CORBETT ROAD

MACRO MUSINGS

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THE OUTLOOK FOR 2018

SUMMARY

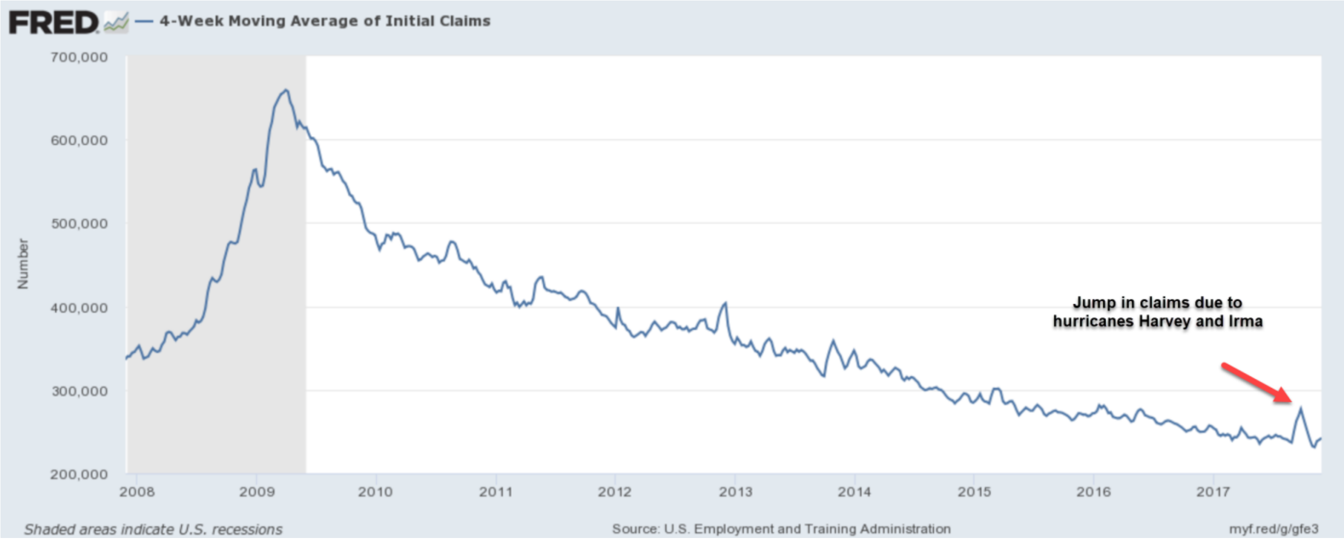
- A positive MACROCAST™ is supported by strong economic data. We expect the economy to grow for the tenth year in a row, making it the second longest economic expansion is US history.
- Next year, we will have a new Chairman of the Federal Reserve. We expect the Jerome Powell led Fed to be consistent with Ms. Yellen's tenure. We anticipate three more rate hikes in 2018.
- The market rose for the eighth consecutive month in November. Using history as a guide, this type of momentum led to better than average returns, which bodes well for at least the first half of 2018.

MULTIPLE ECONOMIC INDICATORS SUGGEST GROWTH WILL CONTINUE

The aggregate economy is doing well. Let's view this strength through the lens of three vital areas of the economy. We will look at housing, employment, and retail sales.

First, new home sales hit a decade high. Recessions do not begin as home sales are hitting multi-year records. This indicator suggests recession is at *minimum* over a year away (chart from the Fat Pitch blog):

Second, unemployment remains low, with initial claims near all-time lows:



Finally, retail sales (adjusted for inflation) notched another all-time high last month. Consumers make up 70% of GDP, so continued strength in retail sales is essential for the economy to keep growing:

NEW FED CHAIR, SAME OLD POLICY

Jerome Powell is set to take over as Chairman of the Federal Reserve early next year. At his confirmation hearing, Powell promised to continue the Fed's focus on economic growth and jobs, while keeping an open mind if the data changes. Below is an excerpt from his prepared statement at his confirmation hearing:

If confirmed, I would strive, along with my colleagues, to support the economy's continued progress toward full recovery. Our aim is to ***sustain a strong jobs market*** *with inflation moving gradually up toward our target. We expect interest rates to rise somewhat further and the size of our balance sheet to gradually shrink. However, while we endeavor to make the path of policy as predictable as possible, the future cannot be known with certainty.* ***So we must retain the flexibility to adjust our policies in response to economic developments.***

We think the choice of Powell signaled to the market that they should expect more of the same from the Fed.

When it comes to the actual policy, the Federal Reserve is expected to raise rates by 0.25% at their meeting next week. This puts the total number of rate hikes for the year at three, while the percentage increase in the Fed funds rate totaled 0.75%. Based on their commentary in recent months, expect the Fed to increase rates by the same amount next year. This would put the Fed funds rates north of 2.00% at the end of 2018, a level that has not been seen since the Spring of 2008.

THE MARKET'S STRONG PERFORMANCE HISTORICALLY BODES WELL

One important theme in 2017 was the consistent gains in the market. November was the 8th consecutive month that the S&P 500 was positive (and 12th consecutive if you include dividends). This is rare, but when it did occur, future returns were promising (table from Schaeffer's Investment Research):

S&P 500 After 8-Month Winning Streak

	1-Month Return	3-Month Return	6-Month Return	1-Year Return
No. of Returns	9	9	9	9
Average Return	0.56%	4.94%	7.62%	13.16%
Median Return	-0.03%	3.46%	10.45%	12.06%
Percent Positive	44%	89%	89%	78%
Std. Deviation	3.93%	5.79%	6.29%	16.85%

Six months later, the market rose eight out of nine times, with an average return of near 8%. The return numbers do not look as robust 12 months out, but even those returns are still above average.

With a positive MACROCAST score, strong economy, and strong momentum, we believe the market has a great chance of finishing positive in 2018. If it does, it would be the 10th consecutive year of market gains, to match 10 years of economic growth.

HAPPY HOLIDAYS

This is the final Macro Musings of the year. We will publish our 2017 Year in Review late next month.

All of us at Corbett Road would like to wish you a happy and joyous holiday season and successful New Year. Thank you for your continued trust and business.

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