Newsletter

State of the Economy December 2016

The surprising election of Donald Trump in November turned the global economy on its head. Since November 8th, the "Trump effect" resulted in gains of over 10% each for the Dow, Nasdaq and S&P 500. As stocks continue to hit record highs, the value of the dollar recently increased to a 14-year high against foreign currencies. Conversely, bond prices were routed as the yield on a 10-year Treasury note climbed to its highest level since September 2014. The drastic swings in the stock and bond markets can be directly tied to investors' optimism towards the President Elect's potential economic policies.

The United States Central Bank added greater enthusiasm to the markets last week after the Federal Reserve Chairman, Janet Yellen, boasted an optimistic tone towards the economy. Consequently, the Federal Reserve raised interest rates by a quarter point for the first time in a year. Yellen pointed out that the labor market is nearing full employment and inflation is moving towards targeted levels. As for future interest rate increases, she suggested the Fed would take a "wait-and-see" approach before deciding how to respond to Mr. Trump's economic agenda. His agenda is anticipated to include increased government spending on infrastructure, tax cuts for corporations and deregulation for banks. While increasing rates a quarter point is a relatively minimal change for our economy, it is a signal to investors that borrowing rates may continue to increase in 2017.

Despite, the positive economic vibes spreading across the US, the rest of world is struggling to keep pace. Earlier this month, the European Central Bank stated it would slow the pace of its asset-purchasing program. Investors were quite surprised by this decision. Slowing the policy of economic stimulus is to occur despite sluggish growth and mounting political uncertainty across the 19-nation eurozone. As the European Central Bank wrestles with their monetary policy, global financial markets are trying to grapple with the surging value of the dollar. The currencies in Japan, India, Turkey, and Brazil are currently tumbling. Also, in China, there are fears that a rising dollar will slow trading of the yuan. In general, if the value of a country's currency decreases, capital will typically flow out of the country resulting in a weakened economy.

As the market continues to hit all-time highs, I believe it is important to stay cautiously optimistic about the market going forward. First, it is necessary to be cognizant of why the market is surging since Trump was elected. The financial and industrial sectors are the primary drivers of higher stock prices because Trump proposes deregulation for banks while rebuilding infrastructure. Considering that the Dow Jones comprises of only 30 stocks and is a price-weighted index, the financial and industrial stocks help explain why it is outperforming all other major indices. For example, Goldman Sachs has the highest stock price in the Dow Jones. Therefore, a significant increase in its price will have a disproportionately large impact on this index. Goldman's stock price has helped catapult the Dow Jones since November 8th.

In 2017, many investors will be focused solely on the United States. However, I advise my clients to continue to have diversified portfolios. The stock market in the US has already reacted to the potential fiscal changes. Nevertheless, many questions remain outstanding. Will lower taxes on corporations boost hiring and profits? Will deregulation result in increased earnings for banks? Could higher interest rates and a strengthening dollar hold back corporate profits? The impact of these policies remains to be seen but the actual earnings of companies is particularly important. As I mentioned above, Europe and emerging markets are not without problems. However, their more attractive valuations should not be overlooked.

I would like to wish you and your family a happy holiday and a great start to the New Year.

Matthew Bagell, CPA
BJL Wealth Management
301 Lippincott Drive | Suite 400 | Marlton, NJ 08053

Partner
Bridge Wealth Advisors
1120 Route 73 | Suite 305 | Mount Laurel, NJ 08054

Wealth Management Solution

Contact Us: Office 856-355-5905 | Fax 856-810-3995 | www.bjlwealth.com