CAPITAL MANAGEMENT GROUP
of Wells Fargo Advisors

The Hefter Report – February 2018

The Pause that Refreshes

It is our fundamental view that the "animal spirits" rally that began in November 2016 is still intact both domestically and globally. Other than some moderate flattening of the yield curve, we do not see any signs of a recession in the near term. Instead, we see synchronized global GDP growth the likes of which we haven't seen since before the Great Recession. Global trade and capital spending have also improved and show no signs of slowing down.

Across the globe, interest rates have moved higher with the US 10 year treasury yielding 2.83% as of February 2nd. That is a 15.5% increase in just one month and signals the end of monetary stimulus and a shift in central bank concern from disinflation to inflation. Although rising interest rates can be a negative for stocks down the road, we don't see any major threat to equities until the 10 year treasury reaches a minimum of 3% (where it was back in 2013). As global economies improve and inflation picks up, commodities usually increase in price. We are seeing that price rise in oil, gold, copper and other natural resources. This is helping emerging markets countries such as Brazil, Russia and South Africa as well as developed countries such as Canada and Australia. We remain overweight in both international bonds and stocks and have stated since November 2016 that the US dollar was overvalued. The precipitous drop in our domestic currency has substantially benefitted our overseas investments. We believe this will continue through 2018 and beyond.

In addition to our being overweight Japan, Europe and emerging markets, we prefer sectors that will benefit from rising interest rates and/or significant tax relief. These include financials and technology. We also believe that global economic growth will benefit energy, industrials and materials more than defensive areas such as consumer staples and utilities.

Our technical analysis gives us some pause for concern. The major US stock indices are now 5% over their moving averages. This has prompted us to raise some cash in order to buy stocks should they return to their trend lines. However, this is just a precaution, as we are otherwise fully invested and believe global equities will continue their upward trend. We are negative on US government, high quality corporate and municipal bonds as we believe there is a major trend reversal occurring in US interest rates. We prefer international bonds with higher yields and the potential for currency appreciation. To hedge risk, we have shifted some funds to long-short managers and are prepared to buy short equity index exchange traded funds if we believe that becomes warranted.

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