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Economic & Market Summary
April 2019

Economic and market data depict a slowing but healthy US economy. Manufacturing and housing have continued to soften, and the flat yield curve warrants close observation. However, claims for unemployment benefits are extremely low, wages are growing briskly, and corporate bond spreads have shrunk since spiking late last year. Trade remains an area of concern. Many businesses are anxious about the US-China trade dispute, and our sense is that economic growth is being negatively impacted. Yet, the recent news flow has been encouraging. While an errant remark (or tweet) from either side could torpedo the momentum, a mutually beneficial deal seems within reach. We believe GDP growth will moderate to 2% - 2.5% in 2019 from 3.0% in 2018.

Economic growth in the European Union and China is losing steam. The European Central Bank (ECB) cut its growth forecast for the EU from 1.7% to 1.1%. China is targeting growth of 6% - 6.5%, down from 6.6% last year. Central bankers are responding. The ECB will soon offer new low-cost loans for banks, and the Chinese central bank injected $83B into their financial system. China went one step further by introducing a $298B tax cut which includes a sizable three point reduction in the value-added tax rate for the manufacturing sector and a one point reduction for transportation and construction companies.

US monetary authorities have adopted a more cautionary policy stance compared to 90 days ago. In December, Fed officials projected two interest rate hikes in 2019. In March, reacting to below-target inflation, financial market instability, and slowing global growth, the Fed guided to no rate increases for this year and announced plans to end the balance sheet runoff sooner than expected. Pausing rate hikes for now is the right move in our view. The flattening yield curve could be signaling that monetary policy is already neutral. With the shift in tone, the Fed is setting a precedent of policy flexibility. While we are encouraged by the pragmatism, too much flexibility could suggest the Fed is easily swayed by short-term data and external political pressure. Central bank independence and credibility drive sound monetary policy which ultimately supports long-term economic stability.

With the Fed pausing, stocks have rebounded sharply off their December lows. Valuations are above historical averages but still within a range we consider “fair”. The forward PE ratio for the S&P 500 is about 17x - below the 19x we saw in January 2018 when optimism was high but up from the 13.5x December low. Earnings for 2019 are expected to grow about 4% year-over-year. This looks more realistic to us compared to the 9% growth anticipated a few months ago. Rising labor costs, moderating growth, tariffs, and a stronger US dollar will lead to challenging comparisons vs last year. Key risks include a Fed policy error, a breakdown of US-China trade negotiations, and a further deceleration of economic growth in China and Europe. Despite some cautionary signals, the US economy remains healthy and the investing environment is generally favorable.

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To request our SEC Form ADV Part II, please contact Michael L. Wise, Chief Compliance Officer, at the address above.