



## Powell does his part; now it's up to Trump and Xi

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The equity market got what it was hoping to get out of Fed Chair Powell's lunchtime address before a packed audience of about 1,200 investment professionals at the Economic Club of New York today. Now that leaves us with another hurdle that can hopefully be cleared in the coming week, a meeting between Presidents Trump and Xi of China.

For now, let's focus on the Fed. Two months ago, Powell told us that we were well short of neutral with interest rates, so the market feared that the Fed would execute on its hawkish dot plots. Today, his updated thinking is that we're now just below neutral, indicating a quarter-point hike in the target funds rate in December to 2.5%, another hike to 2.75% in the first of half of next year, and then maybe we're done. That's a far cry from where the dot plot had us at September's meeting of policymakers: one hike in December, three more in 2019 and one more in 2020, taking us to a terminal value of 3.5%.

In his speech, Powell described a U.S. economy that's in pretty good shape, with unemployment at a 49-year low, core inflation around the Fed's 2% target and GDP running at a sustainable 3% annual pace, well above what many thought possible just a year ago. Notably, Powell said the Fed has no pre-set policy path for future rate hikes; it will let incoming data determine what it will—and won't—do. He sees no dangerous excesses in the stock market at present, with forward P/E multiples now back to roughly their long-term average of 15, having contracted 3 full points so far this year. On the international front, the Fed's keeping an eye on U.S./China trade negotiations, Brexit and Italy's debt discussion with the European Union. In a Q&A, Powell used his famous furniture-in-the-dark analogy—policymakers are willing to go slower to keep risks at bay. They don't want to stub their toe, i.e., make a policy error, without having a clear view of the issues at hand.

**My takeaway:** It looks like the S&P 500's double bottom at 2,600 will hold. If Trump and Xi provide anything remotely positive at this weekend's G-20 meeting, that effectively means two of the market's major risks—a too-fast Fed and a China trade war, both of which could push us into recession—will be averted. Such a positive scenario should let stocks continue to rally hard into year-end, approaching September's highs and providing a potential double-digit rally that would affirm our barbell-year forecast in 2018. That, in turn, could set us up for a nice continuation into 2019, with a low double-digit year and S&P approaching our 3,300 intermediate-term target price. We'll keep you posted.

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Price-earnings multiples (P/E) reflect the ratio of stock prices to per-share common earnings. The lower the number, the lower the price of stocks relative to earnings.

S&P 500 Index: An unmanaged capitalization-weighted index of 500 stocks designated to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries. Indexes are unmanaged and investments cannot be made in an index.

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