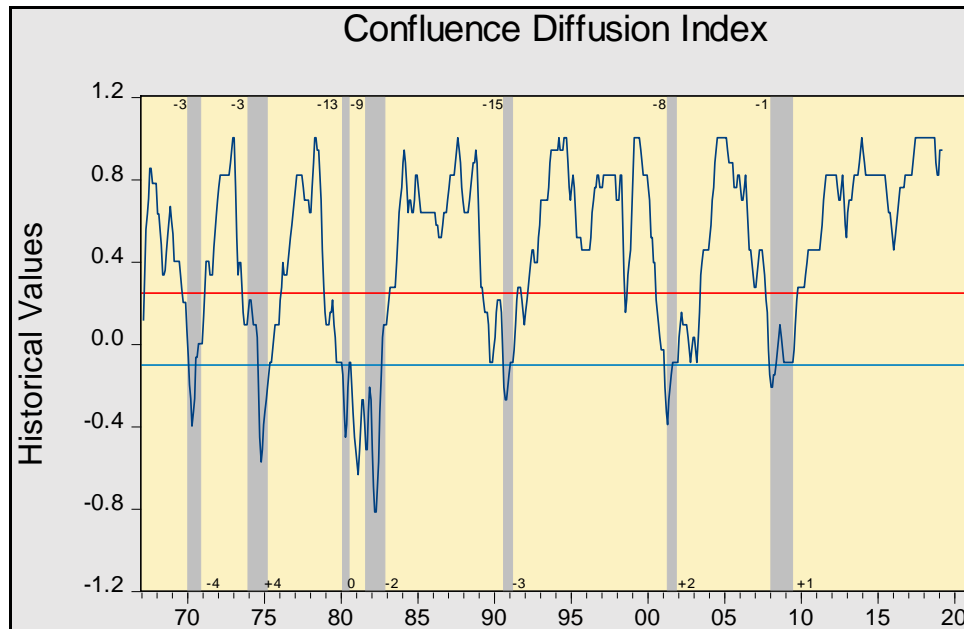
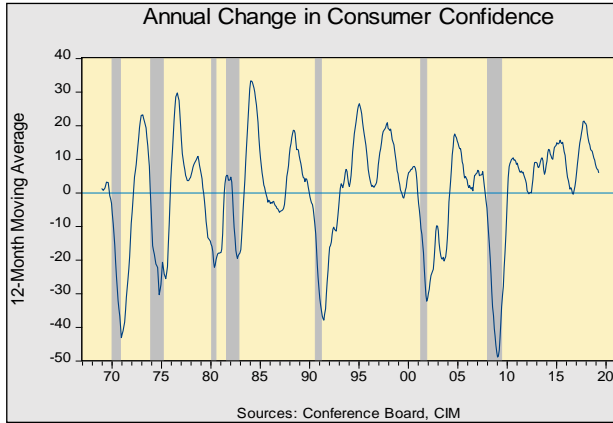


The business cycle has a major impact on financial markets; recessions usually accompany bear markets in equities. We have created this report to keep our readers apprised of the potential for recession, which we plan to update on a monthly basis. Although it isn't the final word on our views about recession, it is part of our process in signaling the potential for a downturn.

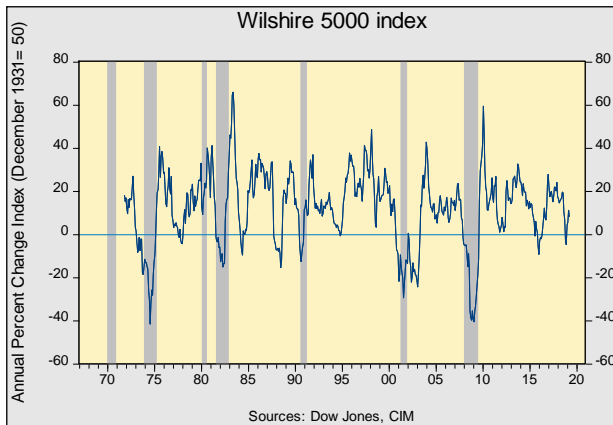
Economic data released for April suggests the economy remains strong but is showing some signs of weakness. Currently, our diffusion index shows that 11 out of 11 indicators are in expansion territory, with several indicators approaching warning territory. The index currently sits at +0.939.



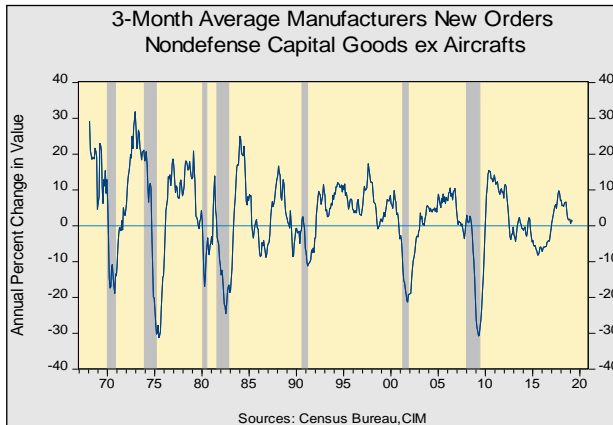
The chart above shows the Confluence Diffusion Index. It uses a three-month moving average of 11 leading indicators to track the state of the business cycle. The red line signals when the business cycle is headed toward a contraction, while the blue line signals when the business cycle is headed toward a recovery. On average, the diffusion index provides about eight months of lead time for a contraction and one month for a recovery. Continue reading for a more in-depth understanding of how the indicators are performing.



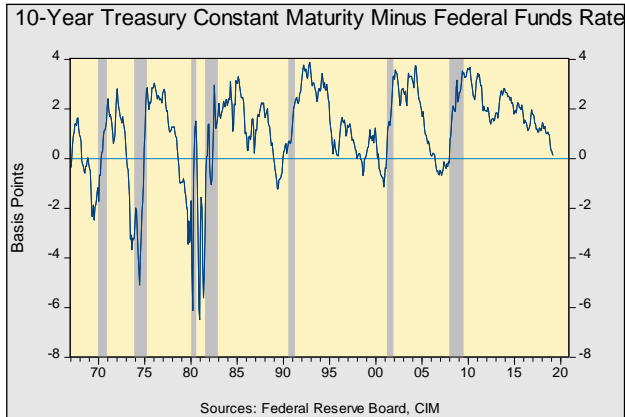
The Consumer Confidence Index is an economic indicator that measures the level of consumer optimism about the overall state of the economy and consumers' personal financial situations. The chart on the left shows the 12-month moving average of the annual change of the index. The 12-month average rose 5.81% from the prior year.



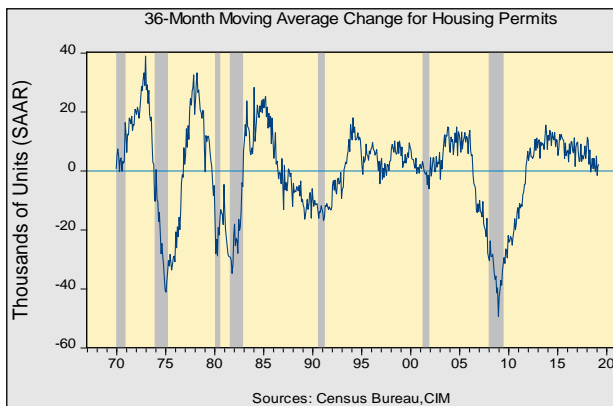
This chart shows the annual change in the Wilshire 5000 Index, which is the broadest U.S. equity index. The index contains 3,500 stocks and is designed to track overall performance of the U.S. stock market. This is an important indicator because steep equity pullbacks have often coincided with economic contractions. The latest reading shows an annual change of 9.17%.



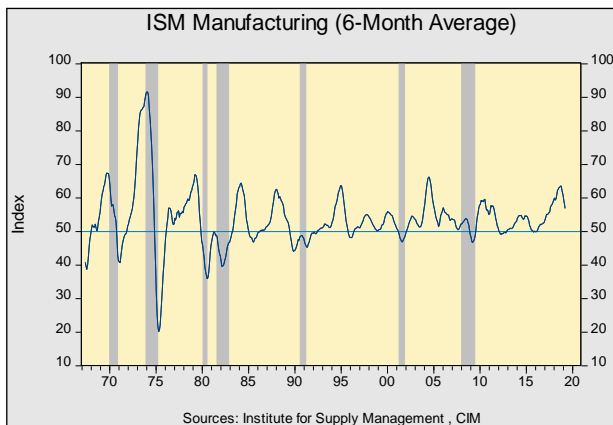
This chart shows the annual change in the value of core capital goods orders. This indicator gives insight into the amount of business investment spending. A positive reports suggests that manufacturers are optimistic about future demand. The current reading shows an increase of 1.09%. The moderation in the pace of capital goods orders signals that business activity may be slowing.



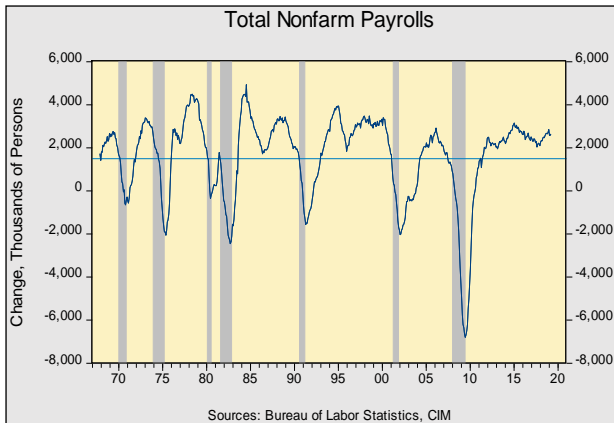
This chart shows the spread between the 10-year maturity and the Fed funds rate. It reflects market sentiment of the future state of the economy. Generally speaking, a negative spread suggests a contraction is likely to occur within 24 months. Currently, the reading remains positive at 0.11%. The narrowing of the spread is largely due to a rise in the effective funds rate as it approaches its upper bound and a declining 10-year Treasury rate due to rising trade tensions.



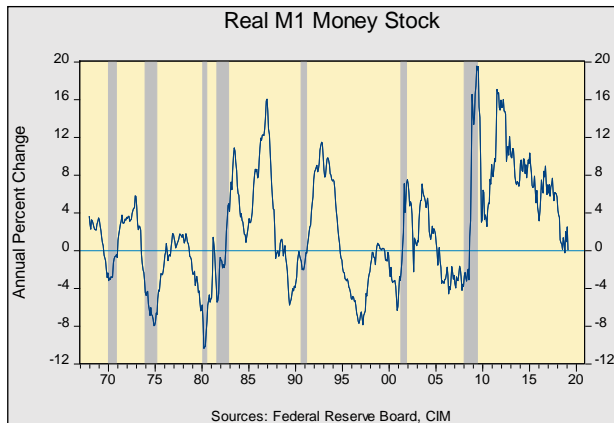
This chart shows the 36-month moving average of the annual change in housing permits. This is an important indicator because it provides a gauge of future construction activity. If housing permits are strong it implies that builders are optimistic about future demand. A reading below zero suggests the economy may be losing steam. The current reading is 2.08%, slightly above the recession indicator.



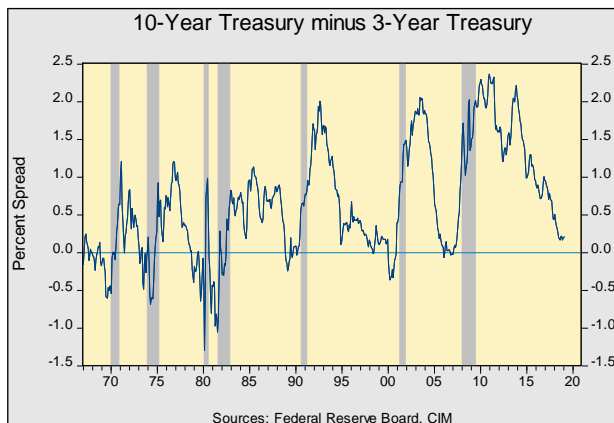
The ISM Manufacturing Index is a report that monitors employment, production, inventories, new orders and supplier deliveries. This index shows a six-month moving average and is used to gauge the level of manufacturing activity. A reading above 50 signals that manufacturing activity is expanding, while a reading below 50 signals that manufacturing activity is contracting. The current reading of 56.7 indicates that manufacturing activity remains robust.



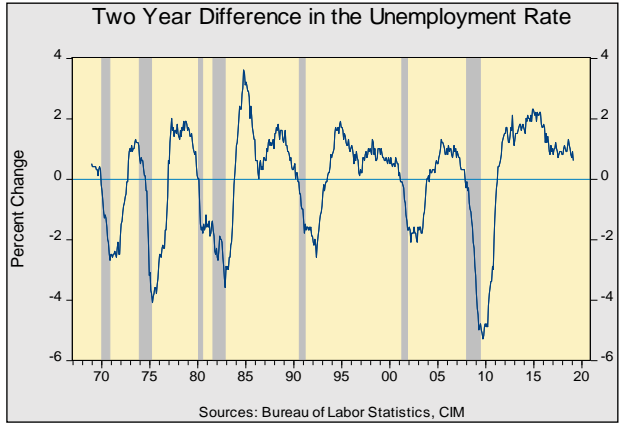
This chart shows the 12-month moving sum of total nonfarm payrolls. This report represents the total number of workers added to the workforce excluding proprietors, private household employees, unpaid volunteers, farm employees and incorporated self-employed. It is a significant indicator of the strength of the labor market. A moving sum that falls below 1,800 suggests the economy is in contraction territory. The latest reading of 2,620 indicates the labor market remains tight.



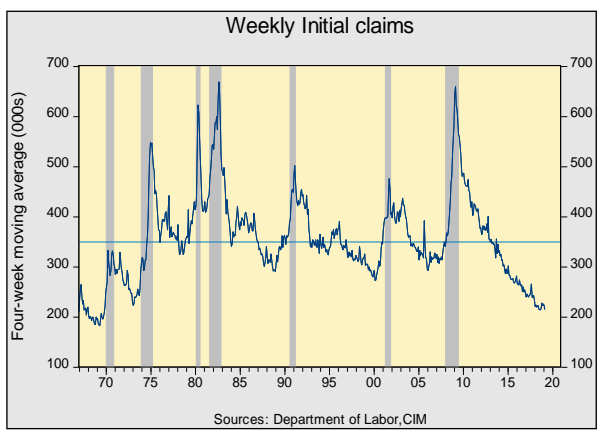
The Real M1 Money Stock report measures the annual change in the money supply minus inflation. M1 is the measure of currency in circulation and represents the amount of money being held for transaction purposes, therefore it can act as a proxy for economic activity. The latest reading is 1.35%, which is slightly above the recession indicator.



This chart shows the spread between the 10-year and three-year Treasury, a gauge of investor sentiment. A widening spread suggests investors are optimistic about the state of the economy, whereas a negative spread suggests pessimism. This indicator is less sensitive than the financial spread as it is less affected by the Fed's decisions. The latest reading is +0.22, which indicates waning optimism among investors.



The two-year difference in the unemployment rate measures the amount of slack in the labor market. When the difference of the two-year unemployment rate falls below zero it indicates the labor market is becoming less tight. The latest reading of +0.8 suggests the labor market is still tight.



This chart shows the four-week moving average of initial jobless claims. A rising initial claims number means the demand for labor is weakening, likely due to a worsening business environment. If the four-week moving average rises above 350k, it signals that the economy may be headed for a contraction. The latest reading of 214k indicates that business sentiment is still strong.

Thomas Wash
 May 29, 2019

This report was prepared by Confluence Investment Management LLC and reflects the current opinions of the author. It is based upon sources and data believed to be accurate and reliable. Opinions and forward looking statements expressed are subject to change. This is not a solicitation or an offer to buy or sell any security.