Bell Bank
Wealth Management

EQUITY & FIXED INCOME OUTLOOK JUNE 2018

Federal Reserve Monetary Policy

The next Federal Reserve meeting is scheduled for June 13. The prospect for another Fed Fund rate increase is high, and we expect the rate to move from its current level of 1.75 percent to 2.0 percent.

Inflation

The most recent year-over-year inflation rate is 2.5 percent. We expect to see it move up to 2.7 percent at the next release date on June 12. We also expect to see rising inflation levels over the next few months. We believe inflation may drift lower, however, in the final quarter of 2018.

Economic Activity

The 3.8 percent unemployment rate has the market spooked about wage inflation and how that may spill over into consumer prices. While we agree there are pockets of labor shortages that will affect prices for consumers, we don't see this as a widespread problem at this point. The current labor force participation rate is 62.8 percent, down from 66 percent prior to the recession. This suggests there is a supply of eligible workers available to re-enter the work force, and that should help keep wage inflation in check.

Investors began the year looking for economic growth to accelerate faster than in the recent past. It appears actual growth is not meeting expectations. Yes, the collective global economy is still growing, but there are early signs of cracks developing. Japan reported first-quarter economic growth down 0.2 percent, in spite of its central bank's generous accommodative monetary policies. The Eurozone's first-quarter economic growth was 0.4 percent, down from 0.7 percent quarterly growth over the previous three quarters. The U.S. posted economic growth of 0.5 percent in the first quarter, on the heels of 0.7 percent or better growth for the prior three quarters. First-quarter economic growth has a tendency to be a little weaker than the other quarters, so we will keep an eye on this data.

Don't sound the alarm yet. Employment is growing, wages are rising, consumption remains stable, inflation remains moderate and wages are rising at a reasonable rate. We see these features remaining in place for the foreseeable future.

Fixed Income

After spending about three weeks near or above 3 percent, the yield on the 10-year U.S. Treasury bond is back down to 2.89 percent. Uncertainty tends to encourage investors to buy U.S. Treasury bonds, and concerns about Italy were the latest news driving the rate back below 3 percent.

Recent strength in employment may encourage the Federal Reserve to implement a total of four rate increases this year. As short-term interest rates rise on the heels of Federal Reserve action, long-term interest rate increases have been lagging. It is hard to pinpoint the exact reason for the flattening yield curve except to say there must be enough demand for longer-term bonds to make the current 10-year interest rate attractive to investors. We tend to see the two- to seven-year area of the yield curve providing the best value.

Stock Market

It's all FAANG so far this year. These stocks – the five most popular and best-performing tech stocks – make up 1.2 percent of the names in the S&P 500. Their capitalization weighting accounts for 12.27 percent of the index, and their return is a whopping 124 percent of the index year-to-date (this means the other 499 stocks diluted the return of these six stocks). It's hard to believe a limited subset of a broader index carries this much influence.

	Name	% Weighting in S&P 500	YTD Return	Contribution to S&P 500
	S&P 500 (SPY)		1.93%	
F	Facebook (FB)	1.93%	8.68%	0.17%
A	Apple (AAPL)	4.09%	11.30%	0.46%
A	Amazon (AMZN)	2.81%	39.35%	1.11%
N	Netflix (NFLX)	0.66%	83.16%	0.55%
G	Alphabet (GOOG)	1.40%	3.69%	0.05%
	Alphabet (GOOGL)	1.38%	4.68%	0.06%
		12.27%		2.40%
	FAANG % of S&P 500 return YTD			124.38%
Data for calc taken from Bloomberg as of mkt close 5/31/2018				

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Tenure: 9/92
Years of Investment Experience: 32 years
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