Five Mile River Investment Management, LLC April 14, 2019
Quarterly Letter
1st Quarter 2019

PERFORMANCE

	FMR Performance		Russell 1000	Dow Jones	S&P 500
	Taxable	Retirement	Value	Industrial	Dividends
2019 Q1	12.32%	13.35%	13.44%	11.15%	13.65%

Historic Federal Reserve Pivot and the Market Response

The 2019 first quarter results were historic across multiple asset categories. The S&P 500 notched the best quarter in ten years at +13.65%! The Federal Reserve Chair, Jerome Powell, pivoted in a speech on January 4th, where he admitted the FED had made a mistake in calling for three more rate increases in 2019. Instead, in this early January speech, Chairman Powell said that 2019 may have only one rate increase! In the most recent Federal Reserve statement in the last week of March, the FED is now saying there may be no further increases this year. This is an historic pivot which has unleashed the animal spirits. The December increase in rates (federal fund rate was increased to 2.375%) was probably the peak for this cycle. During the first quarter there were a number of asset categories setting 10+ year records. The 10-year Government bond rallied from a 3.2% yield in the fourth quarter to a 2.4% yield at quarter end (more on this later), the lowest rate since early 2017. Oil was the best performing major commodity and it was the best quarterly rally for crude prices since 2009. The New York Mercantile Exchange (NYMEX) crude rallied 32% and closed over $60/barrel (WTI). It is worth noting that the Shanghai Composite rose 23.93% in the first quarter! Stock markets are among the best leading economic indicators, so hopefully the Shanghai and S&P 500 are signaling that both the Chinese and U.S. economies have solid footing.

Five Mile River Performance

Five Mile River (FMR) client portfolios' performance gained 13%, depending on the investment style (balanced, income or growth). The heavy weighting of tech in the S&P 500 (23% of the index), was the dominant attribution for the S&P 500's strength. The often-discussed names of Facebook, Amazon, Apple, Netflix and Google (FAANG) comprise the majority of the 23% tech weighting in the S&P 500. In contrast, FMR portfolio average technology weight is between 15% and 20%. FMR holdings in technology include stocks that conform with the FMR investment strategy of holding companies that generate growing free cash flow and growing dividends. Consequently, FMR's technology names differ from the S&P 500 names and include: American Tower, Crown Castle (both benefit from growth in cellular demand), Microsoft, Intel, Cisco, and the premier cloud data center companies, Equinix and Digital Realty. There is a clear distinction in owning the FMR tech companies because there is less price volatility and the companies have attractive valuation metrics, something missing in the FAANG group.

All Inversions are Not Alike

The rally in bonds during the first quarter was driven in part by the Federal Reserve pivot, BUT also because of slowing growth across both the European and Far Eastern regions. With GDP growth estimates contracting, even in the U.S., the recession subject has become quite topical in just the last three weeks. This concern has been exacerbated because the 10-year Government bond yield briefly fell below short-term rates. When short rates are higher than long rates this is called a "yield curve inversion," or just "inversion." Yield curve inversions have preceded every post WWII recession, which explains why this is obviously regarded with genuine concern. However, **not ALL yield inversions lead to recessions!** Typically, an inversion occurs because the Federal Reserve raises short-term rates to cool an overheating economy. This policy of raising short-term rates above longer maturities has the effect of slowing (or killing) the economy, and unfortunately this usually causes a recession.

The current inversion is different from the past tightening cycles because it was caused by the rally in the 10-year Government bond, creating a low yield of +2.40%. This happened at the same time the 3-month and 6-month Treasury bills were trading between +2.40% and +2.50%, hence the modest inversion. The cause of this rally in the 10-year Government bond was the shift in international money flows. Weak international economic data during the first quarter caused international currency weakness (Euro, yen and yuan) and international investors chose to exit a number of international government bonds which had negative interest rates. Nearly a third of the world government debt market was priced at negative yields in the first quarter! As an example, the German 10-year Bund is currently yielding -0.03%. While it should not be a surprise to see money exiting negative yielding bonds, it was a surprise to see the degree to which the influx of international money drove up the U.S. 10-year Government bond price (lowering the yield). **The modest inversion of the yield curve ended in the last week in March** with the combination of LOWER short-term interest rates, and a slight increase in 10-year Government bond yields. This recent and short-lived inversion does NOT imply an imminent recession, AND the Treasury market is signaling that the next move by the Federal Reserve will be to lower short-term rates. The animal spirits mentioned above became unleashed as investors see a path for lower interest rates.

Concerns Du Jour and Federal Reserve Policy

FMR believes that the economic expansion in the U.S. will continue, albeit at a subdued rate of 2.5% to 3%. However, with slightly more modest growth, the health of the U.S. economy will continue to be on the list of concerns du jour. The concerns are real, but are likely non-recurring, ex. Government shutdown, bad weather (U.S. Midwest flooding or West Coast fires), export threats from trade, or political macro concerns like Brexit. What offsets the continually growing list of non-recurring events?

It is the Federal Reserve's accommodative stance that is ready to provide monetary stimulus at the sign of any enduring economic weakness. The Federal Reserve's January pivot demonstrates their willingness to promote and extend this economic recovery. When market declines are brought about by the economic concerns du jour, FMR uses these market corrections to add to existing portfolio positions; to execute new ideas that may have price-corrected; or to swap out of existing holdings into other stocks that have better upside potential. For this reason, FMR client portfolios benefit from market volatility through active management by continually upgrading positions and the weightings of market sectors.

Each year Five Mile River Investment Management renews the company's registration with the Security and Exchange Commission (SEC), and as part of this process we update the Five Mile River Form ADV Part 2. The Form ADV Part 2 is a detailed brochure covering all aspects of FMR's business. Please contact Martha Robbins (203-388-4810 or martha@fivemileriver.com) to request a copy of FMR's ADV Part 2. We wish you an enjoyable spring,

Sincerely,

Lee	Todd	Martha

The S&P 500 Index is a market capitalized weighted index of 500 companies. It is a growth-biased index because the larger the capitalization of a company, the larger the weight it contributes to the S&P 500 Index performance. The index referenced includes the dividends issued by these 500 companies. This index is used for a comparison for FMR retirement accounts.

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