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THE REGISTER CITIZEN

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THE MIDDLETOWN PRESS

MARKET MATTERS: Where's the puck going now?

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Hockey playoffs ended earlier this month with the Pittsburgh Penguins winning the NHL championship. For those teams fortunate enough to make the playoffs and move forward, it's a long and grueling post season. As investors, we also experience "seasons" — periods of higher and slower growth — beginning and ending. With the economic expansion in the U.S. entering its 9th year in July, the current "season" has been a long one — the third-longest in U.S. history.

Although it doesn't appear that this period of growth is going to end imminently, it makes sense to periodically review your portfolio to make sure it reflects what you're trying to accomplish. Unlike the players on our favorite sports teams, our portfolios don't have the luxury of off seasons.

A famous saying of Wayne Gretzy, thought by many hockey fans to be the greatest player of all time, is "I skate to where the puck is going to be, not where it has been." This can have meaning for investors; we also should be thinking about where investment opportunities lie in front of us, not the other way around. Keeping our eye on the future prevents us from falling into something behavioral economists call hindsight bias. This unfortunate trap is akin to driving your car while looking out the review mirror.

So what does the future hold for our portfolios? Morgan Stanley believes the Federal Reserve will raise interest rates again in December of this year and possibly four times in 2018. If this type of restrictive monetary policy by our central bank occurs, it will more than likely have a negative impact on the prices of high quality, domestic corporate bonds and U.S. government bonds. Consider playing defense with your allocation to these asset classes.

Stocks both here in the U.S. and in select international markets are a different story. As much as investors seem to be focusing on political turmoil, underlying economic conditions and corporate earnings have been very good. Unfortunately, for many investors, their attention has been on the “noise,” and not on these two factors that ultimately drive stock prices up and down.

The U.S. market, as measured by the S&P 500, experienced robust sales growth of 7 percent and earnings growth of 15 percent in the first quarter of this year. Although Morgan Stanley believes earnings growth will slow to high single digit growth in the second and third quarters of this year before returning to low double-digit growth in the fourth quarter, we believe this type of growth from these price levels should produce returns of 10 percent to 12 percent.

Japan, the Eurozone and emerging markets have been reporting even better growth than here at home, with the possibility of it continuing for some time to come. With expectations of the U.S. dollar rally fading, stabilized commodity prices, deflation reversing to moderate inflation and the consumer coming to life, these areas offer investment opportunities that may outperform the U.S. for multiple business cycles. Based on the possibility of long-term outperformance, these opportunities are potentials for playing offense in the equity part of your portfolio — as always, only in a manner consistent with your risk tolerance and time horizon.

For long-term investors, there appear to be many opportunities that offer attractive risk-reward profiles in equity markets. As well, overseas markets appear to be in pre-game warm up or the early stages of recovery and are poised to make crowds of investors cheer.

With that in mind, it is important to remember that too many checks of your portfolio can lead to a short-term focus that can cause you to take your eye off of the ultimate prize — achieving your goals with your portfolio by positioning it to take advantage of where you think world markets are ultimately going.

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