Voya Global Perspectives

Markets. Insights. Opportunities.®

Douglas Coté, CFA
Chief Market Strategist

Karyn Cavanaugh, CFA
Senior Market Strategist

Stick to the Plan and Don't Fight the Fed

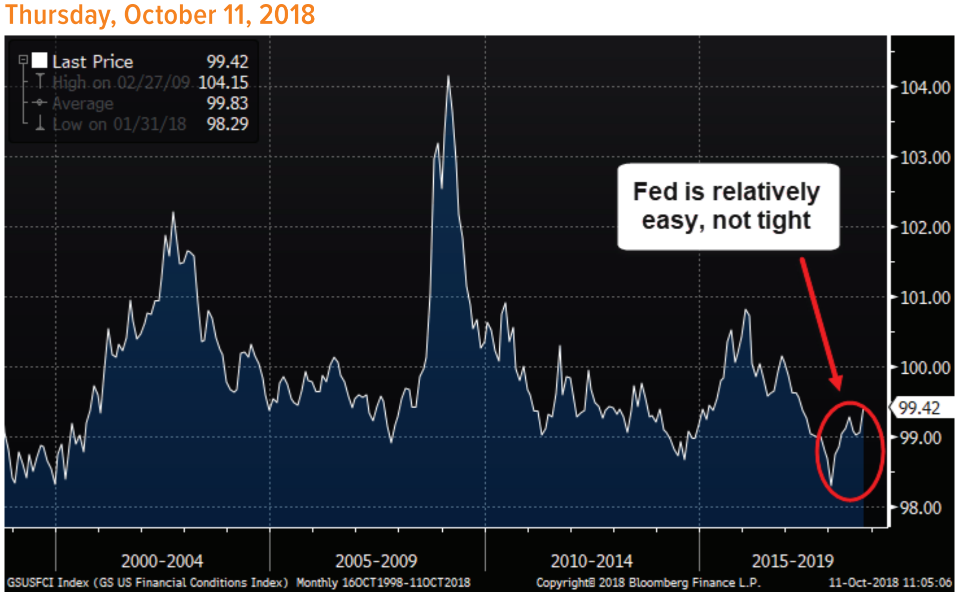
The markets got walloped Wednesday on a Fed that has been raising interest rates at the fastest pace in over a decade, and with expectations for more to come. In fact, the Federal Reserve has raised rates seven times since President Trump was elected. The Fed seems well within their mandate since unemployment is at a 49-year low, economic growth has jumped to 4.2%, corporate earnings are at all-time highs, and financial conditions are relatively easy (see chart). The Fed is arguably trying to keep in-line with an economy that is booming and to tamp down on excesses before they get too extreme. Yesterday's "tech wreck" is a sure signal that things were trending toward extremes, and if anything the Fed likely will be proven correct with its "shot across the bow".

The difficult aspect for investors is that their returns, which were not stellar year to date, just took another hit. Through the third quarter, performance of a diversified portfolio of stocks and bonds was up a dreary 1.7%. However, thus far in the fourth quarter through today:

- S&P 500 large cap stock performance is -4.5%
- S&P 600 small cap stock performance is -7%
- Emerging Market equity performance is -8%
- U.S. corporate bonds performance -1.5%
- U.S. treasury 20 year + long bond performance is -2.75%

Wait a minute. Investors are so concerned about rising rates and their impact on bonds, but even long U.S. Treasury bonds are a hedge compared to equity performance. Yes: building a globally diversified portfolio of stocks and bonds can smooth out the volatility impact that investors' experience. That is why we advocate to "stick to the plan" that you implemented during sounder times considering that market corrections happen – normally – two to three times per year.

Thursday, October 11, 2018



Source: Bloomberg Finance 10/11/18

In our quarterly outlook "The Economic Boom 10 Years after the 2008 Credit Crisis" we pointed out our concern about rising rates and the economy in sections:

- "Economic Growth with a High Degree of Difficulty", reviewing the speed of the Fed rate increases and the resilience and strength of the economy despite the rate increases;
- "Investors Pessimistic About Equities", reviewing that despite markets rising, especially in technology, inflows have been in to bonds over equities this year;
- "Dollar Dread and Interest Rate Anxiety", Rising rates have the ability to disrupt markets. Rising rates impact financial assets by lifting the implicit discount rate and puts downward pressure on earnings multiples.

Market corrections are normal and we last saw one in February 2018. Rates are rising because the economy is so good. This is not a Fed Policy mistake; we are just getting back to normal, and that is disruptive to markets. **"Stick to the Plan and Don't Fight the Fed."**

BBGP-Market Correct 101618 • IM1015-45655-1019