Bell Bank
Wealth Management

EQUITY & FIXED INCOME OUTLOOK OCTOBER 2018

Federal Reserve Monetary Policy

As expected, the Federal funds rate rose 25 basis points, from 2 to 2.25 percent, at the Federal Reserve's last meeting. The next prospective rate increase is projected to be in December, when the market anticipates another 25 basis-point increase.

Inflation

The most recent year-over-year inflation rate of 2.7 percent is a touch lower than we projected in September, which seems to reinforce our theory that inflation won't continue to rise in a meaningful way.

Economic Activity

Continued strength in the U.S. economy is driving increased expectations for favorable employment numbers this month. New jobs are projected to reach as high as 400,000, based on the record-high number announced earlier by the Institute for Supply Management. These numbers have the market wondering if wage growth will continue. That would bring a growing number of people back into the labor force, pushing the unemployment rate even lower and ultimately adding to the economy's strength.

Expectations for the recent burst of economic strength are based on surveys and forecasts collected in advance of the actual data being announced. The real proof will be in the "hard data," or actual results, which need to support the conclusion of the survey data collected in advance. It should come as no surprise that hard data carries much more weight than survey data.

Economic gauges like consumer confidence, investor confidence, gross domestic product, employment and leading economic indicators are all in positions of strength. There is an old adage that suggests caution if everyone agrees on a topic.

Fixed Income

If the flat yield curve suggested concerns about the prospect of economic slowing, the market changed its mind. The yield on the 10-year U.S. Treasury bond is near 3.2 percent – the highest level since 2011. There is talk that longer-term yields could increase even more, because foreign buyers of U.S. Treasury securities are being priced out of the market due to rising costs to hedge currency risk.

Spread is the additional yield that investors receive over comparable U.S. Treasury bond rates for owning corporate, mortgage, asset-backed and other types of bonds. These continue to shrink and offer less protection to investors.

Stock Market

The stock market has been resilient as it touches new highs, but the rising interest rate environment will ultimately result in higher borrowing costs for corporations that have taken on elevated levels of debt. Higher interest costs will make their way onto income statements and eventually result in some sort of earnings pressure. The market is still sorting out whether this additional interest cost can be offset with rising revenue and profit margins.

Third-quarter corporate earnings announcements will begin shortly. Some leading companies have already indicated they may not be able to reach profit levels forecast by analysts.

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Tenure: 9/92

Years of Investment Experience: 33 years

Education: Greg holds a bachelor's degree in business from the University of North Dakota and is a CFA charter holder.