Reilly Financial Advisors

THE ECONOMIC MONTH IN REVIEW AND OUTLOOK – APRIL

US Markets and Economy:

The US bull market in stocks continued right through to the end of April. Both the S+P 500 blue-chip index and the NASDAQ Index reached all-time highs at the end of the month, fully erasing the losses of late 2018. The Dow Jones Average, weighed down by weakness in a few of its 30 blue chips (mainly Walgreens/Boots and Boeing) nonetheless edged close to its all-time high by the end of the month. For the year so far, the S+P 500 has gained around 17%, which is a good showing for any *full* year in a bull market!

What has provided the rocket fuel to keep a 10-year-old bull market roaring ahead? It can't really be current corporate earnings, since the first quarter of 2019 was a poor one compared to previous quarters and may show no growth over one year ago. But Wall Street is projecting a sharp pickup by the fourth quarter of the year to near 10% growth. That should provide a firm underpinning for the market. At the same time, stock traders are still celebrating the Fed's decision to be "patient," that is, to leave short-term rates steady for the rest of the year, and perhaps even through 2020. With the key Fed Funds rate still historically low at 2¼ - 2 ½%, and long-term rates like the US 10-year Treasury yield still low at around 2.5%, monetary policy is accommodative, which is a plus for stocks. If we factor out inflation, both of these "nominal" rates are at less than 1% in "real" terms. Even more surprising, the 10-year rate was much higher a year ago (falling yields are also good news for bondholders), even though the economy continues to boom ahead.

The latest economic data has shown that the sharp selloff in stocks last year was *not* forecasting an economic recession. (As Paul Samuelson said many years ago, "the stock market has predicted 9 of the last 5 recessions.") The preliminary report on first quarter real GDP growth showed a gain of 3.2%, well above many predictions. While this pace is not forecasted to continue all year, even a slowdown to 2% real growth means that the economic recovery since 2009 will certainly become the longest ever in modern US history. And many American workers are benefitting: employment gains are still strong, with April job growth (reported at the beginning of May) coming in at +263,000, and the unemployment rate sinking to a 50-year low of 3.6%. Wages and benefits are now rising at a bit over 3% per year, which means that in real terms the average worker's compensation is growing faster than inflation.

And yet that inflation rate is staying a tad below 2%, which is the Federal Reserve's Open Market Committee (FOMC) published target rate. While many economists are still debating if this rate of inflation will ever pick up, Wall Street traders are celebrating a strong economy, rising earnings, and low interest rates. The FOMC is unlikely to raise interest rates as long as this "Goldilocks-perfect" combination remains in place. An extra boost for the market was the news that neither Herman Cain nor Stephen Moore would be appointed to the Fed's Board of Governors (BOG). (Members of the BOG vote at all FOMC meetings and can serve 14-year terms.) Given that both men are not of the caliber for those typically on the BOG, the Fed's nonpartisan approach to monetary policy is safe for now. And with the economy growing nicely, unemployment low, and inflation quiescent, why mess with success?

To summarize, the bulls are still running the show, after a brief (but painful) appearance by the bears late last year. Long-term investors are sitting pretty, but keep those seatbelts on!

World Markets and Economy:

European stocks, as measured by the blue-chip Eurostoxx 50 Index, followed the US higher in April. A solid gain for the month still left the index below last year's highs, and well below the all-time high of 2015. The story is still the same: even with rock-bottom interest rates, the European economy continues to barely limp ahead. While the Brexit mess has been postponed for a short while, the end result, with Britain probably leaving the EU, will be painful for all parties and could temporarily pull down even US stocks. Even the EU economic powerhouse, Germany is now expecting economic growth of only 0.5% for the current year. While the blue-chip DAX rallied nearly 8% for the month, it is still almost 10% below last year's high. French stocks had a more modest rally, but the CAC40 is actually close to its all-time high, even though France's political troubles continue. British stocks had an even weaker rally, as the endgame for Brexit drew nearer, with no clear outcome.

In Asia, Japanese stocks, as measured by the NIKKEI Index, had a good gain for the month of 5%. Yet the NIKKEI Index is still well below its 2018 high, and of course far below its all-time high set in 1989. The economic stagnation, which set in after their property and stock market bubbles collapsed in 1989, has not really relaxed its grip, even with expansionary fiscal and monetary policy. Chinese stocks, as measured by the Shenzen 300 Index, marked time in April. Traders there are waiting for the completion of a trade deal with the US, and the elimination of the costly tariffs which both sides have erected. There will almost certainly be a deal, but the devil will be in the details.

OUTLOOK:

US stocks remain in a bull market. Economic trouble in Europe and Asia could create ripples in the US market, but stocks still provide the best long-term returns, and the US has continued to lead the way upward.