Investor Insights & Outlook

July 2019 2nd Quarter Concorde Investment Management

Domestic Economic Overview

"Economies aren't like cars. They don't just wear down and peter out after running for several years. Something needs to happen to knock them off course." This was a quote in an article from the June 3rd edition of the Wall Street Journal. July will mark the longest economic expansion on record, lasting longer than the expansion of the 1990's, even if the growth has been less than robust. Contrary to popular media belief, just because we are now in a record setting expansion, that does not mean a recession is imminent. Australia just passed its 28th straight year of growth, while other countries had expansions lasting over 15 years. There are plenty of threats looming, notably Trade wars, interest rate mistakes, and large Federal deficits, but so far nothing has managed to knock the U.S. off course. The consumer is very strong, with manageable debt level and unemployment levels are low.

Normally the expectation around low employment is that low employment begets higher wages (in order to attract talent) which in turn drives prices/inflation higher. So far, this hasn't happened which is why the Federal Reserve has not had to significantly raise rates. Most economists thought this environment was impossible, low employment/low wages/low inflation, but we've been in it for multiple years now.

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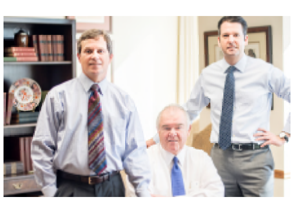
A Message from Concorde Investment Management

Last year we rolled out an app for your smartphone or tablet that allows you to view your entire portfolio as of prior day close and includes a vault where you can view your quarterly reports, billing summaries, and share documents with Concorde from a secure portal. If you are using the app and have any questions regarding or you are not yet set up and would like to utilize this feature, please contact Barbie Spicer for assistance.

The Concorde Team



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Domestic Economic Overview (continued)

The GDP growth in Q2 will be slower than the 3.2% growth in Q1, in part due to the inventory build that enhanced Q1. Earnings are not discussed in this section other than to say some companies have reported Q2 earnings and on their calls made various statements implying the same story; they were prepared for a trade war impacts to their business but those effects never showed. Every discussion of the trade war is connected to the President's reelection chances. Meaning as long as the economy is doing well, the President's reelection chances are higher. We expect the President believes this which is why we expect a trade deal to be reached with enough time to see benefit in the economic activity of the U.S. prior to the election. That would equate to a Q4 2019 or Q1 2020 deal.

International Economic Overview

Global economic activity continues to grow however the International Monetary Fund trimmed its forecast based on U.S.-China trade war concerns, the impending Brexit date on Halloween (along with Boris Johnson being the new Prime Minister), and low inflation. 2019 growth is expected to come in at 3.2%, which is slightly lower than predicted in April and .3% lower than at the start of the year.

In May, China and the U.S. hiked tariffs on billions of dollars worth of each other's goods at the drop of a hat. The market had anticipated a deal being closed in Q2 and prior to a meeting in Washington D.C., the President raised tariffs and claimed the Chinese changed deal terms at the last minute. Economic impact, outside of tariffs, are starting to show their effect in China. Companies have begun to move their supply chains out of China or are outright demanding their Chinese suppliers absorb the tariff impacts. The percentage of China-leaving businesses surveyed by quality control and supply chain auditor QIMA was 80% for American companies and 67% for those based in the European Union.

QIMA has more than just anecdotal evidence. Demand for their China-based audits dropped by 13% as mainland manufacturers are either losing their foreign clients faster due to costs associated with tariffs or are relocating part of their manufacturing out of China to avoid those tariffs. As we've wrote in the past, we believe the U.S. is better suited to handle a longer term conflict and has the correct motivations in getting a deal in place that is measurable and enforceable. The forced intellectual property transfer/theft is unacceptable. It's also the Chinese business model, which makes getting a deal done difficult. We mentioned in the last letter that we think a deal gets done this year and still feel that is most likely. If this trade war is impacting economic activity, it is only temporary until a deal gets done. Meaning, any temporary lag in economic growth should show up after a deal gets done.

Fixed Income

Despite generally encouraging domestic economic and corporate results during the quarter, yields on most fixed income securities fell which helped to add to total return gains for the year to date. The factors that continue to outweigh continued economic growth regarding lower yields include declining inflation expectations and the competing yields on major international sovereign bonds. Declining domestic inflation expectations, which have dropped from around 2.2% in mid-2018 to 1.7% at 6/30/19, are a concern for the Federal Reserve and is a primary reason why expectations are for a cut in rates for the balance of 2019 versus increases that were expected 6-9 months ago. Regarding competition from foreign government bonds, please see the table below for examples of choices that global investors have in 10-year maturity instruments.

Although the obvious attention grabbers are the negative yields in Germany, The Netherlands, Japan, and Switzerland, the yield that we highlight is the 2.26% for Greek 10-year government bonds. Although conditions are somewhat improved from the dire conditions earlier in the decade, it seems shocking that those bonds trade only 20 basis points greater than U.S. 10-year notes even with the long-term fiscal issues that we face. These Greek sovereign issues traded as high as 15% in 2015. An analysis of these various sovereign yields tends to support the logic of lower yields at least for the short term.

During the quarter most corporate and municipal yields dropped along with Treasuries, producing good total returns. Looking forward, the risks appear greatest for corporates if the economy performs below expectations over the next year (credit spreads would likely widen) and for Treasury securities if the economy and/or inflation trend higher than expected (yields would likely head higher). Continued slow growth, the most likely scenario, would not generate any additional capital gains for most fixed income securities and earning the coupon payment would be a reasonable expectation.

10-Year Government Bond Yields @ 06/30/2019			
United States	2.01%	Netherlands	-0.13%
Canada	1.58%	Greece	2.26%
Germany	-0.25%	Switzerland	-0.58%
U.K.	0.79%	Japan	-0.13%
Italy	1.64%	Australia	1.45%

Equity Markets

Domestic equity markets added to the strong recovery in the first quarter, increasing 1-5% depending on market capitalization and investing style. Generally, growth-oriented stocks outperformed value stocks and larger cap companies rose more than small cap stocks. Internationally, most developed market indices also gained although with a wide variety of returns. Broad emerging market indices including China were flat to down, although the Russian and Brazilian markets rallied strongly in U.S. dollar terms. For the quarter, two sectors which primarily include value stocks, financials and materials, posted the strongest returns among the eleven S&P groups. Likely supporting the continued uptrend were modestly positive macroeconomic results and individual corporate earnings results. Although expectations for the full year are less than the tax rate induced results in 2018, growth is likely to be positive. Interest rates should support a stabilizing single-family housing market and lower Treasury bond levels also will have a positive impact on corporate valuations.

With that said, clearly the uncertainty caused by global trade negotiations and the economic weakness in parts of Asia and developed Europe are significant threats even to continued slow growth. Although there is increasing commentary regarding current valuations as compared to the tech / media / telecommunications bubble and bust of 1998-2002, broad statistical analysis including earnings multiples, dividend yields, and ten-year Treasury yields lead us to conclude that the peak in 2000 is not comparable to current markets. Certainly, there are always individual extreme valuations, but collectively medium to large public companies are reasonably valued assuming continued very modest growth and even if bond rates move higher to some degree, say 3-3.50% for 10-year Treasuries. With the clear outperformance of growth over value-oriented stocks since the current bull market began in March 2009, weakness and volatility may present the opportunity for a reversal in that trend. We are finding select long term value investments, particularly in industrials, energy, media and healthcare.

Why Diversifying Your Portfolio is Important

Source: Advisors Websites

If you're a beginning investor, it's likely you're concentrating on building your portfolio. But as important as it is to build that portfolio, you should also ensure that it's diversified.

Why is a diversified portfolio so important?

There are three key reasons why diversifying is important:

1. A diversified portfolio helps minimize risk. Stocks can be a risky investment at any time, but with a diversified portfolio, you can help minimize the risk by spreading that risk among a variety of investments.
2. Diversifying can help investors maintain capital. Someone purchasing stock at the age of 30 has a much different investment goal than someone age 50. For older investors, it may be much more important to maintain capital than it is to increase capital.
3. You'll have a much better chance at generating dividends if your portfolio of stocks is diversified. When one stock is performing well, chances are that another stock has dipped. By having a significant investment in both, you'll help to offset any potential losses from underperforming stock.

It's also common for one particular type of asset to perform better over a specific period of time, depending on external factors such as

- Current interest rates
- Currency markets
- Current market conditions

But it's also important to remember that while one investment may be outperforming others, the standard is that there is no particular investment that will continually outperform others over the long term.

But what is a diversified portfolio?

A diversified portfolio is one where investments vary, with exposure to one particular type of asset is limited. Diversifying can look like two very different things to young investors and those nearing retirement age. Young investors are much more likely to be comfortable riding out the peaks and valleys of their investment portfolio, while investors nearing retirement age are more likely to be interested in slow growth and a more consistent performance without the volatility that more risky investments may face.

In order to truly diversify your investment portfolio, many professionals recommend that your portfolio consists of the following:

1. Domestic Stocks. Stocks are perhaps the most volatile investment in a portfolio, but they also represent the best chance for growth. Short term investment in stocks carries the biggest risk, but stocks can also provide the biggest reward if they are held on to for a significant amount of time.
2. Bonds. Considered less volatile than stocks, bonds can provide a shield against market instability created by stock investments. Stocks also typically provide regular interest income. For those looking for a more significant return, high-yields bonds can be purchased, but they also carry a higher-risk.
3. Money Market Investments. While ultra-conservative, money market accounts and similar investments such as a short-term CD can provide stability and safety that other investment options may not.
4. International Stock. International stock can provide a higher return than their U.S. counterparts, but they can also carry a higher risk. However, for those looking to diversify their portfolio, international stock can be a good addition.

The key to diversification is to find the right balance between risk and stability and add accordingly, which allows you to reach your goals while also worrying less.