THE INVESTMENT COUNSEL COMPANY

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Stocks and bonds seldom rise together. Fortunately, 2019 is proving to be an exception along with many other investment, economic, and political precedents in recent years. Global financial markets have fully recovered from their modest declines in 2018, leading the way to even further gains. The first quarter was the best start in 21 years with U.S. stocks (Standard & Poor's 500 Stock Market Index) outpacing foreign stocks +13.65% versus +10.21% (MSCI All Country World Index Ex. U.S.). Similarly, U.S. bonds were up +2.94% (Barclay's U.S. Aggregate Bond Index) versus foreign bonds +2.75% (Barclay's Global Aggregate Bond Index Ex. U.S.).

The catalyst for the change to a positive market trend from the December 24th low is still unclear. Some believe it was our Federal Reserve Bank reversing policy, halting its aggressive posture of automatically raising interest rates. Others feel it was President Trump's progress toward a trade war resolution with China. The risk of higher interest rates in the face of a fragile but growing U.S. economy and the continued negative economic impact of a prolonged global trade war are perceived as the two largest risks in causing a future recession. Mitigating these threats to global market stability can be reason enough to celebrate, improving investors' outlook. But a third cause for concern is the European Central Bank's remark last month indicating that Europe is still not gaining sufficient economic growth to warrant gradually raising interest rates like the U.S. The bond market's reaction was a sudden reduction in interest rates, while bond prices increased across the globe. As a result, both stocks and bonds continued their rally. These two asset classes appear to increase their relative attractiveness as investors continue to reach for returns above U.S. Treasury Bills and other money market instruments.

Now, everyone is asking where capital markets might go from here. The majority of strategists are convinced that a Trump-China tariff deal will lead to further stock gains. Our Firm is hesitant to conclude that such a market rally will prove sustainable. Investors' captivation with trade talks may have prompted speculators to bid up stock prices in anticipation of a resolution, leading to stronger corporate profits. Buying is also coming from less-disciplined investors who missed the recent rally and, as a result, are eager to add to their portfolios on any market dip. Overwhelmingly, corporations have been the single biggest reason the market has remained in an uptrend the past few years by borrowing aggressively to buy back their shares. Regardless, the market's future direction will likely be determined by the degree of growth in corporate profits. Astute investors recognize that increasing corporate profitability is ultimately the backbone needed to support continued advances in stocks.

Should the economy continue growing for at least four more months, it will be the longest economic expansion in post-war U.S. history. The media, and therefore investors, are persuaded that the market cannot continue rising due to this unprecedented timeframe. But history may prove otherwise. Bull markets do not die of old age! Often the Fed chokes off economic growth by repeatedly increasing interest rates until the economy contracts, ultimately leading to a recession with lower stock prices. So, investors are justified to be frightened by Fed actions to stem inflation without clear and compelling evidence. Just as many investors are concerned about a recession and ensuing deflation, as there are others worried about inflation. Winston Churchill stated that Russia is a "riddle, wrapped in a mystery, inside an enigma," which could certainly apply to the financial markets today.

Our current focus is striving to determine if there is sufficient evidence to support strong conviction that last year's bear market is (or is not) the beginning of a new cyclical bull market in stocks. These varying market conditions are some of the key drivers influencing capital asset prices that we continually monitor. Therefore, we remain committed to taking a measured and disciplined approach in managing potential risks and opportunities on behalf of our clients. As always, we value the trust and confidence placed in our Firm.

Sincerely,

Randy

Randy Garcia
Chief Executive Officer