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Start me up? Or Shut me down?

By Allen Harris

The big story this week is….oh, wait, there are two big stories this week. One is a two-day meeting of the Federal Reserve. The scheduling of the meeting itself is nothing new and not typically, by itself, a big deal. But this one is because the right words could start a rally in stocks. Or, just as easily, could justify the slump.

The other big story is the Friday deadline for lawmakers to get their act together to avoid a government shutdown. After watching last week's casual Oval Office sit-down-gone-tantrum among President Trump and rival Democratic leaders Nancy Pelosi (House) and Charles Schumer (Senate), I don't see a shutdown being avoided. If an agreement can't be made on spending bills, the government will shut down. At the center of the debate is that President Trump wants $5 billion to fund a border wall one the US-Mexico border. At the time of that raucous meeting Democrats were willing to allot $1 billion (specifically for new fencing and levee walls, but no solid concrete walls), but Mr. Trump appears very comfortable, even proud, to be able to shut down the government in the name of border security.

And Ms. Pelosi seems to be considering this a political gift, ready with branding of a potential shutdown as the "Trump Shutdown", using the term freely and repeatedly, as if knowing that she can make it stick all the way up to the Presidential Debates. Seeing the potential strength of the "Trump Shutdown" phrase, Republicans tried to steal it and label it the "Schumer Shutdown". And while I admit the alliteration makes is sound so much better, they just weren't clever enough to strike first and get first-to-market status.

Trump Shutdown doesn't have the same ring to it, but it's sticking. And the Democrats clearly see the political benefit of letting the President have his way when it comes to shutting down the government. On Sunday Chuck Schumer said

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that President Trump "…isn't going to get the wall in any form…all he is going to get with his temper tantrum is a shutdown."

Right now you're r reading this and either cursing Trump or tirading against the Democrats, depending upon how your political ideology shapes your narrative. But your money doesn't care about your ideology. Your money cares about the US debt-ceiling crises of 2011 and 2013, and whether or not the pressure we saw in stock markets due to those will repeat in 2019 .The Friday deadline is not a debt-ceiling conversation (it's about the expiration of seven spending bills simultaneously expiring at 12:01 am Saturday, December 21), but they offer proxies for what type of pressure we might expect on stock prices. And it's a headwind, at the least.

Political poison as it may be for Trump to go through with this shutdown, he did shut it down January 2018 over the Deferred Action for Childhood Arrivals (DACA) immigration policies. A government shutdown would see hundreds of thousands of federal employees working with no guarantee of pay, although in situations like this they're typically paid retroactively. From a purely economic standpoint relative to the US GDP, it's nominal. However, the political infighting dampens animal spirits that flow capital into investments, which is a threat to portfolio values.

The other side of that Friday threat is the Wednesday wish. The economy and the stock market wishes for dovish language at the conclusion of the Fed's meeting. A hike of 0.25% for the federal funds rate to a range of 2.25-2.50% is widely anticipated, so we're not realistically expecting a pause. A pause may be warranted, but given Mr. Trump's tirade about his dissatisfaction over Fed Governor Jay Powell raising rates, the President has made it so that a pause makes the Fed appear political, when it's not. Trump has forced the hand of the Fed to raise rates on Wednesday, even if it wanted to hold off.

So, instead of wishing for an unrealistic pause, the stock market is willing to start a new rally if the Fed comes out after its meeting and says interest rates are deemed neutral and no longer need to go up unless data shows the economy is overheating.

I do wish we could be running the risk of overheating in 2019, but that's not going to be an issue. We expect growth in US GDP next year (the recession will come soon thereafter). Growth will certainly be slower than 2018, and not nearly hot enough to warrant as many rate hikes as the consensus currently expects. Still though, rates have gone up enough to slow the housing sector. Housing has an outsized impact on recession and recoveries. But given we've run out of time, that's a story for another column. A horror story.

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