

Snapshot of the economic and market update for the first quarter of 2019

January 2, 2019

[Jump to disclosures](#)

Hello. This is David Kelly. I'm chief strategist here at JP Morgan Funds. And I head the team that produces the Guide to the Markets.

For many years, I've been an enthusiastic, although distinctly untalented, long distance runner. Each year, as I get older, the experts tell me I will get a little slower and a little bit more prone to injury. And each year, because of this, I need to be a little bit more disciplined in my training strategy.

The current economic expansion and bull market in equities have much in common with an aging runner. Both should stay on the road in 2019, but both should advance at a slower pace than a few years ago, and both will be more vulnerable to an accident. This being the case, investors will need to be more disciplined both in the design and implementation of a strategy. And any such strategy should start with a broad understanding of today's financial environment.

Helping provide this understanding is, of course, the fundamental goal of the Guide to the Markets. However, it's important to do so concisely. There is 65 pages in the guide, but that's way too many for any conversation with an investor about the markets. So what we do here is boil it down to just the top 10 slides in the guide and how you can use these to describe the investment environment. In particular, I'd like to talk about growth, jobs, profits, inflation, the global picture, the Federal Reserve, fixed income, US equities, international equities, and diversified investing.

Starting with economic growth, the US economy accelerated in 2018, with real GDP growth reaching 3% year over year by the third quarter. This was a fairly predictable result of a big tax cut that kicked in at the start of the year. However, as we enter 2019, it is equally predictable that growth will slow down again. In retrospect, the tax cut appears to be more effective at stimulating consumer spending than investment. And without any fresh tax cuts, overall GDP growth is likely to slide back to the roughly 2% pace that it averaged between 2010 and 2016. However, it's important to recognize that barring a major shock, the economy should be able to avoid a recession and sustain this pace into 2020.

There are really two reasons for this judgment. First, none of the cyclical sectors of the economy, such as autos, housing, business investment, spending or inventories, appear overextended. Nor does there seem to be any particular danger of financial excess. Without a boom, it's hard to generate a bust.

Second, while we expect the Federal Reserve to raise interest rates twice more in 2019, they will likely end this tightening cycle at a much lower level of interest rates than is typical for a long economic expansion. They can do this because in contrast to previous cycles, inflation has remained remarkably stable. But by doing so, they may enable the economy to continue to grow for longer than would usually be the case, as well as maintain the valuation argument for riskier assets relative to government bonds.

In the short run, in a rising rate environment and a growing economy, current valuations still favor stocks over bonds. Within the bond market, this environment should also favor taking some credit risk in areas like high yield, rather than duration risk and very long-term interest rate sensitive bonds. However, if interest rates do gradually rise in the months ahead, this positioning will have to be continually monitored as bonds approach more normal valuations.

2018 marks the 10th anniversary of the onset of the global financial crisis, which precipitated a bear market in equities around the world and the biggest global recession since the Great Depression. While both financial markets and economies have fully recovered from this trauma in memory continues to induce a more cautious attitude among investors. This is as it should be. And investors need to maintain balance in order to be prepared for the next downturn, whenever it occurs.

In addition, investors should recognize that a low interest rate environment combined with a long bull market in stocks limits potential portfolio returns going forward. However, with both the US and global economies growing, opportunities remain across the spectrum of global financial markets. And while the bull market in equities is old, it has no particular expiration date.

Equally relevant is the fact that despite Fed tightening, real yields in cash remain close to zero. In a world of very cautious central banks, investors no longer get paid for saving. They only get paid for investing.

Looking forward, we still think the global economy at current valuations justify a diversified approach to long-term investing. However, as interest rates rise and equity prices rise, it will become increasingly important for investors to move back to a more balanced approach. The economy in markets still have room to run. But an older expansion and bull market call for a more disciplined approach, with smaller overweights and underweights relative to a normal portfolio and a heightened willingness to adjust asset allocation as valuation differences diminish and late cycle risks gradually rise.

[MUSIC PLAYING]

Chart 1: Source: BEA, FactSet, J.P. Morgan Asset Management.

Values may not sum to 100% due to rounding. Quarter-over-quarter percent changes are at an annualized rate. Average represents the annualized growth rate for the full period. Expansion average refers to the period starting in the third quarter of 2009.

Guide to the Markets – U.S. Data are as of November 30, 2018.

Chart 2: Source: BLS, FactSet, Federal Reserve, J.P. Morgan Asset Management.

Real 10-year Treasury yields are calculated as the daily Treasury yield less year-over-year core CPI inflation for that month except for November 2018, where real yields are calculated by subtracting out October 2018 year-over-year core inflation.

Guide to the Markets – U.S. Data are as of November 30, 2018.

Chart 3: Source: Barclays, Bloomberg, FactSet, MSCI, NAREIT, Russell, Standard & Poor's, J.P. Morgan Asset Management.

Large cap: S&P 500, Small cap: Russell 2000, EM Equity: MSCI EME, DM Equity: MSCI EAFE, Comdty: Bloomberg Commodity Index, High Yield: Bloomberg Barclays Global HY Index, Fixed Income: Bloomberg Barclays US Aggregate, REITs: NAREIT Equity REIT Index. The "Asset Allocation" portfolio assumes the following weights: 25% in the S&P 500, 10% in the Russell 2000, 15% in the MSCI EAFE, 5% in the MSCI EME, 25% in the Bloomberg Barclays US Aggregate, 5% in the Bloomberg Barclays 1-3m Treasury, 5% in the Bloomberg Barclays Global High Yield Index, 5% in the Bloomberg Commodity Index and 5% in the NAREIT Equity REIT Index. Balanced portfolio assumes annual rebalancing. Annualized (Ann.) return and volatility (Vol.) represents period of 12/31/02 – 12/31/17. Please see disclosure page at end for index definitions. All data represents total return for stated period. Past performance is not indicative of future returns.

Guide to the Markets – U.S. Data are as of November 30, 2018.

For the purposes of MiFID II, the JPM Market Insights and Portfolio Insights programs are marketing communications and are not in scope for any MiFID II / MiFIR requirements specifically related to investment research. Furthermore, the J.P. Morgan Asset Management Market Insights and Portfolio Insights programs, as non-independent research, have not been prepared in accordance with legal requirements designed to promote the independence of investment research, nor are they subject to any prohibition on dealing ahead of the dissemination of investment research.

This content is a general communication being provided for informational purposes only. It is educational in nature and not designed to be taken as advice or a recommendation for any specific investment product, strategy, plan feature or other purpose in any jurisdiction, nor is it a commitment from J.P. Morgan Asset Management or any of its subsidiaries to participate in any of the transactions mentioned herein. Any examples used are generic, hypothetical and for illustration purposes only. This material does not contain sufficient information to support an investment decision and it should not be relied upon by you in evaluating the merits of investing in any securities or products. In addition, users should make an independent assessment of the legal, regulatory, tax, credit, and accounting implications and determine, together with their own professional advisers, if any investment mentioned herein is believed to be suitable to their personal goals. Investors should ensure that they obtain all available relevant information before making any investment. Any forecasts, figures, opinions or investment techniques and strategies set out are for information purposes only, based on certain assumptions and current market conditions and are subject to change without prior notice. All information presented herein is considered to be accurate at the time of production, but no warranty of accuracy is given and no liability in respect of any error or omission is accepted. It should be noted that investment involves risks, the value of investments and the income from them may fluctuate in accordance with market conditions and taxation agreements and investors may not get back the full amount invested. Both past performance and yields are not reliable indicators of current and future results.

J.P. Morgan Asset Management is the brand for the asset management business of JPMorgan Chase & Co. and its affiliates worldwide.

To the extent permitted by applicable law, we may record telephone calls and monitor electronic communications to comply with our legal and regulatory obligations and internal policies. Personal data will be collected, stored and processed by J.P. Morgan Asset Management in accordance with our [Company's Privacy Policy](#). For further information regarding our regional privacy policies please refer to the [EMEA Privacy Policy](#); for locational Asia Pacific privacy policies, please click on the respective links: [Hong Kong Privacy Policy](#), [Australia Privacy Policy](#), [Taiwan Privacy Policy](#), [Japan Privacy Policy](#) and [Singapore Privacy Policy](#).

This communication is issued by the following entities: in the United Kingdom by JPMorgan Asset Management (UK) Limited, which is authorized and regulated by the Financial Conduct Authority; in other European jurisdictions by JPMorgan Asset Management (Europe) S.à r.l.; in Hong Kong by JF Asset Management Limited, or JPMorgan Funds (Asia) Limited, or JPMorgan Asset Management Real Assets (Asia) Limited; in Singapore by JPMorgan Asset Management (Singapore) Limited (Co. Reg. No. 197601586K), or JPMorgan Asset Management Real Assets (Singapore) Pte Ltd (Co. Reg. No. 201120355E); in Taiwan by JPMorgan Asset Management (Taiwan) Limited; in Japan by JPMorgan Asset Management (Japan) Limited which is a member of the Investment Trusts Association, Japan, the Japan Investment Advisers Association, Type II Financial Instruments Firms Association and the Japan Securities Dealers Association and is regulated by the Financial Services Agency (registration number "Kanto Local Finance Bureau (Financial Instruments Firm) No. 330"); in Australia to wholesale clients only as defined in section 761A and 761G of the Corporations Act 2001 (Cth) by JPMorgan Asset Management (Australia) Limited (ABN 55143832080) (AFSL 376919); in Brazil by Banco J.P. Morgan S.A.; in Canada for institutional clients' use only by JPMorgan Asset Management (Canada) Inc., and in the United States by JPMorgan Distribution Services Inc. and J.P. Morgan Institutional Investments, Inc., both members of FINRA; and J.P. Morgan Investment Management Inc.

In APAC, distribution is for Hong Kong, Taiwan, Japan and Singapore. For all other countries in APAC, to intended recipients only.

Copyright 2018 JPMorgan Chase & Co. All rights reserved.

Recorded December 17, 2018