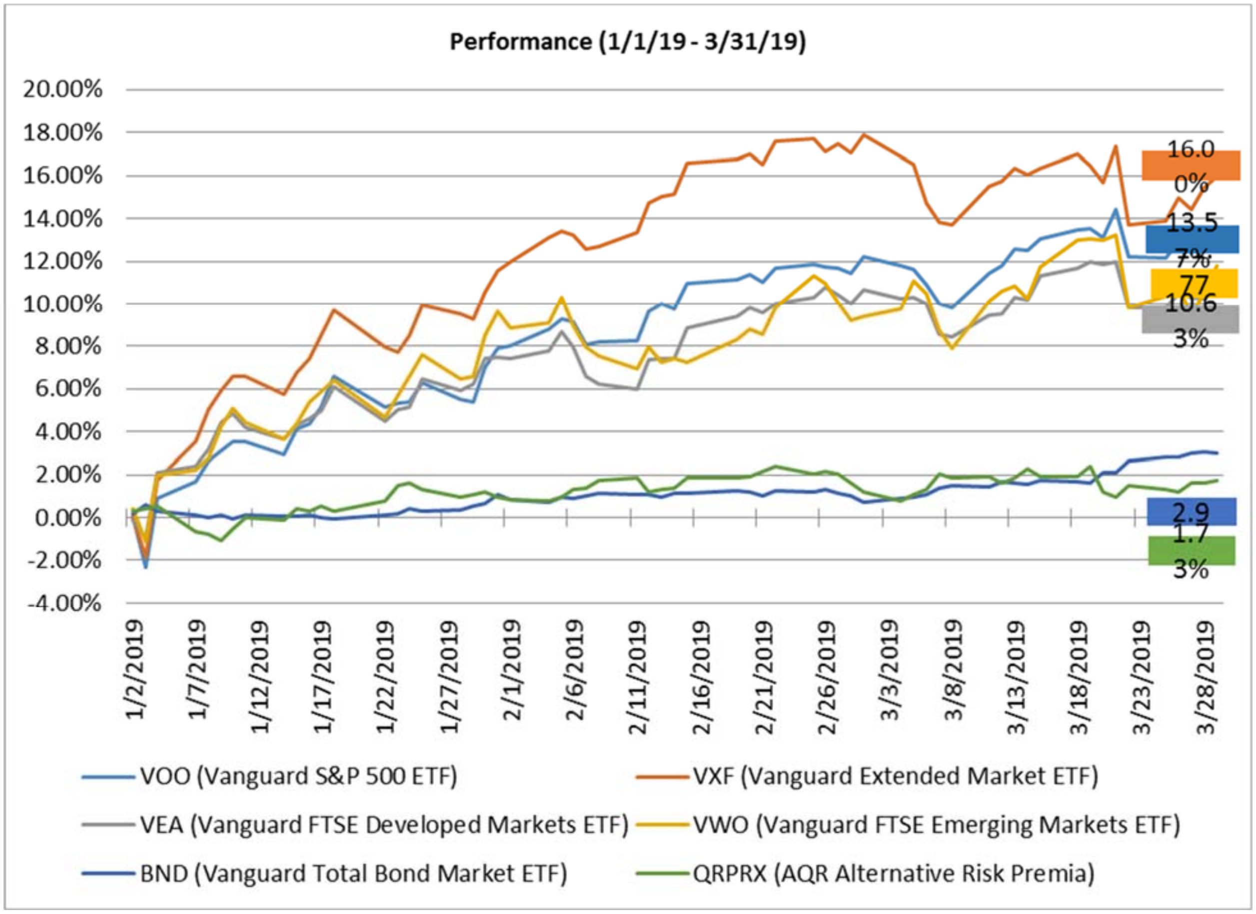
Where this gets complicated is that stock returns are frequently not telling you anything important about the economy, but instead simply reflecting changing investor sentiment. At times, investors will pay more for a given level of earnings, and at other times they will pay less. What's going on in the economy is just one factor in that determination. Stocks are ultimately a reflection of long-term corporate earnings, which is not the same thing as short-term economic growth.

After the fourth quarter of 2018, when the Fed raised rates and began to unwind Quantitative Easing, equities fell nearly 20%, and economic data weakened. Some investors even tossed around thoughts that the cycle was over and the U.S. was headed into recession. Economic softness has continued into 2019, however, consumer sentiment remains strong and technological advancements continue to lift margins and profits.4

The Federal Reserve has paused in its tightening campaign and has indicated that the process of normalizing the balance sheet may also conclude later this year. They can do this because, in contrast to previous cycles, inflation has remained remarkably stable, and has even drifted down so far in 2019.4 By doing so, they may enable the economy to continue to grow for longer than would usually be the case, as well as maintain the valuation argument for riskier assets relative to government bonds. While the Fed is on pause, it is not likely done for the current cycle. And that is good news, since further Fed tightening would signal that the economy has improved.

As shown in the chart on the following page, stocks around the world have rebounded during the first quarter of 2019.

1



A recession is inevitable; the U.S. economy will move into a recession at some point. They always occur at the end of a cycle and set the stage for the subsequent cycle. However, it does not appear to be here yet. Taxes have been cut, regulations reduced, and corporations are more profitable than ever. Employment, wages, housing, and inflation may provide some signs of relief and allow the U.S. to maintain its pace through the remainder 2019. As long-term investors, it is important to remain focused on the long-term. Near-term data can go in either direction; valuation is usually a better guide to long-term returns.

Sources:

1. https://finance.yahoo.com/
2. https://www.morningstar.com/
3. https://fred.stlouisfed.org/
4. Kelly, David. “Economic & Market Update.” Economic & Market Update - J.P. Morgan Asset Management, J.P. Morgan Asset Management, 1 Apr. 2019, am.jpmorgan.com/us/en/asset-management/gim/adv/insights/economic-overview