Martone Capital Management: Weekly Investment Commentary (6/7/2017)

Investors shrugged off bad news last week, including disappointing economic data, falling bond yields, a sell-off in oil and escalating U.S. political uncertainty. The path of least resistance for stock prices was to the upside.

Investors remain highly focused on global political issues. Emmanuel Macron's victory in France has reduced some political risk in Europe, but investors are growing increasingly skeptical about President Trump's ability to deliver on his pro-growth agenda. The growing scrutiny over White House ties to Russian operatives, escalating risks of global terrorism and rising uncertainty around North Korea are all negatives for investor confidence.

But these negatives have not offset positive global macroeconomic conditions. Global economic growth is hardly robust, but looks better than it has in several years, especially in Europe. Manufacturing activity is improving and global trade appears to be recovering. Corporate profits are also trending higher across most markets and industry sectors. Financials remain a weak spot in many areas of the world, but we expect global bond yields will rise as economic growth solidifies, which should help this sector. Finally, monetary policy remains growth- and equity-friendly. The Fed is in the midst of a rate-hiking campaign, but should continue raising rates slowly and predictably.

Given all of the crosscurrents, we see reasons for both optimism and pessimism about global stocks. On the upside, equity markets could climb briskly as investor confidence improves in light of strengthening global economic growth and strong corporate earnings and profits. On the downside, the potential for an accelerating slowdown in China may lead to falling trade levels and renewed fears of global deflation and recession.

We believe the upside scenario is more likely, but our optimism is tempered because valuations are less attractive than they used to be. We think equity prices will move unevenly higher over the next 6 to 12 months, but also expect returns to be more modest than what investors have seen in recent years.