ECONOMY

Interest rate cuts headed for landing

THINK STRATEGICALLY:

The Irish Prayer

Fed May Consider Interest-Rate Cuts; Globe's Central Banks Easing Monetary Policy; Economy May be Overheating

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Federal Reserve, trade wars, Iran, the Irish Prayer

With so much bad news in the world and so much happening in Puerto Rico, I found this traditional Irish prayer that goes something like this: "May God give you…. For every storm, a rainbow; For every tear, a smile; For every care, a promise, and a blessing in each trial; For every problem life sends, a faithful friend to share; For every sigh, a sweet song and an answer for each prayer.

Moving on to the markets, it is noted that most U.S. stocks ended the week in positive territory for the third-consecutive week as both the Dow Jones Industrial Average and S&P 500 closed at new highs. The culprit was not the Irish Prayer, but the main driver for this recent rally was the June 19 Federal Reserve Bank meeting that provided some signals that the Fed may be considering cutting interest rates, thus reversing its previous "patient" position, which would have kept interest rates in a holding pattern for some time. As the Federal Reserve acted, other Central Banks around the world were also shifting their monetary policy toward easing. As we have noted in the past, our recent cycle of economic growth is amid its 10th year, and while some expect the period to end, others are hoping this latest round of monetary policy keeps going.

We have seen the labor market slowing, consumer confidence reduced, inflation softening, wage growth slowing and the impact the U.S.-China trade war has had on the U.S economy is now in the billions—all factors that may have an impact on the continuation of the economic expansion.

Moreover, another dynamic that has entered the market is the recent missile attack on an unmanned U.S. drone, which has both the U.S. and Iran on high alert as both countries have been foes for a long time and further action for Iran may lead the U.S. to war.

Week in markets: Federal Reserve fuels recent market rally

As experienced during other economic expansion cycles, once the labor market softens and inflation rears its ugly head, the final chapter of any period can be pointed to. Once there is increased inflation, this indicates the economy may be overheating. With little inflation, it may signal that both products and services suggest the economy may be slowing. The Federal Reserve Bank had indicated that a 2 percent inflation rate is conducive to healthy economic growth consistent with a robust economy. However, in recent reports, the Fed may reduce its inflation forecast to 1.5 percent. This change in stance and focus has fueled the current market rally.

The Dow Jones Industrial Average closed the week at 26.719.13, for a gain of 629.22, or up 6.49 percent; the S&P 500 closed at 2,950.46, for a gain of 63.48, or up 2.20 percent, The Nasdaq closed at 8,031.71, for an increase of 235.05, or 3.01 percent. Meanwhile, the U.S. Treasury's 10-year note was impacted heavily, reaching 2.00 percent and closed at 2.06 percent.

What does it mean to investors?

Investors with exposure to both bonds and stocks should consider the following:

—Remain invested in stocks and perform periodic portfolio reviews to achieve long-term goals.

—Review bond maturities to include bonds with short-term maturities and protect the portfolio from rising volatility. The Fed: The economy is healthy, but its growth pace is slower.

—Economic growth was a solid 3.1 percent. However, there are signs of weakness as consumer spending, jobs growth and wage gains have all slowed.

—Investors should consider increasing diversification through stocks with attractive valuations that will benefit from lower interest rates.

—Be vigilant for market downturns because they provide substantial investment opportunities, and invest in stocks at attractive prices.

—The forecast calls for international equity returns that are much higher than those in the U.S.

All data reviewed points toward the end of this economic expansion cycle; prepare your portfolios for this change in sequence. Finally, the Federal Reserve Bank also noted that even though the economy may be growing, the uncertainty following the trade tensions has had an impact on global growth because trade impacts more than 60 percent of the world's gross domestic product (GDP).

The key words are "diversify, stay invested and stick to your long-term goals."

Market Close Comparison	6/21/2019	6/14/2019	Change	YTD
Dow Jones Industrial Average	26,719.13	25,089.61	6.49%	7.46%
Standard & Poor's 500	2,950.46	2,886.98	2.20%	15.13%
Nasdaq	8,031.71	7,796.66	3.01%	16.96%
U.S. Treasury 10-Year Note	2.06%	2.08%	-0.96%	-0.060%

Final Word: End of easy Warren Buffet metric calls for market crash

Without any reservation, Warren Buffett and Berkshire Hathaway are probably the best-value investing gurus in the market. Buffett has often used what is referred to as the Buffett Indicator. The Buffett Indicator is a metric used to measure the overall health and valuation of U.S. stocks and, as with all things, Buffett is simply a calculation of the total market capitalization of all U.S. public stocks by the most recent GDP. As a matter of historical reference, the Buffett Indicator surpassed 145 percent just before the dot.com bubble burst and reached 110 percent the week before the financial crisis. One must not confuse the Buffett Indicator as a signal that stocks are cheap, and may get even less expensive, just as happened during the financial crisis or dot.com burst. Currently, the Buffet Indicator is at 136 percent, which indicates levels are higher than the dot.com burst and just below the financial crisis.

However, before jumping to any conclusion, we must consider what has changed. For one, the Tax Reform of 2017 has provided companies a lower tax rate, which translates into increased valuations. What the Buffett Indicator is signaling is that the U.S. stocks are mostly expensive, and to that point, Berkshire has not made any significant acquisitions lately.

In summary, be mindful of the Buffett Indicator because it tells us that most stocks have not been as high, or near their high, as right now. So, indeed, a correction may be approaching.

The Irish Prayer

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