3 FACTORS Supporting a Strong Market

By Matt Orton

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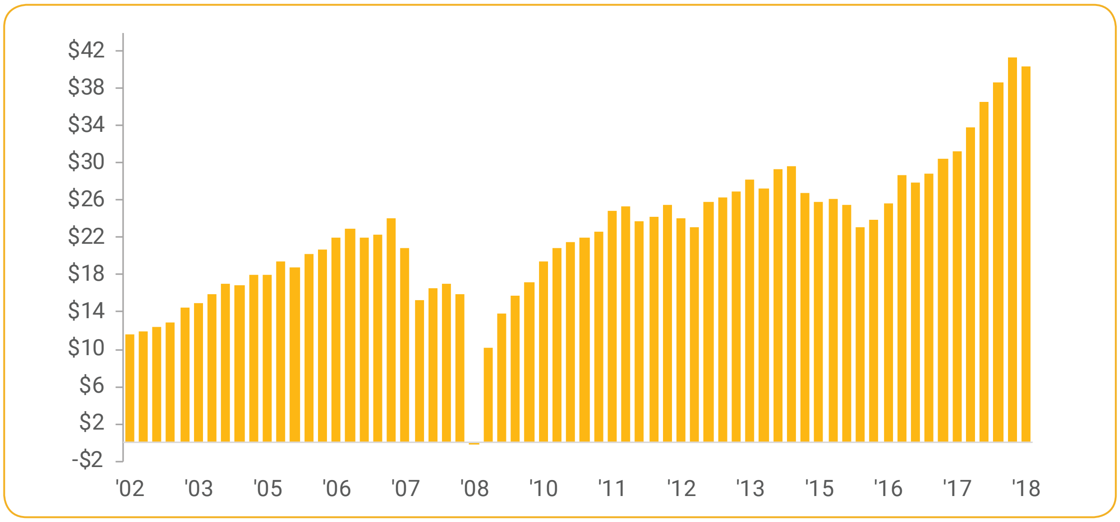
The United States is experiencing what may soon become the longest bull market in 150 years. Many investors are apprehensive about the end of the market cycle and what could follow. I believe the following three factors support the case for informed investor confidence.

1. EARNINGS GROWTH

In the first month of 2019, the S&P 500 posted the strongest January gains since 1987. There are possibly fewer factors more correlated to the long-term direction of the market than earnings growth, and corporate profitability still appears strong. Corporate earnings growth is expected to normalize as tax cuts roll off and global growth slows. EPS growth expectations, however, remain positive through 2019.

Earnings growth remains positive despite heightened fears

S&P 500 Operating Earnings Per Share (EPS)



Source: S&P Dow Jones Indices. Operating earnings are profit earned after subtracting from revenues those expenses that are directly associated with operating the business, such as the cost of goods sold, general and administration, selling and marketing, research and development, depreciation and other operating costs. It is a measure of profitability that tells investors how much of revenue will eventually become profit for a company.

2. CONSUMER CONFIDENCE

Consumer confidence indices may have pulled back from recent highs, but they remain at the upper end of their historic range. Solid jobs growth has helped sustain that optimism, despite not having strong wage growth. Consumer confidence has also helped offset some damage from trade concerns, which is important, since a consumption-based economy depends on consumers feeling comfortable spending money.

Confidence has rebounded post-Q4 market moves

Conference Board Consumer Confidence Index (9/30/1977 – 3/22/2019)

Source: Bloomberg

While consumer confidence declined along with the markets through the fourth quarter of 2018, levels rebounded in February with the gauge of Americans' views on present conditions rising to an 18-year high. The Conference Board reported that its Consumer Confidence Index rose from 121.7 in January to 131.4 in February and The Present Situation Index improved, as consumers continue to view both business and labor market conditions favorably.

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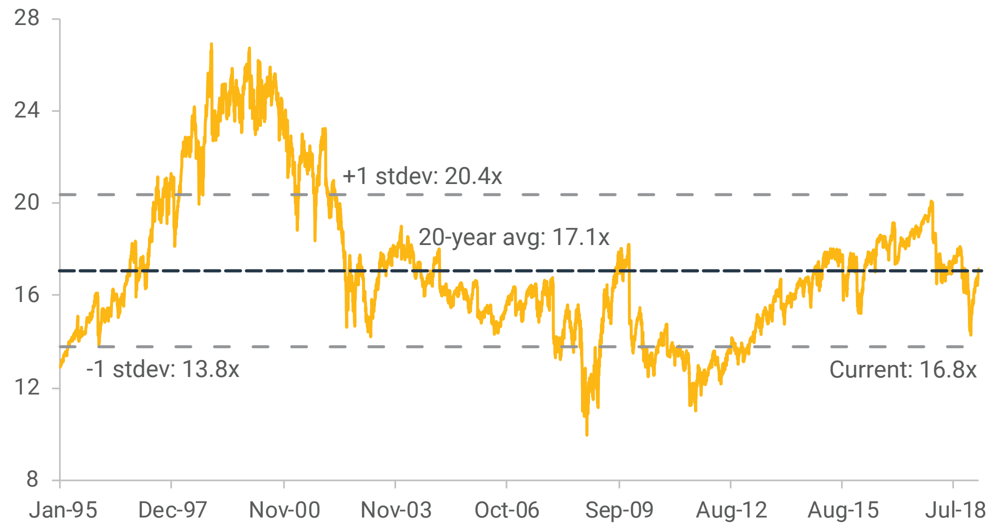
3. REASONABLE VALUATIONS

Valuations look more attractive than they have for some time, with markets having pulled back to correction territory in conjunction with expanding earnings. With earnings growth of the S&P 500 in excess of 20 percent in 2018, we saw one of the largest multiple contractions in recent history, as markets separated from fundamentals. Following the market rebound in early 2019, valuations are only approaching long-term averages, and there remains a very strong fundamental backdrop in place.

Valuations have normalized

S&P 500 Index 12-month forward P/E



Source: FactSet, S&P Dow Jones. Price to earnings is price divided by consensus analyst estimates of earnings per share for the next 12 months as provided by IBES since December 1989, and FactSet for March 22, 2019. Average P/E and standard deviations are calculated using 25 years of FactSet history. Std. dev. over-/under-valued is calculated using the average and standard deviation over 20 years for each measure. Forecasts are represented by consensus FactSet analyst views. Past performance is not a guarantee of future results.

STAY THE COURSE, AIM TO MINIMIZE RISK

Risks that should be closely monitored in 2019 include evolving trade negotiations with China, slowing global economic growth and communication of monetary policy by the Fed.

The Fed funds futures are increasingly pricing in the probability of a rate cut in 2020, which contrasts with where the dot plots are, and that could present a challenge for equities. The deviation is going to have to be reconciled, and any communications missteps by the Fed – like in December 2018 – could be a risk.

The brief inversion of the yield curve between the 3-month and 10-year Treasury in late March alarmed many investors. Historically, it has proven to be a reliable indicator of a recession; however, recessions have tended to follow periods of **sustained** yield curve inversion – not the dip of a day. Even if a recession does follow, that does not ensure a repeat of the Financial Crisis of 2008.

A yield curve inversion certainly highlights the need to focus on risk, but it does not mean investors should run for the hills. Panic surrounding brief inversions could even be a good buying opportunity, provided the fundamentals are still supportive.

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Matt Orton is a vice president and portfolio specialist at Carillon Tower Advisers, working with two of Carillon's affiliates, ClariVest Asset Management and the Growth Team of Eagle Asset Management. In addition to supporting these teams, He also provides U.S. market commentary, strategy, and analysis for clients.

Orton has nine years of investment experience and joined Carillon Tower from BNP Paribas in New York where he was a Vice President in the Global Equity & Commodity Derivatives group, focusing on hedge fund and asset manager structuring and sales. Prior to that, he worked for Goldman Sachs Asset Management within the Quantitative Investment Strategies team where he focused on volatility research.

He earned his MBA with a concentration in Capital Markets & Asset Management from Cornell University and his bachelor's degree from Vanderbilt University.

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