ALTMAN INVESTMENT MANAGEMENT

# BRIEF MARKET INSIGHTS

**APRIL, 2018**

## A Note on Global Trade:

In the past couple of weeks, the Trump administration shifted gears by addressing US trade policies - testing the waters in early March announcing tariffs on aluminum and steel, and more recently shifting attention to other industries. The Chinese response was muted initially but followed by a tough reaction to the follow-up rhetoric. Although still early in the negotiations, we don't believe a full-scale trade war will result.

***What we do know*:** Economies around the world continue to experience synchronized growth, as they have since the second half of 2016. However, the recent concerns of an imminent trade war coincident with some weaker global economic indicators has spooked markets by introducing the possibility of a slowdown in the global economy. However, we believe it's far too early to jump to any conclusions since there is no real evidence of a global slowdown in the reported stats we follow.

***Global trade at record levels***. We don't expect the current administration's position to materialize into a trade war. Global trade remains at a record high. We believe that countries have become too interdependent to resort to widespread prohibitive protective barriers. The volume of world exports rose 4.5% y/y to a record high during December 2017. The sum of inflation-adjusted US imports and exports closely tracks the global measure of world exports. It was up 3.0% y/y during January, edging down from December's recent high. The growth rates of both measures have been running around 4.0% since late 2016, a significant improvement from the near-zero growth rates during late 2015 and early 2016.

Given the importance of China in world trade, we also note that the sum of Chinese imports and exports, in nominal terms, rose 19.3% y/y to a record high of 30.0 trillion Yuan during February. Global PMI remains high with the March readings remaining solidly above 50.0. Although the March levels for the US, Eurozone, the UK, and Japan all were down from recent cyclical highs, they were still solid nonetheless and the March PMIs for the major emerging economies (Russia, India, China and Brazil), although more muted, all exceeded 50 as well. In fact, the US is experiencing a trade boom, with both real merchandise exports and imports in record-high territory. Keep in mind that imports continue to exceed exports by over $800 billion and any fears associated with US trade imbalances is overdone.

***Morgan Stanley Capital International's forward revenues continue to move higher*** according to Bloomberg with The Broader Index; the All Country World MSCI also rose to record-high territory this year as industry analysts continue to raise their global revenues estimates for both 2018 and 2019.

***Is President Donald Trump bullish or bearish for the stock market?*** In a little over a year into his first term, he has been both. Since Election Day (November 8, 2016), the S&P 500 rose 34.3% through January 26 of this year. The stock market was discounting a more pro-business White House with fewer regulations on doing business and possibly tax reform. The Tax Cut and Jobs Act (TCJA) was enacted on December 22, 2017, and stock prices proceeded to melt up during January as analysts scrambled to raise their earnings estimates as a result of the cut in the statutory corporate tax rate from 35% to 21%.

The forward P/E's of the S&P 500 soared after Election Day through early 2017, but then eroded as investors lost confidence in the likelihood of tax reform. Their confidence rebounded during the second half of last year and was rewarded with the passage of the TCJA. The melt up during January of this year ended abruptly during February and March, as Trump turned toward his America First protectionist agenda. As of this past Monday, the forward P/E's of the S&P 500 have fully retraced their rise since election day dropping to 15.9. However, the post-TCJA jump in forward earnings remains intact. In our opinion, the P/E correction has been overdone and may be over soon. Meanwhile, the outlook for earnings remains bullish. That's as a result of the TCJA and solid global synchronized growth. The profit picture still looks particularly good and there appears to be little evidence that wage pressure is eating away at corporate profitability.

Market volatility, appears to be entrenched in markets for the time being and does signal some uncertainty associated with the sustainability of the economic expansion. Valuations are certainly more supportive at current levels, as markets have readjusted to the uncertainties of the back half of the business cycle. Globalization has most certainly thrown more noise into the equation, but the current price to earnings ratio of 16 times for the U.S. market on a trailing 12-month basis versus 19.2x just a week ago is well within historic levels.

***We remain constructive on markets coincident with the U.S. economic expansion continuing,*** and we project tax savings on corporate earnings could lead to forecasts for 2018 higher than current consensus (+15% growth over last year). As long-term investors, we believe that in spite of significant volatility and global noise, we are not overly concerned that these are signaling a fundamental shift in capital markets that would change our asset allocation bias.



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