COVINGTON
CAPITAL MANAGEMENT

Investment Outlook

January 2019

	POSITIVES	NEGATIVES	
ECONOMIC	▪ US economy continues to expand ▪ US employment strong and wages growing ▪ Consumer & small business confidence remains high ▪ Foreign interest in US investments continues ▪ Interest rates remain relatively low ▪ Leading indicators remain strong ▪ No signs of a recession on the immediate horizon	▪ Global manufacturing indices trending down ▪ European central banks reducing stimulus ▪ China's slowing growth hurting Asian markets ▪ Brexit looming and path uncertain ▪ Higher rates increasing debt service costs ▪ Emerging markets hurt by weak currencies ▪ Upward pressure on inflation	ECONOMIC
FISCAL	▪ Lower personal tax rates encourage consumer spending ▪ Lower corporate tax rates make US more competitive ▪ Infrastructure projects may be on the horizon	▪ Budget deficits on the rise ▪ Debt ceiling must be addressed once again ▪ Crowding out effect pushes private sector yields higher ▪ Protectionist policies have been ratcheted up	FISCAL
MONETARY	▪ Federal Reserve nearing end of rate normalization ▪ Federal Reserve policy remains transparent	▪ Federal Reserve unwinding large balance sheet ▪ Global central banks less accommodative ▪ Yield curve has flattened dramatically ▪ Higher mortgage rates hurting housing market	MONETARY
VALUATIONS	▪ Corporate profits continue to grow ▪ Companies raising dividends and buying back shares ▪ Stock markets at reasonable valuations ▪ International markets are trading at discount	▪ Business cycle nearing final phase ▪ Profit margins near peak levels ▪ Positive earnings revisions have slowed ▪ Market volatility scaring investors	VALUATIONS
GENERAL	▪ Cost structures have dramatically improved ▪ Corporate default rate has declined ▪ Corporations emphasizing US manufacturing base ▪ Oil/gas discoveries leading to US energy independence ▪ Friendlier regulatory environment ▪ Strong corporate balance sheets ▪ Highly capitalized financial system ▪ Unit labor costs rolling over ▪ Weak energy prices will slow headline CPI	▪ Profit growth decelerating ▪ Potential trade wars around the corner ▪ Dollar strength a headwind for US multinationals ▪ Corporate debt has reached new highs ▪ Benefits of tax reform becoming less impactful ▪ Quick twitch—algorithm driven—traders abound ▪ Mistrust of Washington and Wall Street ▪ Continued risk of cyber-terrorism ▪ Anti-immigration policies slow tech innovation	GENERAL
CATALYSTS	**What will make us more bullish on equities:** ▪ Trade tensions diminish ▪ Corporate profits surprise to the upside ▪ Corporations boost capital spending ▪ Merger activity accelerates ▪ Upturn in the Chinese economy ▪ European fiscal integration ▪ Inflation pressures moderate ▪ Extreme market fear and rampant pessimism	**What will make us more bearish on equities:** ▪ Inflation accelerates ▪ Synchronized global recession ▪ Housing prices turn down precipitously ▪ Interest rates rise faster than anticipated ▪ Yield curve inverts ▪ Consumer confidence declines ▪ Dollar collapses—foreign liquidation of U.S. debt ▪ Business investment slows ▪ Geo-political crisis—Iran, North Korea, Russia, Turkey	CATALYSTS
SUMMARY	**We are in the later-stages of the business cycle, warranting prudent asset allocation rebalancing: gradually increasing cash positions, maintaining higher quality and shorter maturity fixed income holdings, and broadening equity diversification with a focus on durable competitive advantages and predictable cash flows.**		SUMMARY