November 2017 — Over the Horizon Market Commentary by David Offer

This time last year it looked like 2017 was going to be a volatile year. Instead, 2017 became the year that experienced the lowest level of investment volatility in living memory!

We entered the year with concerns over the long-term stability of Europe, with fears nationalistic sentiment could result in the break-up of the Euro. It didn't happen. Concerns over the Chinese economy proved misplaced and North Korea still exists! In the US, an unknown President Trump floundered from one scandal and gaffe to the next. This became the new 'business as usual' for the White House. While the subsequent 12 months bought next to no policy achievements for the Trump Administration, this didn't stop the US share market from having a stellar year, rocketing up 35% in the 14 months since the US election.

Overnight, the US Federal Reserve raised interest rates for the third time this year and how did the US share market respond? It went up 81 points to close at 24,585 and set a new record high! Compare that to several years ago when talk of US interest rate rises would create global share market gyrations. Welcome to a good old-fashioned equities Bull Market; where all news is good news. Boohoo Bear Markets, when the same news is viewed negatively.

While US inflation continues to remain under the Fed's 2% target, the Fed's overnight decision to raise rates appears to have been an easy one given the US jobless rate is now at a 17 year low of 4.1%. The US jobless rate is expected to fall even lower in the year ahead against the backdrop of a strong labour market. Notwithstanding low inflation, a strong US economy has the Federal Reserve forecasting another 3 interest rate hikes for next year and a further 2 interest rate hikes in 2019.

Sooner or later, a strong and strengthening US labour market will result in strong wage growth. In turn, stronger than expected inflation will result. A lingering thought is what happens if Trump's planned tax cuts do become law and work as planned; lighting a fire under an already strong US economy? It is possible to have too much of a good thing. The likely result would be additional and unexpected US interest rate rises and these coupled with a strong US Dollar would present a new set of challenges for the US and wider global economy. The second half of 2018 and into 2019 could be when US inflation finally wrong-foots global share markets.

Also lingering is the recollection that tax policy changes do not necessarily remain in favour post their introduction. In June 87 the Keating Government introduced franking credits. At the time, franking credits were perceived to fundamentally change the value of Australian shares with Corporate profits no longer double taxed. 4 months later, after a period of optimism and extreme share market gains, we had the 1987 share market crash. While the 1987 share market crash was brought on by global events, our elevated Australian share market felt the impact of the 1987 crash particularly hard. Will it be the US share market's turn in 2018?

We feel 2018 will be a more 'exciting' year than the one just gone with the current historically low market volatility unsustainable. We are extremely conscious of the evolving investment landscape with the investment decisions we make. However, with 2018 still 17 days away let us not get ahead of ourselves and the interim, may you have a Merry Christmas and Happy New Year.

Please do not hesitate to contact our office if you would like to discuss any aspect of your investment portfolio.

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