Outlook for November 2019

WORLD ECONOMY

United States

- The U.S. economy is slowing, but the current growth rate remains comfortably above any near-term recessionary lines thanks to steady consumer spending and a resilient housing market.
- While capital spending on plant and equipment outlays continues to decline, the news isn't all bleak. Businesses are investing in productivity-enhancing intellectual property, particularly software.

Developed Markets

- Eurozone growth is admittedly anemic but still positive. The economic benefits from structural tax and regulatory reforms implemented by France and Spain are offsetting the weakness in Germany and Italy. Look for Germany to announce an expansionary fiscal policy early next year.
- The ongoing Brexit saga and slower global growth are beginning to chip away at the U.K. economy. Uncertainty around year-end elections may impede this country's growth and could precipitate a mild recession.
- Japan's new value-added tax (effective October 1) caused a surge in consumer spending during the third quarter. This boost in GDP will likely be given back this quarter. Growth is expected to be positive, but below 1.0% in 2020.

Emerging Markets

- The tariff wars are making it more difficult for the Chinese government to manage the economic slowdown. Fiscal and monetary expansion should help prevent any notable decline below 5.0% GDP next year and into 2021.

MONETARY POLICY & CURRENCIES

United States

- The 0.25% (25 basis points) rate cut at the end of October should be the last one for this year, and possibly this economic cycle. Relatively strong GDP growth and the resolution of the inverted yield curve have given the Fed a little more breathing room.
- Lower interest rates and the potential narrowing of the GDP gap between the U.S. and the rest of the developed world could stop the dollar's rise. That said, we don't foresee any dramatic declines in the near future.

Developed Markets

- Debate over the effectiveness of negative yields and the dangers of excessive quantitative easing continues to rage at the European Central Bank, which may make it difficult for Chairman Lagarde to move in an even more dovish direction in 2020.
- Given that the 2.0% inflation target remains far from current levels, the Bank of Japan appears open to possibly reducing already low interest rates and increasing monthly asset purchases.

Emerging Markets

- Emerging market central banks are relying on more traditional rate-cutting tools to support their economies. Rates in these countries are positive, and generally not as close to zero as in the developed economies. Under cover of Fed easing, China, Russia, Brazil, India, and Korea were able to cut their rates while preventing any substantial declines in their respective currencies.

BOND MARKETS

United States

- The U.S. Treasury yield curve, while still flat, is no longer inverted as the Fed's 0.75% (75 basis points) rate cut this year has effectively met market expectations, and the economy hasn't deteriorated to recessionary levels. We expect the curve to steepen from here, with the ten-year approaching, and perhaps slightly exceeding, 2.0% next year.
- Corporate bonds, in general, but particularly below-investment-grade bonds, are becoming expensive. The narrow spread to Treasuries is a strong sign of healthy balance sheets and a reasonably strong economy, but investors seeking extra yield may be pushing high-yield rates too low.
- Exclusive of some state-specific issues, municipal bonds are relatively attractive compared to taxable issues given their underperformance so far in 2019.

Developed Markets

- With central banks potentially reaching both the natural and self-imposed limits of their asset purchase programs, developed market bonds appear vulnerable to price declines. Budding recoveries in some of these economies present further risk for this asset class.

Emerging Markets

- Year to date, emerging market bonds have performed well, with dollar-denominated debt notably outperforming bonds in local currency. We expect that gap to narrow as interest rates fall due to domestic monetary ease, and currencies stabilize and, in some instances, appreciate relative to the U.S. dollar.

Outlook for November 2019

EQUITY MARKETS

United States

- While earnings growth is slowing, it has so far defied concerns of an earnings recession. Positive earnings growth combined with low rates may allow valuation multiples to expand, and this bull market to continue into next year.

Developed Markets

- The valuation gap between European and U.S. equities has started to close due to the reduced risk of a no-deal Brexit and overall better than expected economic and earnings growth. Any fiscal policy initiatives, particularly out of Germany, could produce even more outperformance in this sector.
- The performance of Japanese equities has been inhibited by the safe-haven status of the yen and the global trade wars. Performance for the remainder of the year will depend in part on the continued weakening of the currency and any meaningful trade resolutions.

Emerging Markets

- Emerging markets are historically cheap compared to U.S. equities because they've been affected the most by the tariff wars and slower global growth. As trade disputes appear to settle into a long-term impasse with no further escalation and policy initiatives help revive global growth, this equity class may be well-positioned to outperform developed markets.

ALTERNATIVES & COMMODITIES

Oil

- Concerns about global demand and U.S. shale production have kept an upside cap on oil prices. With American frackers idling some production at current price levels, the floor shouldn't be notably breached. We expect oil prices to hover in the $50-$60 range for the foreseeable future.

Gold

- Gold has benefitted from monetary easing here and around the world. With no tangible inflation threats or additional Fed rate cuts on the horizon, gold prices are likely to decline by year-end.

Industrial Metals

- Any sign of easing trade tensions could boost the industrial metals complex as it would improve the economic outlook for China and other commodity-intensive emerging markets.

Hedge Funds

- Our outlook for this market remains the same as reported in October. After a difficult period characterized by abnormally low market volatility, high intra-asset correlations and historically low interest rates, the return to more normal market conditions has allowed hedge fund managers to demonstrate their value-add in both good and bad markets. Defensive strategies provided beneficial downside protection during the Q4 2018 downturn while directional strategies participated strongly in the Q1 2019 rebound.

Private Equity

- Our outlook for this market remains the same as reported in October. High asset valuations and fierce competition to invest the rising backlog of committed funds awaiting deployment remain a major challenge for the category, particularly in buyouts. These risks can be mitigated by focusing on specialist managers with a demonstrated record of generating outstanding returns in different market cycles while maintaining investment discipline.

Important Information

Benjamin Pace
Chief Investment Officer

Ben Pace is the Chief Investment Officer and a member of the Investment Committee. Prior to joining Cerity Partners, Benjamin Pace was Chief Investment Officer and Head of Global Investment Solutions for Deutsche Bank Private Wealth Management in the U.S. Ben has more than 25 years of experience in investment management. Prior to joining Deutsche Bank in 1994, he managed equity income funds for two investment organizations.