OmniStar financial group

Market Perspectives

A Glance at How the World Affects You

November 27, 2018

2019 Interest rates and inflation shouldn't represent a serious roadblock to equities.

Economic and corporate earnings fundamentals have remained relatively positive over the past few months amid increasing volatility; many stocks have entered correction territory. Investor concerns have grown as a number of issues remain unclear; trade talks, oil price declines, strengthening (U.S.) dollar and unresolved monetary policy. The year 2018 is almost in the rear-view mirror, but significant events over the last 12 months will continue to shape economic outcomes.

On the whole, we think the global economy is expanding and reasonably solid, but recent trade conflict presents a significant and serious threat.

An escalating trade war could quickly suppress global growth and produce fear in corporate management teams. On a positive note, tensions between the U.S. and China appear have eased in recent weeks and conversations have resumed. Nevertheless, investors are not ready to accept this as the end of potential trade wars. To refuel confidence, investors want empirical evidence that additional tariffs will be contained. From our perspective, a worsening trade environment is negative for growth in the short term.

Next year is just around the bin and the strong U.S. dollar is negatively affecting U.S. growth. However, the recent decline in oil prices is providing some relief. Still, we have been suggesting that total growth will slow in 2019 and that outcome appears reasonable. Nevertheless, we don't expect anything more than a moderate pullback. U.S. real gross domestic product growth should exceed 2% in the coming year.

Notwithstanding economic uncertainty, corporate earnings growth has been stable throughout this year. Hiring and job creation has been strong, job openings are plentiful and corporate profits have been outstanding, helped largely by the late-2017 tax bill. However, rising protectionism, higher interest rates, the stronger dollar and wage pressures have clouded expectations for the coming year. Our outlook for corporate earnings is similar to the global economy: We expect a slowdown with an overall positive trend.

Reiterating our stance on a modest reduction in economic growth, current fiscal and monetary policy should remain largely on track. In fact, our opinion holds that legislative change before the 2020 elections is highly unlikely. The Federal Reserve will likely continue its move from accommodation to tightening as the economy continues to do well. Next year will (most likely) feature slightly higher interest rates and inflation than 2018, but neither should become a significant economic or equity market roadblock over the next 6 to 12 months, but both will add further complications to an already tortuous environment.

The decline in stock prices over the last few months confirms a risk-off phase. However, the enormity of this phase seems less severe than corrections in 2015 through 2017. For now, the volatility index (VIX) remains slightly elevated; forecasting periods of selling in stocks and other risk assets. Using technical analysis (charting) we believe equity markets are oversold and a rebound is reasonable, thought not a foregone conclusion.

Investing has always been a strategy that performs best over the long haul. Throughout investing history, equity markets have faced many challenges and today, markets must deal with a number of ongoing headwinds. Trade wars and top the list followed by many geopolitical issues, but it doesn't have to be a foreign issue to ignite volatility of a major correction. Our politicians have been known to make plenty of mistakes, allowing the pendulum to swing well past the intended point.

Having said all that, we continue to maintain a positive outlook and remain invested with a pro-growth stance. This means we tend to overweight stocks relative to bonds as long as fundamentals for equities remain relatively good. Our optimism will increase as global growth picks up and trade tensions are mollified.

Best Regards,
Phillip L. Clark, RFC
President & CEO