Bell Bank
Wealth Management

EQUITY & FIXED INCOME OUTLOOK FEBRUARY 2019

Federal Reserve Monetary Policy

The next Federal Reserve meeting is scheduled for March 20. We anticipate the Fed shifting to a “wait and see” approach to future Fed Fund rate hikes. This is a noticeable change from the Fed’s telegraphed moves over the last year. Rising inflation has been a concern for the Fed, but has not materialized. In addition, the shape of the yield curve, stock market sensitivity and consumer surveys all suggest a more data-dependent approach to future rate adjustments. The Fed Fund rate currently sits at 2.5 percent.

Inflation

The most recent year-over-year inflation rate was reported at 1.9 percent. The next data release is scheduled for February 13. After reaching a high of 2.9% last July, inflation has drifted downward. We expect the release in February to be consistent with this trend. Look for inflation to be in the range of 1.6 to 1.7 percent for the February report.

Economic Activity

Consumer consumption, government spending, private investment and exports are all components of economic growth. Combined, we expect the economy to grow at a rate near 2.25 percent in 2019. This is a bit lower than market consensus growth expectations.

Look for housing to pick up some strength now that mortgage rates have drifted down over the last couple of months.

Employment conditions remain stable, with unemployment at 3.9 percent. Wages and the labor force participation rate are also moving higher, and consumer credit metrics look good.

Sustained muted oil prices could interrupt the growth theme. A growing economy tends to need more energy to fuel its growth, but low oil prices suggest demand is muted. Low oil prices can be partially, but not entirely, explained by elevated supplies. Consumer confidence remains elevated, but has slipped from near-record highs. We see the same theme in consumer expectation surveys. Leading economic indicators have also slipped below recent highs. None of these factors suggest an immediate problem, but we will continue to watch them.

Fixed Income

Market fears of rising interest rates have moderated noticeably. The 10-year U.S. Treasury bond rate, which stood at 3.25 percent in early November, progressively declined to 2.63 percent at the end of January. Declining interest rates suggest investors are moving toward safer assets. They could also indicate growing interest in U.S. bonds from foreign investors as the dollar has drifted lower against a basket of foreign currencies.

Shorter-term bonds offer a positive real rate of return and principal protection if the market remains suspicious of rising interest rates. Our fixed income models have a good balance between both themes.

Stock Market

The S&P 500 is poised to show its best January performance since 1989. This increase was enough to offset last year’s loss. The 13-month return on the S&P 500 is 3.32 percent, which translates into an annualized return of 3.04 percent. This is a good reminder of how hard it is to use market timing as an investment strategy. Longtime readers know we favor asset allocations that are consistent with each investor’s personal investment profile.

Does this mean the stock market is looking to regain the former glories of annual double-digit gains? We see the performance in January as a smoothing event, recovering some of the more violent downward movement we saw in the final quarter of last year. Our primary thesis – considering corporate earnings growth expectations, stage of the business cycle and consumer surveys – is for equity returns to be in a more normal range of 5 to 10 percent. If January does prove to have been a smoothing event, if greater stability continues, and if the market migrates toward our thesis, then 2019 could see double-digit “compartmentalized” returns. However, we feel the trend is toward more normalized returns.

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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.

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