Outlook as of November 2015

World Economy

- The outlook for global economic growth remains very much a function of how much the improving health of the US consumer can help offset the drop in industrial spending in China.
- While 3Q US GDP growth slowed in a weaker global growth environment, US consumers are finally beginning to spend the "tax cut" provided by lower energy prices. Job and wage growth will provide additional impetus to consumers.
- The Chinese economy is growing slower than the government's officially reported rate. It appears that the burgeoning consumer sector is expanding fast enough to counteract the necessary decline in capital spending in the transition from an investment-driven to consumer-driven economic model.
- A weaker euro and strengthening US economy are allowing exports to the west to compensate for the slowdown in east bound exports within the European Union.
- As China's largest Asian trading partner, Japan is vulnerable to the slowdown in emerging Asia and, most likely already in recession. Further stimulus measures are expected, but there is growing skepticism over their effectiveness longer term.
- Emerging market economies have been overwhelmed by the slowdown in China and its impact on commodity producers. Look for a broader distinction over the coming quarters between commodity producers and commodity consumers.

Monetary Policy & Currencies

- The Federal Reserve continues to prepare markets for the first tightening move in 9 years, but continued low inflation and weakening overseas economies are providing sufficient cover for further delays and an overall gradual approach.
- In addition to extending the Eurozone bond buying program beyond its current September 2016 termination, Chairman Draghi has stressed the availability of additional monetary tools to help achieve the ECB's inflation target.
- The Bank of Japan is hesitant to expand its quantitative easing program. However, further easing appears inevitable given Japan's weak economy and complete lack of wage inflation. There is a possibility the central bank will deem it has done enough and leave further moves in the hands of the fiscal policymakers.
- The Federal Reserve's tightening bias, compared to the overall dovish stance of most global central banks, is a bullish indicator for the dollar against most currencies in the near term.
- With markets calmer following the Q3 volatility, emerging economy central banks should have more flexibility to ease rates to help boost economic growth.

Bond Markets

- After falling sharply in Q3, US Treasury yields have now begun to rise in anticipation of higher rates. We expect Treasury yields to reflect tightening cues emanating from the FOMC ahead of the December meeting.
- Corporate bond spreads have narrowed as overall market volatility has subsided. Outside of the energy and mining sectors, low default rates and stronger economic growth should raise the attractiveness of high yield bonds in a yield-starved market.
- Notwithstanding credit issues in specific cases such as Puerto Rico and Illinois, the municipal bond market has benefited overall from improving credit conditions, making interest rate risk a much bigger concern to investors than credit risk.
- Low absolute yields and unusual volatility around impending central bank policy announcements render developed market bonds a rather poor investment for dollar based investors.
- Emerging market bonds offer attractive current yields. Central bankers in these countries have the flexibility to allow rates across the curve to decline, which could provide additional return upside. Investment in dollar-denominated bonds can help neutralize any currency weakness arising from easing measures.

Equity Markets

- Outside of the energy and mining sectors, US corporate earnings growth has been positive, especially for companies and sectors less exposed to offshore economic and currency weakness. Assuming the Fed maintains a measured approach, continued low rates and positive earnings could lead to some valuation expansion.
- European equities are responding positively to dovish central bank statements and the declining euro and pound. Any additional monetary easing could be a catalyst for prices to rise further through year-end. Currency hedging continues to be advisable.
- Japan has been one of the better performing equity markets in 2015, but investors have priced in expectations of further monetary easing and a lower yen. Failure of the BOJ to deliver could lead to market vulnerability.
- Compared to the developed markets, emerging market equities are notably cheap. However, positive EM earnings growth is less certain, due to weak commodity prices, the slowdown in China and the prospect of higher US interest rates. Since hedging EM currencies is difficult, dollar-based investors should expect weaker relative performance due to currency depreciation, at least through year-end.

Alternatives & Commodities

- Low energy prices have finally slowed supply growth. Prices are expected to remain weak for the foreseeable future, reflecting low global demand, particularly among the emerging economies.
- Any further delays in Fed tightening can give a bid to gold prices, but the bias towards tightening will restrain any meaningful increase in prices despite the dovish leanings of other central banks around the world.
- Industrial metals are trying to find a bottom at current price levels. The oversupply situation is not as pronounced as in energy, but demand is heavily reliant on the slowing emerging market economies. Opportunities here may develop some time in 2016 if global growth picks up.
- Hedge funds fared relatively well in Q3's turbulent markets. Funds positioned for macroeconomic uncertainty and market volatility are attracting interest from investors seeking downside protection and lower correlations to unstable public markets.
- High valuations are making it challenging for private equity firms to buy assets at reasonable prices. We remain focused on disciplined managers, secondary funds, and sectors such as private debt and infrastructure, where valuations are more reasonable.

Important Information

Ben is the firm's Chief Investment Officer and a member of the Investment Committee. He has more than 25 years of experience in investment management. Prior to joining HPM Partners, he was Chief Investment Officer and Head of Global Investment Solutions for Deutsche Bank Private Wealth Management in the U.S.

Ben has been featured in the *Wall Street Journal* and *Reuters*, and is a frequent commentator on Bloomberg TV and radio, Fox TV and CNBC, appearing regularly on network programs such as *Power Lunch, The Closing Bell, Squawk Box, and Worldwide Exchange.*

Benjamin Pace

Benjamin Pace
Chief Investment Officer