Economic Outlook

Fourth Quarter 2019

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Our Outlook for 2020: No Boom, No Bust, No Bear

By: James R. Solloway, CFA, Chief Market Strategist and Senior Portfolio Manager

SEI recently released its fourth-quarter Economic Outlook. A summary of the conclusions is provided below:

- We believe that the U.S. and global economies will likely continue to expand in 2020, although at a slower pace. This should support further gains in stocks and other higher-risk assets. The combined effects of positive economic growth and positive equity markets should keep inflation at bay. We believe that a tame inflation environment will encourage central banks to continue to err on the side of easy monetary policy. We also think that quantitative easing should keep fixed-income yields steady, despite government deficit-spending accelerating. Overall, this scenario should be a boon for risk assets.
- At the close of 2019, we saw an increasing number of signals that the U.S. economy is converging with the rest of the world. Economic and earnings growth in the U.S. contracted during the year. Therefore, we expect international markets to outperform U.S. equities in the New Year due to the disparity in stock-market valuations.
- We forecast that China's economy should stabilize and improve in the near-term. The trade-war truce with the U.S. along with a steady progression of fiscal and monetary stimulus over the past two years should be supportive in 2020. Early signs of improvement can already be seen. Our wish for the New Year: *No presidential tweets about tariffs.*
- We believe that the U.S. dollar should move lower after a period of buoyancy. The Federal Reserve's (Fed) pivot toward an aggressive approach to supporting the overnight lending market has the potential to significantly increase the global supply of dollars. Since the greenback appears overvalued on a fundamental basis, we believe that a U.S. currency depreciation is a high-conviction call. This would be a tailwind for non-U.S. economies and financial markets.
- Going into the New Year, we are hoping for less Brexit uncertainty and a trade deal between the U.K. and European Union. We expect rational minds to prevail, but a no-deal Brexit remains a residual risk. As the year-end 2020 transition deadline approaches, U.K. and European markets could experience renewed volatility if the negotiations appear to be foundering on irreconcilable differences. In the near-term, equity investors may still react positively as signs of improved global economic growth accumulate.
- Presidential politics have the potential to roil U.S. equity markets. There is little clarity at the moment regarding which Democratic nominee will face President Donald Trump. We believe that the picture should get clearer in March.
- The impact of Fed policy is a potential wildcard in 2020. While we do not see it as a likely outcome, the Fed's dovish stance at a time of full employment could cause a "melt-up" in stock prices. The Fed's mid-cycle pivot in the mid-1980s contributed to the stock market bubble that burst in 1987. The mid-1990s pivot eventually spawned the tech bubble and bust of 1998-1999. Even at low interest rates, we would consider a forward earnings multiple on the S&P 500 Index of more than 20 times as a danger sign. Another stellar year for U.S. equities in 2020 would be a source of concern rather than celebration.
- Overall, we believe the Fed has adopted an asymmetric monetary policy that is skewed toward easing. If the economy exhibits unexpected weakness, or inflation posts surprisingly low readings, the central bank will probably cut the federal funds rate one or more times in the year ahead

A full-length paper is available if you wish to learn more about these timely topics.

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Definitions

Earnings multiple: Earnings multiple is equal to the stock price divided by earnings per share. It is expressed in years. For example, an earnings multiple of 10 means that it would take 10 years of earnings to equal the stock price.

Forward-earnings-multiple: The forward earnings multiple is an estimated number used in an effort to calculate a company's estimated future earnings.

S&P 500 Index: The S&P 500 Index is an unmanaged, market-weighted index that consists of 500 of the largest publicly-traded U.S. companies and is considered representative of the broad U.S. stock market.

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