State of the Economy March 2017

The beat keeps rolling on as the market continues to climb to all-time highs through the first few months of 2017. The consistent ascent to new records didn't happen overnight as price increases occurred gradually. The stock market has resiliently withstood the constant barrage of headline news coming from Washington. Also, consumer sentiment rose to decade-long highs. Clearly, many investors anticipate that President Trump's promises on cutting taxes while boosting infrastructure spending will stimulate growth in the economy.

The positive vibes investors are feeling are not solely dependent on President Trump's proposals. Last week, the employment report showed the economy added 235,000 jobs in February exceeding analyst expectations. Meanwhile, the unemployment rate decreased to a healthy 4.7%. Additionally, the earnings reports for various corporations reflected an increase in profits. The reported earnings for the 4th quarter of 2016 greatly outperformed analyst projections.

The Federal Reserve added to the headlines last week by raising interest rates a quarter percentage point. Federal Reserve Chairman Janet Yellen stated that the economy is doing well. She takes confidence in the robustness of the economy and its ability to withstand shocks to growth. Yellen also pointed out that overall inflation is moving closer to her 2% target after undershooting this target for many years. The central bank is striking a more aggressive tone as they plan on raising rates further throughout the year.

Investor confidence surrounding the overall economy continues to carry the U.S. stock market into uncharted territory. The U.S. consumer confidence index climbed to the highest level since 2001. Last week demonstrated how investors and the Federal Reserve are on the same page. After the Fed raised interest rates, stock prices jumped higher. Investors cheered the Fed's decision unlike the prior two rate hikes since the financial crisis. In addition to the gradual climb of stock prices, there has been very little volatility in the market. As of last Friday, the S&P 500 has not dropped more than 1% since the election in November 2016. This is the longest period without a 1% loss since 2006.

With the market running on all cylinders we must not forget the obstacles it faces. First, the economy isn't showing many signs of reversing the long trend of subpar growth. When the Federal Reserve raised rates, they did not point to major increases in productivity. In fact, most data projections show slow growth continuing. These projections seem to attribute much of the rise in stock prices to consumer confidence. Second, the recent slide in oil prices resulting from an increase in stock piles in the U.S. could inhibit rises in market expansion. Lastly, there are many issues overseas still lingering. Greece faces another deadline in July to secure a deal to pay private investors or face a default. The global economy is struggling to stimulate growth and many countries are still offering negative interest rates to their investors. We live in a global economy and it would be very hard for the U.S. economy to grow without meaningful contributions from the rest of the world.

Furthermore, the economic numbers are not entirely adding up. The S&P 500 is currently priced at 22 times its current earnings compared to its historical average of 16. In other words, the U.S. stock market is likely overheated. This could be the calm before the storm. While I do not see a recession coming in the near future, I would not be surprised if the market faces some unexpected swings very soon.

My advice is to continue to stay the course, but be prepared for some turbulence ahead.

Sincerely,

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