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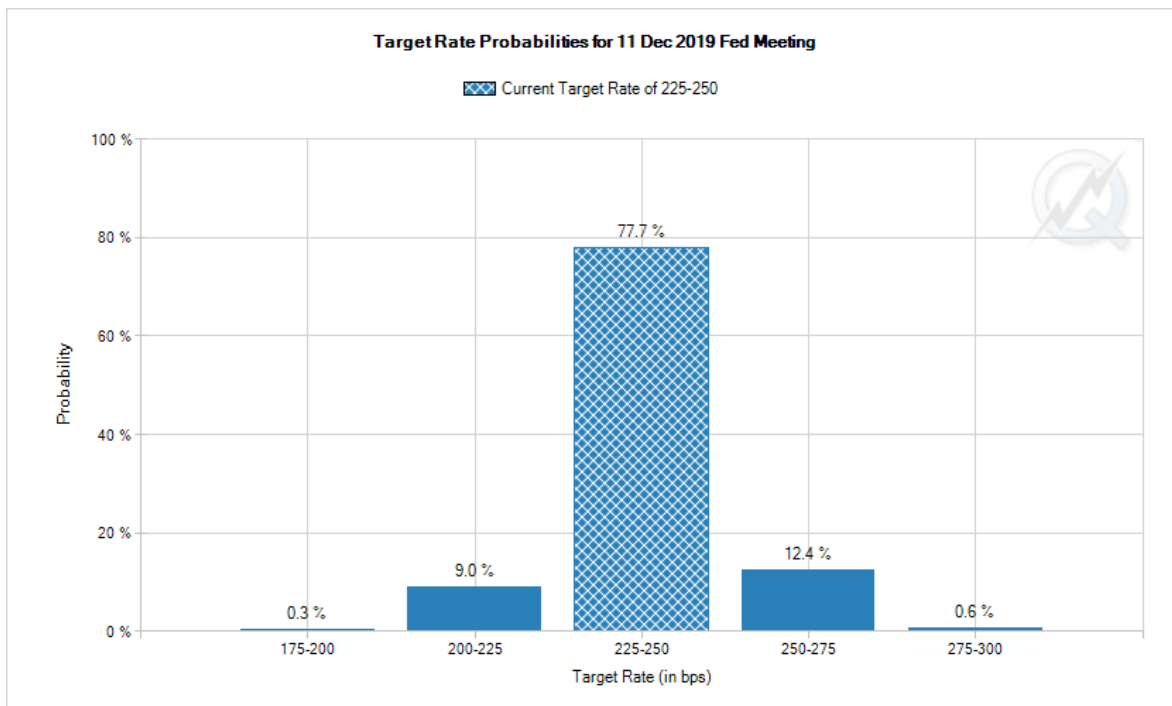
Proactive Investment Management & Financial Planning

Economic Chart of the Week January 2, 2019

By all accounts, the big drop in global stock prices over the last few months reflects investor concern about increased inflation pressure, rising interest rates, and protectionist trade policies. Investors fear those problems will produce slower economic growth and weaker gains in corporate profits. What surprises us is how much those fears seem out of whack with the current trends in the economy. We're especially surprised at how those fears have impacted an important gauge of investor expectations about monetary policy.

Published by the CME derivatives exchange, the "CME FedWatch Tool" shows how likely it is that the Federal Reserve's benchmark "fed funds" interest rate will be at a particular level at some point in the future, based on investors' buying and selling of certain derivative contracts. Just a few months ago, the tool showed investors were expecting the Fed to hike rates several times in 2019, boosting the target range well beyond the current 2.25% to 2.50%. In contrast, the tool is now showing a 77.7% probability that the Fed won't hike rates at all in 2019. Investors now think the fed funds rate will stay at 2.25% to 2.50% through the Fed's final policy meeting of the year. That's a dramatic turnaround, suggesting investors now foresee a 2019 economic slowdown that will be so early and big that the Fed will be too fearful to tighten monetary policy further. The new expectation is quite out of line with what the Fed policymakers themselves project (most of the policymakers expect to hike rates at least twice in 2019). We continue to think such pessimism is excessive. All the same, we need to respect what the market is doing. If we continue to see such extreme pessimism, we would expect continued market volatility and would be more likely to keep cutting our exposure to stocks, as we did in the second half of 2018.

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Chief Investment Officer



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