July 9, 2019

“Talk is cheap. Words are plentiful. Deeds are precious”
-Ross Perot

When we shared with some peers that we were planning to discuss the friction between the President and the Federal Reserve and its impact on the stock and bond markets many suggested we were crazy. We’d upset someone given our increasingly polarized nation. In the spirit of Allen Hilton, leader of House United, an organization that aims to narrow the political rift in America, we’re going to attempt a “courageous conversation” and share our non-politically intended analysis of the Federal Reserve vs. Executive branch disagreement.

Regardless of whether you’re a fan or foe, one must acknowledge that President Trump is a master of commanding attention. Most recently his public criticism of Federal Reserve Chairman Jerome Powell has been the rod attracting the media lightning. Historically disagreements have been handled behind closed doors because the independence of the Federal Reserve is one of the cornerstones of American monetary policy. President Trump is not your conventional politician and he has been vocal in his criticism of Mr. Powell for not providing a more accommodative monetary policy while the President is working to renegotiate trade agreements with China.

President Trump believes that the independent Federal Reserve puts America at a disadvantage. China’s central bank is under control of the Chinese Administration and it enacts policies desired by its central government. The Federal Reserve has a dual mandate to maximize employment while also keeping inflation low following policies that are less exposed to political pressure. For the last four years the Fed has been gradually raising rates and unwinding quantitative easing strategies it implemented during the 2008 financial crisis, repositioning monetary policy back to neutral.

The President was elected on a platform promising to bring jobs back to America and to negotiate more favorable trade agreements worldwide. In September 2018 the Trump administration decided to elevate pressure on China to renegotiate trade deals by implementing tariffs and threatening to intensify them should a new trade agreement fail to materialize. This sent shockwaves through global supply chains causing many American manufacturers to seek alternative suppliers away from China. The US economy slowed. President Trump became upset that the Fed appeared to be more focused on returning monetary policy to “neutral” than on supporting the American economy as it experienced a shock from the brewing trade war. The stock market fell 14% in the fourth quarter, wiping out gains for the year as uncertainty increased.

By early January the Federal Reserve changed its messaging to the markets indicating it would place greater emphasis on recent economic data and pause further interest rate hikes. The stock market rallied on the news and bond yields plunged from 3.2% last fall to 2.0% at the end of the second quarter. In his latest testimony to Congress, Chairman

Powell signaled a further move toward easing monetary policy so that now the Fed has positioned itself to be a backstop for the economy should the trade war with China escalate.

During the trade negotiations the market has responded to each ebb and flow of the process. We believe reacting to ongoing discussions is risky, especially as the Fed has signaled its willingness to be more accommodative. Our strategy remains one of being long term oriented investors that own companies generating free cash flow run by management teams that reinvest the cash to grow their businesses or return it to shareholders through dividend increases or share buybacks. We seek to mitigate risk by keeping money clients may need in the near term in more liquid investments so that clients are not forced to sell stocks to meet short term needs during a temporary market swoon. If a business fails to meet our expectation, we sell it. A study conducted by Blackrock reviewed stock market returns since 1928. If an investor was to invest and hold only for a month then the investor would make money 62% of the time. However, if the investor had a holding period of 10 years the investor would make money 95% of the time. Market timing is very difficult because one must be correct on when to sell and also on when to buy back into the market. Clearly the odds favor long term investors, plus the capital gains incurred are less onerous.

Thank you for entrusting Ayrshire Capital Management with your money. We look forward to speaking with you in the coming quarter.

Sincerely,

JM Sam Nevin, Jr
Managing Partner

W. Joseph Ryan III
Partner