THE DANA VIEWPOINT

February 25, 2019
Dow: 26,092

We Have Reached Cruising Altitude

We certainly had a bumpy ride there at the end of our interest rate climb. It is time for the Fed to level off, take their hands off the controls, and turn the seat belt sign off. Let market participants move about the cabin and assess the current economic and market situation without any further input from the Federal Open Market Committee.

It is difficult to look at the market events of the last five months without laying the mantle of responsibility on the Fed. As equity markets fell in October, November, and December, the Fed did virtually nothing to change their tone, and followed through with their fourth rate increase of the year on December 19th. It appears we now know what kind of a market swoon it takes to get the Fed's attention. From its high on September 20th, the S&P 500 Index fell 14% through the Fed meeting date on December 19th. Jerome Powell's news conference following the meeting outlined their intent to continue rate increases and the runoff of the balance sheet. In the next three days, the S&P 500 Index fell over six percent for a total decline of almost 20% from the September high. This move did get the Fed's attention, and members of the Board of Governors and Fed presidents began commenting in far more conciliatory tones.

One of our concerns in January was that the market rebound would be so strong that the Fed would forget the message sent by the market in December. On the date of the January meeting, the S&P 500 Index was up 7% for the year and 14% from its Christmas Eve low. The interest rate doves got what they wanted from the January meeting, as the Fed did not raise rates and said, "The Committee will be patient as it determines what future adjustments to the target range for the federal funds rate may be appropriate to support these outcomes." Patient is the keyword here, and the Fed backed up their change of heart by discussing an end to the shrinking of the balance sheet at the January meeting.

Although the Fed has said they will still be flexible with regard to incoming information, it is clear to us that the inertia is now indicating they will stay put. This is an entirely different mindset from the Fed compared to the last four years, when their bias was to raise if they could.

(CONTINUED ON REVERSE SIDE)

Now they need a reason or reasons that indicate significantly stronger inflation in order to raise rates again. We still worry about the fragility of the system. Debt levels are setting records at the sovereign level, and they have been increasing at the consumer level. There are warning signs indicated by the subprime auto loan market. To ensure that we are out of the woods, we would like to see commodity prices stabilize or even drift upward. We would also like to see the dollar remain within a range and not strengthen, and high yield spreads remain at reasonable levels and not gap up. We would even like to see longer Treasury bond yields drift upwards. So far this year, Treasury yields have not moved much from where they were at the end of the year. To us, that indicates that there still is some skepticism about this rally.

Earnings season was the weakest in two years, and expectations for 2019 earnings have been coming down. This does not have to be bad news for the equity market, as clearing a lowered hurdle can still result in market advances. Low and steady interest rates can also help support higher price-to-earnings ratios, and this could help drive the market higher. We are seeing market breadth broaden, which is creating more rewarding opportunities. Let's hope we can maintain this cruising altitude in the market this year, and avoid any unexpected turbulence.

Random Thought for February 2019: "Games are won by players who focus on the playing field – not by those whose eyes are glued to the scoreboard." - Warren Buffett

20700 SWENSON DRIVE • SUITE 400 • 53186 • P.O. BOX 1067 • BROOKFIELD, WI • 53008-1067 • 262.782.3631 • FAX 262-782-0581
365 ERICKSEN AVENUE.N.E. • SUITE 312 • SEATTLE, WA • 98110-1888 • 206.855.8781 • FAX 800.560.6227

E-Mail: dia@danainvestment.com
Web Site: www.danainvestment.com