Basis Points

Weekly Market Commentary

Basis Points – March 28, 2019

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Above the Fold

- The inversion of the yield curve has taken center stage as investor worry of the week. The yield on the 10-year government bond, at 2.36%, is lower than the yield on the two-year bond at 2.41%. This type of inversion is rare, as it indicates that bond buyers prefer a lower yield and a longer term compared to a higher yield and a shorter term. This preference has historically indicated that investors believe the economy is slowing rapidly, which will lead to the Fed cutting short-term rates sharply. Anticipating a cut in short rates, bond buyers prefer to lock in an acceptable yield for a longer period. The inversion of the yield curve has been a somewhat reliable precursor to an eventual recession, but the record is not perfect and typically a recession follows the inversion over the next 12 to 18 months. There is strong debate this week about what, if anything, the inversion is telling the market about the economy. Some investors have discounted news of the inversion as the economy is strong, unemployment is low, consumer and business confidence are high and worker wages are rising.
- One specific metric in the inversion debate that market bulls point to is spreads in the corporate bond and high yield market. If the economy was in fact slowing at an alarming rate, this concern would be reflected in the health of the corporate bond market. However, spreads are still currently very low, indicating that corporate and high yield bond buyers are not yet worried about the credit health of the underlying issuers. Bond investor worries about the creditworthiness of companies would certainly be reflected in higher bond yields. The yield curve last inverted in 2007, but at that time high yield spreads had widened considerably, presaging the 2008-09 recession and financial crisis. We are not currently seeing any signs of a similar dislocation in the high yield market, however.
- McDonald’s announced the acquisition of Dynamic Yield (DY), a leader in digital personalization and decision logic technology, for $300 million. It is notable as

McDonald's first acquisition in years but very much in keeping with the company's strategy to embrace technology to improve the customer experience. McDonald's will use DY's technology to provide a more personalized and highly targeted guest experience by leveraging customer data and making digital menu boards in the drive-thru smarter. The technology will use artificial intelligence to vary the content displayed on the menu boards based on time of day, weather, current restaurant traffic and trending menu items. DY will continue to operate as a stand-alone company, serving more than 300 brands around the world.

Three Things

- Strategas Research noted that for the first time in history, a congressional committee will vote this week on a cannabis banking bill. The House Financial Services Committee is expected to pass the Secure and Fair Enforcement (SAFE) Banking Act, moving it to the full House where the legislation has 143 cosponsors, including over a dozen Republicans. SAFE allows banks to offer services to cannabis companies with federal protection so long as the companies comply with state laws. Currently, cannabis companies are often forced to operate on a cash-only basis because marijuana remains illegal at the federal level and financial services companies could be found guilty of money laundering or drug law violations. The SAFE Banking Act does not change the legal status or drug classification of marijuana at the federal level, so most banks, especially large ones, will likely not service cannabis companies yet. Most announced Democratic candidates for president have given support to the legalization of marijuana at the federal level, so expect the topic to be debated throughout the 2020 run for the White House.
- Does anyone answer their phone anymore if it flashes a number that is not identified? Blame the robo-calls. More than 10 billion robo-calls have been placed so far this year, twice as many as this time last year, and industry groups estimate that half of all calls placed this year will be scams. The Do Not Call registry initiative in 2003 was effective for a while, but then came the proliferation of mobile phones, off-shore auto-dialing firms out of the jurisdiction of the FCC and technology that can mask the location of calls. Some call-block apps may help, such as HiYa, RoboKiller, TrueCaller and Mr. Number. Or you can call your carrier and they can code your account to block robo-calls. I did this with AT&T and it has quieted my phone considerably.
- The Ross Perot family in Dallas has hired a veteran hedge-fund trader as its new investment chief. Boaz Sidikaro, 44, started at the multibillion-dollar Perot Investments in March after more than 20 years at New York hedge-fund firm Och-Ziff Capital. Sidikaro takes the reins from Steve Blasnik, the family's CIO for more than 30 years. Sidikaro will run the 20-person team that invests across asset classes and in outside money managers. Perot Investments also runs an aircraft-leasing business, a holding company of radio stations and regularly takes stakes in other businesses. The family's wealth can be traced back to Mr. Perot's 1984 sale of his

> businesses. The family's wealth can be traced back to Mr. Perot's 1984 sale of his Electronic Data Systems to GM for $2.6 billion. Perot hired Blasnik, who had advised him on both transactions, to manage his large post-deal cash pile. Perot and his son, H. Ross Perot Jr., founded Perot Systems, which they later sold to Dell for $3.9 billion.

Did You Know

Driving in New York is about to get more expensive.

The New York Times notes that New York City looks to become the first U.S. city to implement a congestion charge on cars, with a toll to be placed on vehicles entering some of the most gridlocked areas of Manhattan. The money made from the tolls is expected to be used on Metropolitan Transportation Authority subway repairs, according to state officials. Los Angeles, San Francisco and Seattle are mulling a similar idea, while London, Singapore and Stockholm have already put it into practice, and supporters say it reduces pollution and makes cities safer for pedestrians.

The proceeds from congestion pricing are expected to enable the Metropolitan Transportation Authority, which operates the city's public transit network, to raise billions of dollars in bonds to modernize the antiquated subway. Such a windfall overwhelmed lingering concerns about various aspects of the plan, including the cost to commuters in the boroughs and suburbs outside Manhattan who rely on autos.

Those arguments have been bolstered by the success of plans in places like London, Stockholm and Singapore, where congestion pricing helped unclog streets. Still, such plans have also been derided by drivers and critics as an unfair tax that especially hurts poor people who do not have access to public transit.