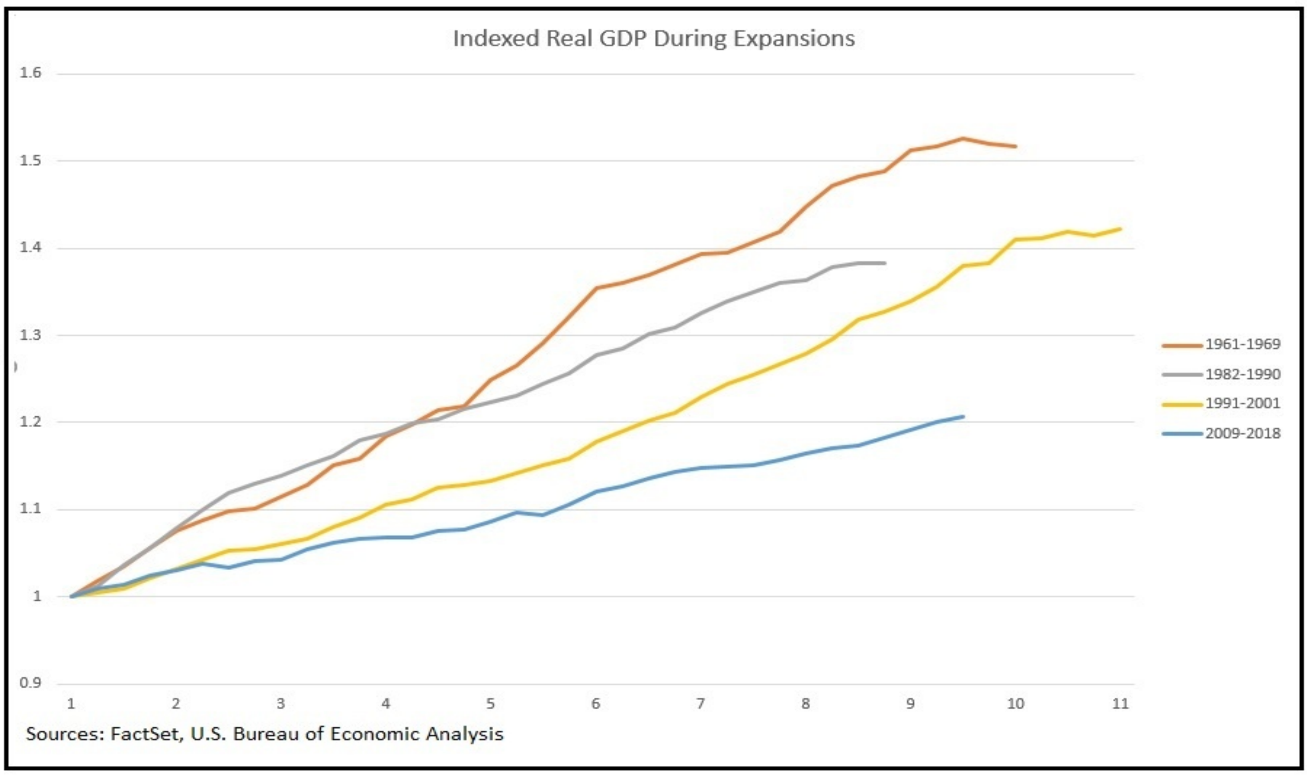
This month, the current U.S. expansion reaches the 107-month mark, making it the second longest business cycle expansion since World War II. Having just surpassed the 1961-70 expansion (106 months), the next milestone is the 1991-2001 expansion of 120 months. With a recession nowhere in the forecast between now and 2020, it is increasingly likely that this expansion will last at least another year and become the longest of the post-war period.

The length of the current expansion has often been overshadowed by concerns over its lack of depth or breadth. Through the first quarter of 2018, real GDP had grown by only 21% since the Great Recession, far lower than the 36% growth that had been experienced during the same period of the 1991-2001 recovery. Interestingly, the growth path of our economic expansions (chart, below) has been shifting



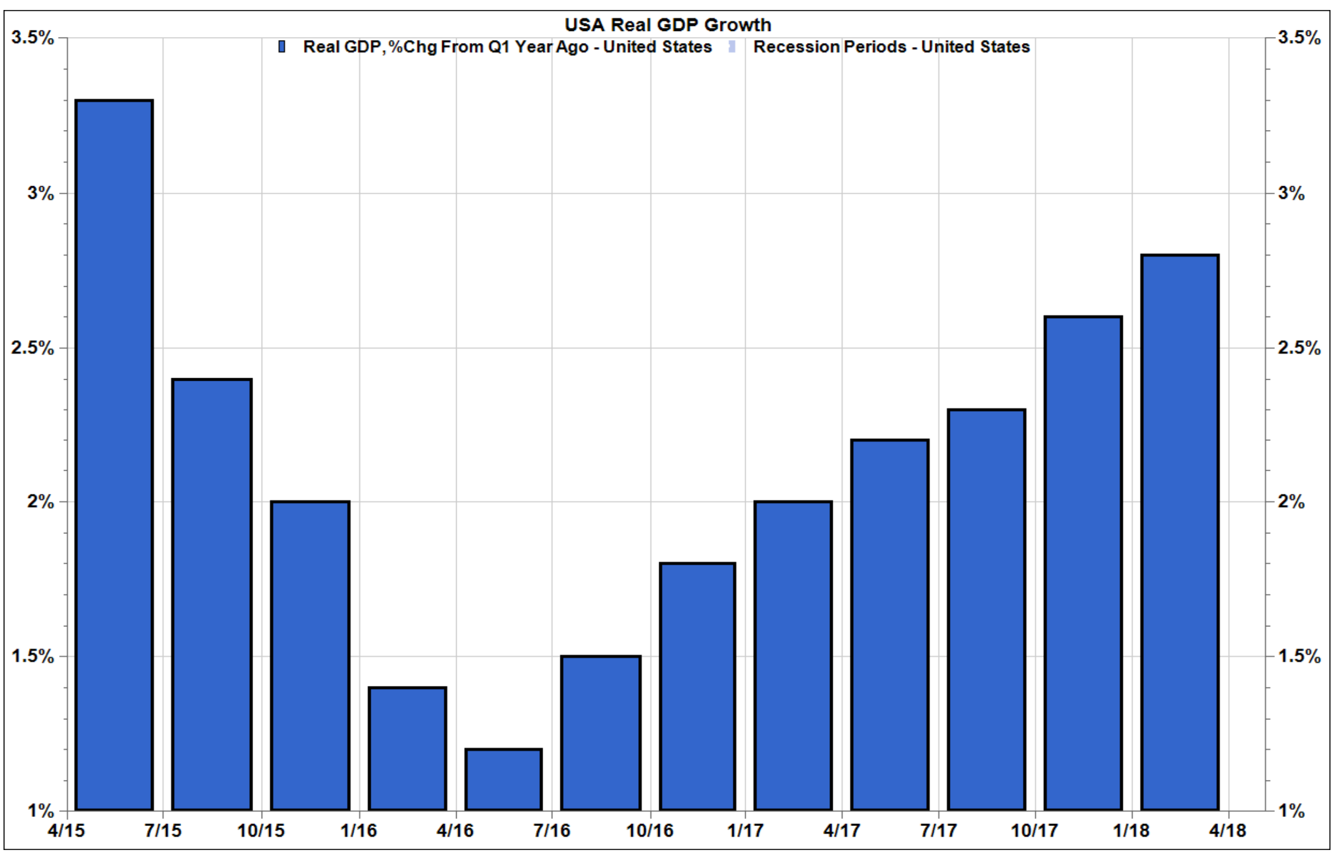
lower over time. Just as the current growth rate lags behind what was generated during the 1991-2001 expansion, that expansion similarly lagged what was experienced during the 1980s, which in turn lagged the growth seen in the 1960s. Demographic changes undoubtedly account for some of this phenomenon, and productivity growth has remained elusive despite tax inducements and several generations of new technologies.

Personal consumption, which comprises 70% of GDP, has been a major contributor to our overall sluggish economic performance. This is understandable when you consider the fact that household net worth declined more than 14% during the 2008-09 recession. In fact, the 2008-09 recession was the *only* recession preceding the four longest expansions where there was a decline in household net worth. It didn't help that wage growth remained sluggish during the early years of the recovery, though it has picked up as the economy has reached full employment.

Consumers are not the only group to have shown uncharacteristic restraint during this economic expansion; investment from the private (non-government) sector has materially lagged the levels of prior expansions. Normally, you would expect a low interest rate environment to spur investment spending. However, the hangover from the real estate collapse left both consumers and businesses reluctant to incur additional debt, and a more restrictive regulatory environment made banks more reluctant to lend money.

The point of this exercise is to try to understand where we are in the context of where we've been. The comparative weakness of the current expansion was the consequence of the financial crisis that preceded it, not bad trade deals or high corporate tax rates. But the Fed's response to that weakness has resulted in what will likely become the longest peacetime expansion in our history, with an economy that is now at full employment - the lowest unemployment rate since April 2000. Wages are rising once again, and there are more job openings than there are qualified applicants to fill them.

Real GDP growth (chart, below) has accelerated on a year-over-year basis for the last seven quarters. The regulatory environment has eased and businesses have been given greater inducements to invest. Inflation is finally approaching the Federal Reserve's 2% target, and the Fed appears poised to continue on its measured path to "normalized" rates.



In spite of all the good news, the S&P 500 Index is up barely 1% year to date. If the early years of this expansion were characterized by a rising market and a muted economic recovery, we are now experiencing just the opposite - a rising economy and a muted market reaction to good news. Perhaps investors are now more aware of the old adage that expansions don't die of old age, they are killed off by policy mistakes. Positive earnings and economic reports are intermittently obscured by an "on again, off again" trade war with China, and counter-productive tariffs on steel and aluminum imports from Canada, Mexico, and the European Union, among other suppliers. Geo-political risks seem to be growing, not abating, and a messy political season is about to start. There is also the fear that a tax cut so late in an economic expansion may cause the Fed to raise rates faster than expected.

Whatever the concerns, it is increasingly clear that much of today's good news is already priced into the market, which is now in the process of discounting a more uncertain future. In that context, we find the market's muted reaction to be oddly reassuring.

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