# BULL & BEAR BULLETIN

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## Bull Versus Bear

Volatility made a significant comeback in 2018 with mini 10% corrections in February and April and most recently in November and December. The bear argument for the fourth quarter of 2018 and for 2019 is based on slowing gross domestic product (GDP) growth in the U.S., weak third quarter results by some international countries, higher interest rates in the U.S. and a long and protracted trade "war." Reasonable interpretation of each of these can dismantle the argument for impending hard times.

While it is true that forward looking industrial measures have turned down at different times during 2018 and are a sign of slowing GDP growth, this does not indicate a pending recession for the first half of 2019. The tax cuts that were enacted in December 2017 coupled with the deregulatory environment of the current administration provided stimulative growth in 2017 and 2018, bringing GDP to a 3%+ growth rate. Of course, as we begin to anniversary the regulatory rollbacks and tax cuts, GDP will begin to slow toward a 2%+ rate of growth from 3%+, but this is still growth, not recession, and would be faster growth than the sub-2% growth of the last year of the prior administration, as the tax cuts will continue to have some stimulative effects. Second, negative GDP growth in Germany and Japan during the third quarter of 2018 appears regulatory and/or transitory in nature due to recently enacted and poorly executed regulations in the German auto industry and Japan suffered multiple natural disasters that cut off industrial output. This is hardly a sign that a global slowdown will end American expansion, especially since these are issues that should add to GDP as Germany has added personnel to process auto inspections and the rebuilding effort in Japan should boost output. The third and fourth arguments are higher interest rates in the U.S. and trade "war." Higher rates have cooled the stock market's growth, but much of this is priced into the market as stocks pulled back 10% in November. As for a trade "war", we have agreed with our North America Free Trade Agreement (NAFTA) partners, Canada and Mexico, to a new trade deal known as the United States-Mexico-Canada Agreement (USMCA). Only 12% of the U.S. economy relies on exports compared to 26% in China and 51% in Germany. Trade with Canada and Mexico comprises approximately 4% of U.S. GDP with another 1% coming from China and 1.25% from the European Union Ex-UK. A trade war with China and the European Union would have negative consequences, but limited ones, as the U.S. has firmed up its agreement with its primary export markets, Canada and Mexico.

If GDP in the U.S. slows toward a 2%+ rate, corporate profits should continue to increase with current consensus expectations calling for growth at a high single-digit pace for S&P 500 companies for 2019, with unemployment continuing to decline while wages continue a modest appreciation, all positive contributors for continued economic growth. With the S&P 500 trading below 15 times 2019 earnings, stocks seem attractively priced when compared to the 50-year average forward multiple of 16.5 times. Any indication that the Federal Reserve will hold back on excessive interest rate increases, strong holiday sales or continued strong employment numbers could trigger a rally in stocks.

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