"Are you optimistic? Perhaps Here is why."

By Tommy Williams, CFP®

• Are you bullish, bearish, or neutral about the U.S. stock market?
• Are U.S. stocks undervalued, overvalued, or fairly valued?
• What is the biggest threat the U.S. stock market faces this year?


Tommy Williams

During the first four months of 2018, U.S. stocks have experienced not one, but two, 10 percent declines. These short-term reversals are known as corrections. They occur relatively often. It helps to wring out investor exuberance and, sometimes, to create buying opportunities as share prices drop.

The two recent corrections appear to have created a fair amount of uncertainty, according to Barron's bi-annual Big Money Poll of professional investors. The ranks of the bullish have diminished, and the bearish remain relatively unchanged, but the number of those who are 'neutral' has grown:

Investment advisors say their clients are also unsure about stock markets. They indicated 60 percent of clients were neutral about stocks, while 23 percent were bullish and 17 percent were bearish. When asked about market valuations, a majority thought U.S. stocks were fairly valued (57 percent) after the corrections. Thirty-five percent believe stocks remain overvalued, and 8 percent believe stocks have become undervalued.

If either 'political/policy missteps' or 'rising interest rates' was your answer to the biggest threat to U.S. stocks, then you're thinking like a professional investor. Their list of worries included:

Of course, a primary political/policy action lately has revolved around trade wars and tariffs with our major trading partners. Brian Wesbury a well-respected Economist with First Trust offers up some excellent thoughts on trade:

When the report on international trade came out earlier this month, protectionists were up in arms. Through February, the US' merchandise (goods only, not services) trade deficit with the rest of the world was the largest for any two-month period on record. "Economic nationalists" from both sides of the political aisle, think this situation is unsustainable.

Meanwhile, some investors ran for the hills when President Trump started announcing tariffs on steel, aluminum, and other goods, thinking this was the reincarnation of the Smoot-Hawley tariffs that were a key ingredient of the Great Depression. We think the hyperventilating on

both sides needs to stop.
Running a trade deficit means the US gets to buy more than it produces. In turn, we have this ability because investors from around the world think the US is a good place to put their savings, leading to a net capital inflow that offsets our trade deficit. Notably, foreign investors are willing to invest here even when the assets they buy generate a low rate of return. As a result, this process can continue indefinitely.

It's important to recognize that free trade enhances our standard of living even if other countries don't practice free trade. Let's say China invents a cure for cancer and America invents a cure for Alzheimer's. If China refuses to give their people access to our cure, are we better off letting our people die of cancer? Of course not!

Imposing or raising tariffs broadly would not help the US economy. Nor would imposing tariffs on specific goods, like steel or aluminum. Giving some industries special favors will only create demand for more special favors from others. It'll grow the swamp, not drain it. All that said, we understand the frustration policy makers have with China, in particular, which has been levering access to its huge market to essentially steal foreign companies' trade secrets and intellectual property. It has a long-term track record of not respecting patents or trademarks.

In theory, letting China into the World Trade Organization was supposed to stop this behavior. But no company wants to bring a WTO case against China when it thinks China would respond by ending its access to their markets and letting in competitors who are more willing to be exploited. In addition – and this is very important – China is unlike any of our other trading partners in that is a potential major military rival in the future. There is a national security case to be made – even if one were to take a libertarian positon on free trade in general – that the US could accept a slightly lower standard of living by limiting trade with China, if the result is a lower standard of living for China as well. Mr. Wesbury's analysis seems to be consistent with the "credible consensus" on trade. Stay tuned, we'll see how it all plays out.

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