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ON THE RADAR SCREEN

1. Strong retail holiday sales would be indicative of improving sentiment and a deeper conviction that the economy remains on track.

2. Congressional budget negotiators have until mid-December to draft the parameters of an agreement to keep the government open beyond the mid-January expiration of the current funding resolution. If sequester spending cuts are replaced or meaningful reforms to tax policy and entitlement spending can be found, the markets would react favorably.

3. A reduction in the pace of quantitative easing is possible in December, but would almost certainly be accompanied by other forms of stimulus aimed at keeping short-term interest rates low for a prolonged period of time.

4. A broad reform agenda was adopted at China's recently completed Third Plenum. Details were scarce, but markets nevertheless responded favorably. We look to the Central Economic Work Conference convening in December to start filling in the blanks.

5. Territorial disputes in the East and South China Seas are again flaring up. An escalation of hostilities could derail regional and global economic growth.

GLOBAL ECONOMIC REVIEW

Market & Economic Outlook

TIMELY INSIGHTS & PERSPECTIVES

MainStay Investments is pleased to present economic and market insights from the Portfolio Managers in the Multi-Asset Solutions Group.

Level setting. The government shutdown is receding further into the past, but economists continue to wrestle with data distorted by its effects. The picture that is gradually emerging does not look much different from what was evident before the shutdown. Job losses continue to trend lower, bringing the unemployment rate down with it; the manufacturing sector shows moderate strength in most of the developed and the developing world; signs of inflation are about as common as snowfall in Barbados; the housing market continues to heal, albeit at a slower pace than was seen during the spring months. As one might expect, both stock prices and bond yields rose steadily through the month on these developments. The indicator that could bring with it a further acceleration in stock price gains could be a bump in retail sales. The holiday shopping season is upon us, and recent surveys projecting soft sales notwithstanding, we think the numbers could be quite strong (by way of a disclaimer, this is being written before Black Friday and Cyber Monday, two days that do much to set the tone for the season in total). Factors discussed in the section below are setting the stage for the return of conspicuous consumption.

Also worthy of note are events in China during the past several weeks. Slowing growth, credit excesses, and a suspiciously bubbly property market in the world's second largest economy have predictably generated considerable concern

> "I shop therefore I am."
> —*Barbara Kruger*

of late. President Xi Jinping and Premier Li Keqiang publicly elevated expectations for major reform announcements that would address some of these worries in advance of the Communist Party's third plenary meeting, arguably the most significant event of their term. The initial statement was rather hollow, leaving investors disappointed, but a more detailed document emerged a few days later listing specific areas

GLOBAL ECONOMIC REVIEW

Market & Economic Outlook *(continued from page 1)*

in which reform efforts will be focused, and seemingly embracing a greater liberalization of financial markets. Although these changes will be many years in the making, and some may never materialize at all, the market reaction was immediate and positive. Our sense, and the opinion of the majority it would seem, is that these statements do indeed reflect a genuine and welcome effort to change the direction of economic policy making that will benefit not only China, but the global economy in the decades ahead. We like what we've heard.

Over the past several years, households have reduced outstanding debt loads considerably. At the same time, home prices and investment portfolio values have increased quite sharply. Less debt and more assets mean that household net worth is a lot higher than it was four or five years ago. Job growth has been steady, inflation is very much in check, and prices at the pump have been falling. These are the kinds of things that typically leave consumers and small business owners feeling pretty good about the state of the world around them. Not so today.

A variety of consumer sentiment indicators remains at depressed levels, even though we are now four plus years into a recovery. It's unclear just what factors can be held responsible for this pervasive sense of unease, although we surmise that gridlock in Washington and the botched rollout of Obamacare are playing a role. There is typically a relationship between sentiment and consumption/investment patterns, but that has fortunately been weak during the current cycle. Retail sales and capital expenditures have fared surprisingly well under these circumstances. Nevertheless, we believe negative sentiment has been a restraint on growth, and we expect sales and investment activity to gather steam as perceptions of the economy gradually change for the better and the sense of gloom finally lifts.

> "Confidence is contagious. So is lack of confidence."
> —*Vince Lombardi*

Investors have generally maintained a more sanguine view, but even there the zeitgeist is hardly exuberant. Surveys suggest that many investors remain cautiously positioned, and we notice a bubble in bubble diagnosis. That's fine by us. The mere fact that so many are concerned about a bubble helps ensure that one doesn't develop

So, while we look for improving sentiment amongst consumers and business owners on the one hand, we hope that same cheer doesn't permeate the investment community.

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