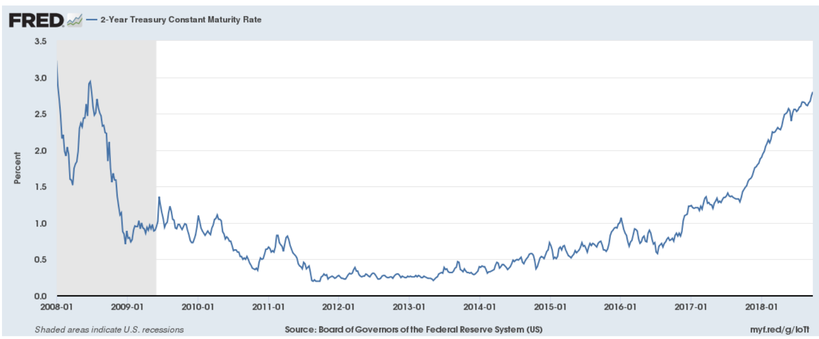
MANAGEMENT, LLC
www.arxmgmt.com

SEPTEMBER 2018 MARKET COMMENTARY *"I Don't Know"*

"Don't look at me for answers. Don't ask me. I don't know." -Ozzy Osbourne

That could have just as easily been Fed Chairman Jay Powell at his press conference, after raising rates ¼ point to 2-2 ¼% last week. For the past two years, investors have pretty much been able to count on a 25 basis-point increase in interest rates each quarter, as the Fed raced to shift away from its ultra-accommodative policy toward a "neutral" Fed Funds level, where monetary policy is neither inflationary nor restrictive. By no longer characterizing its policy as "accommodative", the Fed is giving itself the flexibility to pause tightening or respond to unanticipated market events.



The 2-year U.S. Treasury yield reached a level not seen since the Financial Crisis.

Treasury rates rose across the curve during September, in anticipation of the 9/26 rate hike but also reflecting the view that a strong US economy will continue to push inflation higher. Short- and long-term rates increased approximately 20 basis points, putting the yield curve's flattening bias on hold. As such, there has been less chatter about an impending recession, even though the looming risks we've previously detailed still exist. Chairman Powell said as much this month when he stated that The Fed *"is navigating between the shoals…with only a hazy view of what seem to be shifting navigational tides"*.[1] Chief among these questions is how the economy and markets will respond to the Fed pulling the punch bowl away with both hands – raising rates and unwinding its massive quantitative easing program – during a record bull market that is beginning to show some cracks. Consider the shift away from banks toward asset managers as the new providers of liquidity, and the Fed has no playbook to reference when attempting to predict the effects of a massive removal of accommodation.

Equities paused after setting a record for the longest US bull market in August, as the S&P added just 0.4%. Stock volatility remained low, but we could see this pick up as Q3 earnings season approaches, imbalances between the US and other developed markets persist, and select emerging markets remain distressed.

Outlook:

We expect short-term rates to keep trending higher into another Fed tightening in December or January. Longer maturities seem range bound, with resistance around 3.15% on 10s and 3.25% on the long bond, so we expect the curve flattening to resume. We still believe short-term bonds possess the best risk/return profile, offering the perfect environment for actively managed Qualified Settlement Funds – a relative no-brainer compared to low paying bank escrow programs.

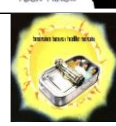
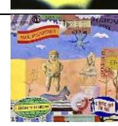
[1] https://twitter.com/arxceo/status/1040677990554722304

www.arxmgmt.com

Market Snapshot:

	8/31/18	9/30/18	Change
Fed Funds Target Rate	1.75-2.00%	2.00-2.25%	+25
3-month US Treasury	2.10	2.18	+8
2-year US Treasury	2.63	2.81	+18
10-year US Treasury	2.85	3.05	+20
30-year US Treasury	3.01	3.20	+19
S&P 500	2,901	2,914	+0.4%
Stock Mkt Volatility (VIX)	12.86	12.12	-0.74
US Dollar (DXY)	$95.10	$95.13	UNCH
Oil	$69.88	$73.56	+5.3%
Gold	$1,212	$1,196	-1.3%
Bitcoin	$7,013	$6,567	-6.4%

ARX Spotify "I Don't Know" Playlist:

Q:	A:
What will be the "neutral" Fed Funds rate?	 Ozzy Osbourne
How will rate hikes and QT make this market cycle different?	 The Beastie Boys
Is strong US growth organic or the last of the sugar high?	 Paul McCartney
How many more rate hikes before the yield curve inverts?	 The Replacements

About ARX Management:

Established by professionals with direct experience in complex litigation and institutional investment management, ARX offers an unmatched mix of skills relevant to managing 1.468B Qualified Settlement Funds. Prior to establishing ARX in 2011, our partners actively managed $8 billion in fixed income assets for a large institutional investment manager. Our expertise investing conservative capital preservation products is directly applicable to the management of institutional QSFs. Contact us today at arxadmin@arxmgmt.com or meet with us at Mass Torts Made Perfect in Las Vegas this week.