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As Good As It Gets?

We are currently in the second longest bull market in U.S. history. Equity valuations are at high levels, bond spreads are tight, and some feel the markets are priced to perfection. Investors have been grappling with how to interpret positive news coming from labor markets, economic surveys and equity markets for some time. The upbeat economic indicators reflect many positives. Yet enough uncertainty persists for us to pause and ask, is good news truly good news or is it actually bad news? Can markets and economies continue to grow, or is this as good as it gets?

For the balance of 2018, we feel the following will be on the minds of investors:

- **The Global Economy Continues to Grow.** We expect global growth to continue slowly expanding, as underlying data looks healthy, but not robust. The recent tax cuts appear to be benefitting both consumers and corporations, and corporate earnings are poised to grow at a decent clip throughout the rest of the year.

- **Equity Market Volatility Returns to Historic Norms.** After over a year of abnormally low volatility, market activity appears to be rising back to normal levels. This should be expected as the Fed normalizes its balance sheet and becomes less accommodative. With company earnings rising and prices remaining relatively flat, valuations such as P/E ratios have fallen from 15-year highs earlier in the year.

- **Bond Yields are on the Rise.** Outside of some recent spikes over tariffs concerns, bond prices are generally falling, causing yields to rise. With equity volatility returning to normal, the important role bonds play in reducing portfolio volatility has never been more evident.

- **Risks Shifting.** Geopolitical concerns about North Korea have moderated. On the other hand, risks around a trade war are increasing as populism grows around the globe.

After many years of speculation over the timing of bond yields rising, it finally appears to be happening. Bond yields are rising as the Fed normalizes rates. It is a sign of confidence in the economy, as the Fed now feels the economy is on solid enough footing to be able to do this and not rattle markets. Perhaps the tax cuts helped by adding stimulus to the economy, which is nearing a 10-year bull market run. Corporate earnings are on the rise and the labor markets are at their strongest levels in many years. The fear now is whether this is as good as it gets. Is it all downhill from here? While a future recession is inevitable, we do not believe it will happen this year. There are risks to our outlook, but the fundamentals appear strong.

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