PeoplesBank Wealth Management
Economic & Investment Strategy Outlook
April 3, 2018

Economic Outlook

When I was 17 years old, my Dad took my sister and me to Cedar Point amusement park in Ohio. It is known as the "Roller Coaster Capital of the World". Earlier that year, the Millennium Force roller coaster had opened. At the time, it was both the world's tallest (310 feet) and fastest (93 mph) roller coaster. It is pictured at right. I love riding roller coasters even though I am slightly scared of heights, and the ride didn't disappoint. At the top of the lift hill, you can see quite far over Lake Erie (which I saw through my fingers), and the first drop is incredibly fast and steep. The coaster has the world's 6th longest track, so it is also a satisfyingly long ride. The US stock market has recently become a roller coaster, with more large up and down days than the market has had dating back to 2009. With a volatile stock market still in correction mode as the background, this month the Investment Strategy Committee debated whether our cautiously optimistic outlook is still appropriate.

Despite the continuing stock market correction, we see few signs of a recession on the horizon. Economic data this quarter is coming in slightly weaker than data from the fourth quarter of last year, suggesting that economic growth has slowed over the past few months. Interestingly though, this has been the pattern for the past several years, where economic growth in the first quarter of the year is the slowest quarter of growth for that year. In examining data that is more forward-looking in nature, such as the jobs market, the structure of interest rates, and the bond market, none of our main recession indicators are flashing a warning sign. This says to us that it is still appropriate to be cautiously optimistic.

One stumbling block to the stock market rallying instead of bouncing around seems to be the escalating talk of trade tariffs between the US and China. Since early March, news headlines have been dominated by both sharp rhetoric between each country's leaders and small but escalating tariffs. There is no doubt that if the US and China find themselves in a trade war, i.e. large reciprocal tariffs, this would be a bad situation for global trade and the global economy as a whole. Looking at the details of what has been currently been announced so far though leads us to view the situation with cautious optimism. First, the size of the tariffs as currently announced are simply not that large. Second and most important is that there is a possibility that the tariffs will never actually be enacted. The Chinese government did not specify when its tariffs would be imposed. Under the US plan, companies have until May 22nd to object to the proposed tariffs, and then the government has 180 days after that date to decide whether or not to implement the plan. Therefore, there is time for negotiations, and we will continue to monitor the situation closely.

The outlook for corporate earnings is another reason for cautious optimism. According to MSCI, analysts expect 2018 corporate earnings in the US to grow just under 20% year-over-year. Looking outside the US, earnings are expected to grow 8% in Europe and 14% in emerging markets. There is no doubt that with investor expectations so high there is the possibility that earnings will disappoint. On a positive note though, analysts have been revising their estimates higher as we near first quarter reporting season, which is opposite from the historical pattern where overly optimistic analysts revise down their estimates closer to reporting season.

Overall, the Investment Strategy Committee believes it is appropriate for our broad views to remain cautiously optimistic. We will continue to evaluate these views and we will change them as the weight of the evidence suggests we should.

Investment Strategy

The US stock market has been in correction mode since early February. As stated in last month's Outlook, the typical price pattern of a correction is an initial low, then a rally (or several) which stops before the initial high, a retest (or several) of the initial low and then a rally which carries the market to a new high. The chart at right shows the price pattern of the S&P 500 at the time of this writing. The index is following the general pattern described previously as it is currently retesting its early February low. We obviously have no idea where exactly the market will head from here, but history suggests the correction should last a while longer. We have had four 10% corrections during this current expansion. Between the initial high and the point at which the market exceeded that high, the corrections have lasted 125 days, 144 days, 97 days and 417 days for an average of just under 200 days. As of the time of this writing, it has only been 66 days since the January 26th high.

Given that we do not see a recession on the horizon and that we expect corporate earnings growth to remain strong over the next year, we continue to recommend that client portfolios remain overweight equities. We also continue to favor broad emerging markets where we find the favorable combination of relatively strong economic growth, accelerating corporate earnings growth, and lower valuations than in developed markets.

Looking at the bond side of portfolios, our expectation remains that longer-term interest rates are more likely to rise than fall over the next several months. Therefore, we favor areas of the bond market that help us to both decrease the interest rate sensitivity and increase the yield of bond portfolios. These areas include preferred stocks and short-term high yield bonds.

We made no changes to our asset allocation recommendations this month. Please see our overall asset allocation recommendations on the next page.

Michael Haun, CFA, CFP ®
Vice President, Investment Strategist

PeoplesBank Wealth Management
Relative Asset Class Recommendations

As of 4/3/18

	Unattractive	Slightly Unattractive	Neutral	Slightly Attractive	Attractive
Stocks				X	
US Large Cap			X		
US Mid/Small Cap		X			
International Developed			X		
Emerging Markets					X
Energy Infrastructure MLPs					X
Bonds		X			
US Investment Grade				X	
Inflation Protected Securities (TIPS)		X			
High-Yield			X		
International Bonds	X				
Municipal Bonds				X	
Preferred Stocks					X
Real Assets					
Real Estate		X			

As of 4/3/18. Recommendations subject to change at any time without notice.

Investment Process

PeoplesBank Wealth Management's asset allocation process develops both long-term (strategic) and shorter-term (tactical) recommendations. The strategic recommendations are based upon how the Investment Strategy Committee believes investment portfolios should be positioned in a generally neutral market environment over the next five to seven years. The tactical recommendations are meant to highlight opportunities over the next one to two years where the Committee sees either increased opportunity or risk.

The Wealth Management Investment Strategy Committee (ISC) is responsible for establishing and updating both the strategic (long-term) and tactical (short-term) asset allocation for Wealth Management's investment management and trust relationships. The committee is comprised of the senior members of Wealth Management and is chaired by Michael Haun, our Investment Strategist. The committee is also responsible for monitoring and updating strategies, managers, and funds within client portfolios. The ISC meets on a monthly basis.

If you have any questions or would like to discuss PeoplesBank Wealth Management's outlook further, please call Michael Haun at 717.747.2419 or email him at mhaun@peoplesbanknet.com.