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Eight Investment Trends to Watch in 2016

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2015: The Year that Wasn't

2015 wasn't supposed to turn out the way it did. Following nine years of middling growth, the U.S. economy finally looked ready to shake off its lethargy and deliver some robust and sustainable growth.

Apparently, the American consumer missed that memo and generally stayed home.

What was widely expected to be a break-out year for the U.S. economy instead turned out to be just so-so with economic growth at a tepid 2.00% to 2.50% for the year, due primarily to fits and starts in the consumer and manufacturing sectors. These two key areas just couldn't seem to get their acts together despite holding two strong cards: decent job growth and plummeting energy prices. So, as we look ahead to this year's economic prospects, here are the eight trends I think are worth watching.

1 From a "Low and Slow" Start, the U.S. Economy Will Likely Finish a Little Stronger in 2016

While weakness in global manufacturing may limit the upside, the strength of more domestically focused sectors do appear to limit the downside. That means 2016 could likely start out to be an extension of 2015: uninspiring growth, low inflation and some interest rate tightening on the part of the Federal Reserve before the economy finds its footing and moves up in the second half of the year.

2 Energy may be poised for a turnaround

While not shifting directions quickly, the energy sector finally seems poised to reverse course and start outperforming other sectors in the second half of the year. As the global supply and demand equation for energy starts to balance out, this sector is likely to reward thoughtful investors. Meanwhile, opportunities in the alternative energy space are likely to continue to gain ground in 2016. Solar power and wind power have been catching up with fossil fuels as an emerging presence on the nation's electrical grid.

3 The Return (Finally) of the American Consumer

Expect to see continued improvements in the labor market accompanied by some long delayed increases in wages. If energy prices continue to poke along at depressed levels for the first half of the year, increasingly solvent consumers may very well open up their wallets and starting spending their pent up energy savings. An unemployment rate below the Federal Reserve's 5% target will help earnings pick up in 2016, too. The result: Consumers, who still propel 80% of economic activity, will amp up consumer spending.

4 Look Elsewhere than Bonds for Income

The fact is that bond yields have so little room to fall now that heir return outlook is poor through most of 2016. With rare exceptions, bond returns in 2016 will likely continue to be low even as the Fed begins to raise rates. Fixed income investors won't do any better overseas either due to the fact that many other nations have put in place the kind of Quantitative Easing programs that so dominated U.S. credit markets two years ago. Back in the U.S.; expect to see rates climb by 1.25% to 1.50% by year end which will further undercut any return from fixed income vehicles.

5 Still, the Fed Will Remain Cautious

If the domestic GDP plods along below 3%, don't expect the Fed to raise rates significantly over the course of the year. The reason: U.S. interest rates will likely be kept somewhat in check by global rates set by the overseas Central Banks.

6 The Dollar's Rise Will Likely to Come Back to Earth

The rising dollar, which hampered U.S. exports last year, will likely provide a drag for the first part of 2016 as slowly rising interest rates in the United States and stable to lower rates overseas drive the dollar higher. However, U.S. interest rates may still rise less than most people think. In the current "low and slow" cycle, such expectations may be overblown since Japan and even some countries in Europe seem to be resisting the siren call of Quantitative Easing.

7 We May Have to Start "Whipping Inflation" Again

While core inflation has remained relatively stable because global overcapacity has kept the lid on price increases, that situation may be changing as labor markets tighten. This could become even more significant as baby boomers retire. The elimination of excess capacity through industry consolidation also alters pricing power. For example, the airline industry's consolidation of routes and flights actually led to higher prices last year. Similar consolidations are happening to other industries too.

8 Election year adds wild card to the mix

Of course; one ringer in our economic outlook this year is the influence this year's Presidential election year will have on the markets. According to a Princeton/Bureau of Labor Statistics study, Presidents and the U.S. Economy: An Econometric Exploration1 authored by Alan S. Blinder and Mark W. Watson, over the past seven Democratic and nine Republican terms, market activity during Democratic administrations outperformed in most major growth metrics. A look further back, however, presents a different picture. Research completed by CMC Markets 2 went back to the McKinley administration and discovered that on one measure of growth – stock market performance – the Republican administration of Calvin Coolidge correlated with the biggest stock market advance of all: the Roari

Bottom line:

While in our view, 2016 may not be a banner year, we shouldn't underestimate the impact ofwhat a few positive macro economic tilts can achieve. Overall, there is good news ahead: With barely a sign of recession from here to year end, we may find that 2016 does not have to be an outstanding year for the markets to be a good year for investors.

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If you would like to know more about designing an investment management strategy customized to your needs, contact Mike Albertson at mike@tradewellfinancial.com or call him at 260.490.2084.

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[1] Blinder and Watson
https://www.princeton.edu/~mwatson/papers/Presidents_Blinder_Watson_July2014.pdf

[2] CMCMarkets
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