Outlook for December 2019

WORLD ECONOMY

United States

- Disappointing business spending on longer-term capital projects is holding back the U.S. economy from achieving its 2.50% - 3.00% GDP growth potential. The reluctance stems primarily from the uncertainty around the trade wars and their impact on global economic activity.
- While U.S./China trade frictions will be long-lasting, we expect a truce in the coming months, which could allow the strong consumer and burgeoning housing sector to drive 2.00% GDP growth in 2020.

Developed Markets

- The disappointing economy of continental Europe appears to be bottoming just shy of a recession. Any reduction in trade tensions would be beneficial for Germany. The country's consumption spending has remained surprisingly strong throughout its yearlong industrial slump.
- The upcoming U.K. elections should provide some clarity around Brexit. The uncertainty has caused a slowdown in the country's economy.
- While the recent increase in the value-added tax has distorted Japan's economic results, the impact on consumer spending appears to be milder than previous tax hikes.

Emerging Markets

- China's economic growth will likely continue to decline due to longer-term overcapacity and demographic issues. Trade tensions have made it more difficult for the government to manage the magnitude of the downturn. However, recent fiscal and monetary policies should prevent a sharper economic decline and more pronounced capital outflows.

MONETARY POLICY & CURRENCIES

United States

- The Fed is likely at or near the end of its downward "mid-cycle" adjustment but has left room for additional cuts should trade negotiations collapse, or the economy slows to recessionary levels.
- The transition this year from tighter to looser monetary policy should stop the two-year advance of the dollar. Stronger economic growth and the higher absolute level of U.S. rates relative to most developed markets should prevent any sharp decline.

Developed Markets

- The European Central Bank continues to be accommodative but may soon pressure governments to implement fiscal policies that would help pull the region out of its economic doldrums.
- With fiscal policy becoming tighter, the Bank of Japan may implement additional rate cuts and longer duration asset purchases to stoke economic growth.

Emerging Markets

- The Peoples Bank of China will likely make more rate cuts to help the government better manage the economic slowdown. However, it needs to be careful not to depreciate the renminbi and provoke unwanted capital outflows.

BOND MARKETS

United States

- Intermediate and longer-term U.S. rates may decline slightly over the coming months as economic indicators provide inconsistent fourth-quarter results. Reasonably strong economic growth next year should put upward pressure on rates, with the 10-year Treasury approaching 2.00% during the first quarter.
- Trouble in the energy sector has caused the spreads in the high-yield bond space to widen. Other economic sectors have relatively strong balance sheets and better revenue and earnings growth prospects, which should prevent any dramatic price declines.
- Municipal bonds are attractive at current levels given their year-to-date underperformance against taxable bonds, our forecast for slightly higher rates, and the favorable supply/demand dynamics.

Developed Markets

- Negative yields to maturity across the duration spectrum make it difficult to maintain or establish positions in international bonds of developed markets.

Emerging Markets

- Despite the central banks cutting rates, local-currency emerging market debt has a significantly more attractive yield premium compared to dollar-based debt at this time.

Outlook for December 2019

EQUITY MARKETS

United States
- The prospect of continued economic growth should fuel valuation multiple expansion in the U.S. equity markets. Low interest rates for cash and core fixed income securities make these investments poor alternatives to dividend-paying equities.

Developed Markets
- The apparent bottoming of European economic growth may help pull equity markets out of their earnings recession. Positive earnings growth in 2020 could help close the large valuation gap with U.S. equities.
- A weakening yen is removing a significant headwind to Japanese exports and the more cyclical sectors of the Japanese stock market. Easing trade tensions may further help the country's cyclical and industrial sectors. A resilient Japanese consumer could boost stock prices in the discretionary and staples sectors across market capitalizations.

Emerging Markets
- The emerging markets space is historically cheap compared to the U.S. This discount is well deserved given trade tensions and slower earnings growth (or earnings declines) in many countries. This asset class needs a truce in the trade war and a pickup in the cyclical sectors of the economy to end its decade-long underperformance.

COMMODITIES

Oil
- The ongoing debate around U.S. shale production and the surprising discipline of OPEC+Russia in maintaining their production cuts may exert upward pressure on oil prices. Should this occur, U.S. production would likely increase quickly enough to help prevent any spike in energy prices.

Gold
- The end of the Fed's mid-cycle tightening program should signal the end of gold's strong performance this year. The lack of inflationary pressure is the ultimate headwind for any further price appreciation.

Industrial Metals
- Industrial metals prices are bidding higher in anticipation of a de-escalating trade war. This uptick is another sign the global economy is not currently at risk of recession.

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.

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