After The Close

A recession 'signal' combines with trade skepticism to send shares sharply lower.

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Major Domestic Equity Indices - Today			
Benchmark	**Index Level**	**Net Change**	**% Change**
S&P 500 Index	2,702.00	-88.40	-3.2%
Dow Jones Industrial Average	25,055.00	-771.40	-3.0%
Russell 2000 Index	1,481.00	-68.00	-4.4%
NASDAQ Composite	7,162.00	-279.50	-3.8%

All data via FactSet as of approximately 4 PM ET

Growth prospects once again come into question

Investors made another run for the exits today. Renewed skepticism over the U.S. /China trade relationship offered some pressure at the open, but it was an unusual development in the bond market that really greased the skids to the downside in the afternoon.

Interest rates on the Treasury Department's 3-year bonds exceeded that of its 5-year bonds at the close of trading on Monday. This is an unusual development and one that implies something is not quite right in the bond market. Under normal circumstances, even the U.S. Treasury should have to pay a higher interest rate to borrow money for a longer period of time.

When shorter-maturity treasuries offer a higher interest rate than longer-maturities, it's a situation referred to as an "inverted yield curve." Historically, such situations have had a good track record of signaling a pending recession with about one to two years warning. The relationship between the 2-year Treasury and the 10-year is usually the most closely watched relationship, but as shown today, any inversion along the curve is still a concern likely to fuel market turbulence.

A flat and/or inverted yield curve is also a clear negative for banks as they seek to "lend long and borrow short." This consideration was evident today as the S&P Financials Sector led to the downside with a loss of 4.4%.

Stocks had started the day under pressure from a re-evaluation of just how much progress toward a U.S. /China trade agreement was actually accomplished at the G20 Summit this past weekend.

A dinner meeting between President Trump and China's President Xi (as well as other officials on both sides) was said to have produced encouraging dialog, even leading the U.S. to delay a scheduled increase in tariff rates on Chinese goods due to go into effect January 1st.

Most major U.S. stock Indexes added more than a full percentage point on the news yesterday. Upon closer examination, however, there appeared little of tangible value to back up such optimism, causing many to question China's true intentions toward making the trade policy changes that most Western governments seek.

Committee View

Based on a strict evaluation of economic fundamentals, we still believe U.S. recession odds over the intermediate-term remain low. There is little doubt, however, that risks to the outlook have risen. Unfortunately, markets are likely to remain volatile until there is clarity on key issues such as the U.S. /China relationship and the path of Federal Reserve interest rate policy.

In our view, it is in such periods of heightened uncertainty and market turbulence that the value of investment diversification shines. We continue to recommend investors follow a modestly more cautious profile in their investment allocations until greater clarity on these issues can be ascertained.

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