



## NEWS OF THE MONTH

### Sound Income Strategies Newsletter, June 2019

#### May 2019

Index	Month	YTD
DOW	-6.30%	+7.56%
S&P500	-6.34%	+10.74%
NASDAQ	-7.77%	+12.86%

10-Yr Treasury yield began the month at 2.50% and ended May at 2.12%.

#### Markets

Uncertainty returned to the stock market in a big way in May. The Dow Jones Industrial Average fell below 25,000 for the first time since January, and the S&P 500 finished the month down about 6.5%. Overall, it was Wall Street's worst May since 2010.\*

The fear among investors was driven mainly by trade, as President Donald Trump once again ramped up his trade war with China, then announced new tariffs on Mexican imports. If it all felt familiar, you'll recall that for most of 2018 the markets experienced record levels of volatility, mostly driven by uncertainty over Trump's trade policies. Things were much calmer this year until May, despite no real progress in resolving the trade war and the emergence of new warning signs for the economy—most notably the flattening of the yield curve.

In May, that warning sign continued, with the yield curve becoming the most inverted it's been since 2007.\*\* For most of the month, the yield on the 10-Year Treasury rate was lower than current Fed Funds rate of 2.5%.\*\*\* This is exactly the situation I forecast two months ago, and I believe it will continue. I also stand by my forecast that the inverted yield curve could go from being a classic symptom of recession to being the major cause of a recession by sometime in 2020, if not sooner—and others agree. According to a new report by the National Association of Business Economics, a majority of economists surveyed say they believe a recession will hit by the end of 2020, with about half of them saying they believe it will begin halfway through next year.\*\*\*\*

With all this in mind, it's clear that big investors once again have "one finger on the trigger," ready to pull out as soon as the next sustained major market drop takes hold. Before that

happens, though, it's possible the volatility could diminish and the markets start trending upward again. In fact, last month I noted that the inverted yield curve could actually be good for the stock market in the short term. The stalled low-interest rate environment may force some everyday investors back up the risk curve and into the market, and prompt corporations to continue increasing their use of stock buybacks. Those drivers could expand the equity bubble further in 2019, but I believe the odds of the market regaining its previous peak and climbing higher from there are increasingly slim, given all the factors at play. Ultimately, this may be a year in which the old Wall Street adage "Sell in May and Go Away" turns out to be good advice.

### **Portfolio Transactions:**

When managing your portfolio at SIS, we look for one of four possible "enhancement" trades while reviewing securities and possible transactions. Income generation is our primary goal for our clients, and we consider the following four portfolio enhancements before transacting: current yield, yield to worst (minimum projected annualized total return), interest rate risk, and default risk. The intents of these transactions are categorized as follows:

- Pay Me Now – Enhancing current yield
- Pay Me Later – Enhancing yield to worst
- Cover My Assets I. – Managing interest rate risk
- Cover My Assets II. – Managing default risk

We evaluate the transactions by determining whether they meet one, two, three, or all four enhancements. A baseball analogy for this: SINGLES, DOUBLES, TRIPLES, and HOME RUNS.

During the month of May we had the following swaps:

- o Sold Arrow Electronics- ARW 3.5% 4/1/22 @ 3.05% ytw
- o Sold American International Gp- AIG 3.75% 7/10/25 @ 3.37% ytw
  - Sold International Paper- IP 3.8% 1/15/26 @ 3.32% ytw
  - Purchased Toll Brothers- TOL 4.35% 2/15/28 @ 4.70% ytw
  - Purchased Lennar Corp- LEN 5% 6/15/27 @ 4.75% ytw
  - Purchased Huntsman International- HUN 4.5% 5/1/29 @ 4.35% ytw

These three swaps were to pick up yield and would be considered singles.

\*"Trade War, Tariffs Send Wall Street to Worst Month of May Since 2010," Money and Markets, May 31, 2019

\*\*"Inverted Yield Curve Becomes Most Inverted Since 2007," Yahoo Finance, May 29, 2007

\*\*\*Macrotrends.com

\*\*\*\*“Economists’ Fears of a 2020 Recession in the US Surge,” CNN Business, June 3, 2019

*Note: The above trades were recent block trades and do not reflect all trades done on an individual specific basis. Sound Income Strategies, LLC is a registered investment advisor. Information presented is for educational purposes only and does not intend to make an offer or solicitation for the sale or purchase of any specific securities, investments, or investment strategies. Investments involve risk and, unless otherwise stated, are not guaranteed. Past performance is not an indication of future results. Be sure to first consult with a qualified financial advisor or tax professional about your specific financial situation before implementing any strategy discussed herein.*

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