Bell Bank
Wealth Management

EQUITY & FIXED INCOME OUTLOOK APRIL 2017

Federal Reserve Monetary Policy

The activity surrounding the Federal Reserve's March 15 decision changed very quickly after we prepared our March 1 outlook, when the likelihood of a rate increase moved from a 50/50 probability to near certainty in about seven days. Currently, the Fed Fund rate is 1 percent, with the Fed's next meetings set for May 3 and June 14. We anticipate June 14 as the next date for a possible Fed Fund rate increase.

Inflation

Year-over-year inflation was 2.7 percent in March. The core inflation rate, excluding food and energy, was up 2.2 percent over the last 12 months, and down from 2.3 percent in February. We expect new inflation numbers to remain stable at around these levels when they are announced in April.

Economic Activity

The economic growth rate for the fourth quarter of 2016, originally reported as 1.9 percent, was updated to reflect a 2.1 percent annualized rate. We still think the foundation is in place to support full-year economic growth around 2.25 percent. The labor market should support a low unemployment rate of around 5 percent, while wages are increasing at a slightly faster rate than inflation. Consumer debt, demographics and the prospect of inflation eating into wages could keep growth from reaching the 3 percent rate markets are expecting.

Consumer confidence has reached a 17-year high. It moved from 109.4 on November 30, 2016, to 125.6 at the end of March 2017. Conversely, news media are reporting that President Trump's approval rating has dropped below 35 percent, the lowest level since he took office.

The Leading Economic Indicators Index (LEI) is also up. In the 12-month period ending in November 2016 (to coincide with the presidential election), the annual increase in the LEI was 0.73 percent. From November 2016 through February 2017, the annualized increase in the LEI was 7.09 percent. Part of our economic analysis includes reviewing data consistency. There appears to be a noticeable gap between the media's survey results and economic survey results.

Home sales and prices continue to move higher. Home sales are running close to the long-term average at 5.5 million units per year. The average home price is now above the peak reached during the most recent real estate buying frenzy. The average home price reached $184,600 in August, 2006, but declined to $134,100 by February 2012. Today, the average home price is $185,510.

Fixed Income

Fixed income investors continue to be on the edge of their seats in fear of rising interest rates. Each time longer-term rates look like they are set to rise, they end up coming back down. The 10-year U.S. Treasury bond has risen above 2.5 percent three times in 2017, only to come right back down each time. It currently stands at 2.4 percent.

Many economic forecasters are predicting the 10-year U.S. Treasury bond yield will rise above 3 percent by the end of the year. It may get there if inflation continues to rise, but we predict that the actual yield will be a bit below that forecast.

Stock Market

Several economic indicators suggest everything is fine with the economy. For that reason, the stock market appears to be fully priced – perhaps even a bit disconnected from reality. While the markets and the economy appear to be in harmony, bumps often occur along the way and leave investors questioning the status quo. We wonder what the next bump might be and where it will leave the markets.

If you are a long-term investor, these bumps don't mean much; you know they will happen over and over again, and you've learned to remain invested in the market. If you are closer to the principal-preservation phase of your investment life cycle, and are holding on to elevated stock positions to receive an extra balance boost going into retirement, perhaps you should revisit your allocation strategy.

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Tenure: 9/92

Years of Investment Experience: 31 years

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