fin|news

TRENDS | 09.13.23

Short-Term Bonds, U.S. Stocks Attractive As Recession Signals Fade: Angeles Investment Advisors

By JUSTIN SLAUGHTER

With the prospects of a recession or bear market moving farther away, short-duration bonds and U.S. public equities are increasingly attractive for institutional investors, according to **Angeles Investment Advisors** CIO **Michael Rosen**.

The possibilities of either a structural bear market, caused by excessive leverage or valuations, or a cyclical bear market, spurred by events like the tightening of the money supply or inflation, in today's economy seem less likely at this time than many institutional investors predict, Rosen said, in a recent interview at the firm's Manhattan office.

"Some traditional signals of a recession are still here, like an inverted yield curve, some slowdown in housing activity and some weakness in manufacturing output … However, there are some mitigating factors around those signals," he said.

The housing market in the U.S. has slowed down slightly, in part due to rising mortgage rates that dissuaded many homeowners from selling their homes, effectively limiting supply and elevating prices, while some recent Annual Survey of Manufactures data shows "manufacturing is low, but not dramatically low," Rosen added.

At the same time, the levels of economic growth and employment remain elevated in the U.S., driven by strong consumer spending, leading the Santa Monica, Calif.-based outsourced cio to overweight short-duration fixed-income and U.S. equites within its portfolios.

"The initial jobless claims are at the lowest levels in years, which doesn't signal a recession is imminent, not at all. If anything, the opposite is true. The economy is accelerating. The third quarter numbers for the GDP will be higher than in the second quarter. We've seen already, the GDP numbers revised to be higher by some economist estimates," Rosen said.

Initial claims for state unemployment benefits were 216,000 in the week ending Sept. 2, the lowest since the same level was reached during the week ending Feb. 11 and the fourth straight weekly decline, according to data from the *U.S. Department of Labor*. The Federal Reserve Bank of Atlanta estimated the U.S. economy's real gross domestic product growth will be 5.6% during the third quarter, an increase from the 3.5% growth rate the branch had first estimated on July 28, according to its data.

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Many of these factors are why Angeles has tilted its fixed-income portfolio toward short duration assets as a way to "capture the return from the inverted yield curve by taking our position on the short end of the curve," Rosen said.

"The market is projecting a significant recession that would require the [Federal Reserve] to cut rates dramatically and quickly. But that scenario doesn't make sense and requires you to give up a significant amount of basis points by extending duration. The market is confident that is near, but I'm not confident," he said.

"To me the biggest disconnect is the yield curve, how steep it is inverted and how long it has been inverted … Even if I'm wrong, if the Fed starts cutting rates, from an investment perspective, you still want to stay short. You're giving up so much yield to extend duration, that the Fed would have to cut so much of its rates to make that worth it. I can't see the Fed cutting rates to that extent," Rosen added.

In part because of strong market factors staving off a bear market, Angeles Investments is "overweight U.S. assets," including equities, which is a "reflection of the relative strength and attractiveness of U.S. markets" compared to Europe and Asia, according to Rosen.

"The European markets, with a war going on next door that could flow over, had good reasons for underperformance," he said, noting the spike in energy prices on the continent due to the ongoing Russia-Ukraine War and disrupted trade between European countries and China make European-based assets less attractive.

And by contrast to U.S.-based equity, emerging markets equity strategies remain less attractive than U.S. equities due to the general overweight exposure to China, where the economy has shown a dramatic slowdown recently due in large part to the country overbuilding its real estate market, he said.

"Real estate, to a great degree, was a source of wealth in China, with people buying apartments as investments, as a storage of wealth, as opposed to keeping investments in banks. We've all seen the overbuilding that has occurred. That creates the reasons why the economy has slowed dramatically. And also, the statistics aren't ever very believable before and now [the government] stopped publishing them, and that tells you the statistics are a lot worse. So, there are a lot of challenges to investing in China," Rosen said.

In contrast, the American economy is healthier due to the nation's consumers who are "really driving the economy," Rosen finds.

"Consumers are in good shape. Households are less leveraged. Consumers are spending savings built up during the pandemic. Income and wages are up, particularly the nominal wages, which have shown 5% to 6% growth," he said, adding that this is particularly true for "low-wage earners that spend all their money and that helps drive the economic activity."

"And just the anecdotal evidence, you see every airplane seat is full, every restaurant is full, and every **Beyonce** and **Taylor Swift** show is full," Rosen noted.

Rosen co-founded Angeles in 2001 alongside **Howard Perlow**, who was named as the firm's ceo in the second quarter.

Angeles has approximately $6.4 billion in fully discretionary outsourced cio assets and $34.8 billion in non-discretionary assets, according to its website.

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