BEHIND THE NUMBERS
A PERSPECTIVE ON THE MARKETS AND ECONOMY

CALAMOS® WEALTH MANAGEMENT

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CALAMOS WEALTH MANAGEMENT

Michael serves as CIO of Calamos Wealth Management and is a member of the Investment Committee, which oversees all aspects of investment strategy, asset allocation, and manager due diligence. In his role, he is responsible for identifying and analyzing economic trends, as well as strategic and tactical investment opportunities. Michael has more than 20 years of industry experience.

Key Upcoming Dates

January 20
U.S. Presidential Inauguration

January 27
U.S. Q4 GDP Report

February 1
FOMC Meeting

The Waiting Game

By now, we all know the story. Trump won the election, investors embraced his "pro-growth" agenda, and stocks soared. By mid-December, the Dow Jones Industrial Average was set to hit 20,000, and Wall Street was ready to celebrate. But it is now a full month later, our 45th President has been sworn into office, and the index still sits just shy of this historic level. Some are starting to wonder if it is time to put away the party hats.

A broader look reveals that it is not just equities taking a breather. Oil prices, the U.S. dollar, and interest rates have also stopped climbing, and in some cases retreated a bit. It's as though the financial markets have collectively entered a holding pattern as they decide whether to accelerate again or come in for a landing.

In retrospect, the initial post-election rally was the easy part. Investors bid stocks higher largely on the promise that the new administration will enact large tax cuts, a robust infrastructure spending plan, and a lighter regulatory environment for corporate America. In the process, valuations on the S&P 500 expanded further.

Now we must wait and see whether the policies that actually get passed validate this move higher. The legislative process will take months to fully play out, but investors have reached the point where they need some additional clarity on each of the major campaign pledges before pushing forward.

Will the federal corporate tax rate truly drop from 35% to 15%? If so, will that come at the cost of firms no longer being able to deduct interest expense? How about personal taxes? Will the rate on the highest tax bracket drop from 43.4% (including the Obamacare surcharge) down to 33%? And regarding that spending plan, just how big is "big"?

These are but a few of the central questions left unanswered at this point, and the market would much rather have specifics about these policy proposals than read about the latest Twitter war. To date, investors have tried their best to wait patiently for these policy details, though that patience is starting to wane. The latest readings on the so-called volatility index have remained close to all-time lows, and the S&P 500 has now gone 68 straight days without a decline of 1% or more – the longest such streak throughout the post-2008 recovery. With that said, we have seen more down days than up days over the past two weeks.

Perhaps the key reason why equities have held up, despite all the political uncertainty, is the improving global economic backdrop, which has picked up over the past several months across both developed and emerging markets. In the U.S., the data started to show improvement prior to the elections, creating a solid foundation on which to grow further. With the S&P 500 priced well above its 10-year average, however, Trump cannot afford to disappoint on his pledge to return the economy to a more accelerated path, aspiring to a GDP growth rate of over 3%.

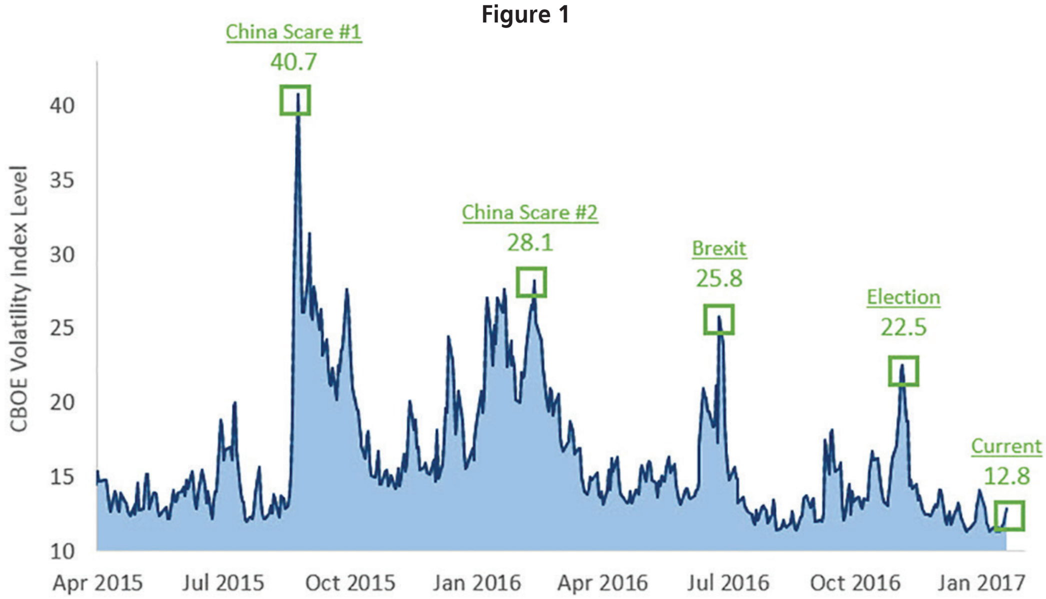
If there is one thing we have learned over the years, it is that Wall Street will not wait patiently forever. They are anxious to see whether the hype priced into the markets during November and December was indeed warranted, and they will be quick to take action if this proves to not be the case. Our new President does not strike me as particularly patient either, and I suspect we will start to get the policy specifics that investors crave, sooner rather than later. Therefore, we think it makes sense for equity investors to sit tight.

As the song goes, *the waiting is the hardest part*. We think those who manage dynamically and have the fortitude to see past short-term uncertainty will ultimately be rewarded. More simply put, good things will come to those who wait… notwithstanding a few bumps along the way.

Key Numbers

12.8 That's the current level of the CBOE Volatility Index, more commonly known as the VIX Index. This measure reflects a market estimate of near-term volatility for the S&P 500 Index. As shown below, this index has spiked several times in the past year during times of heightened uncertainty. Despite the many unknowns regarding the new administration's policy proposals, the VIX Index remains only marginally above all-time lows.

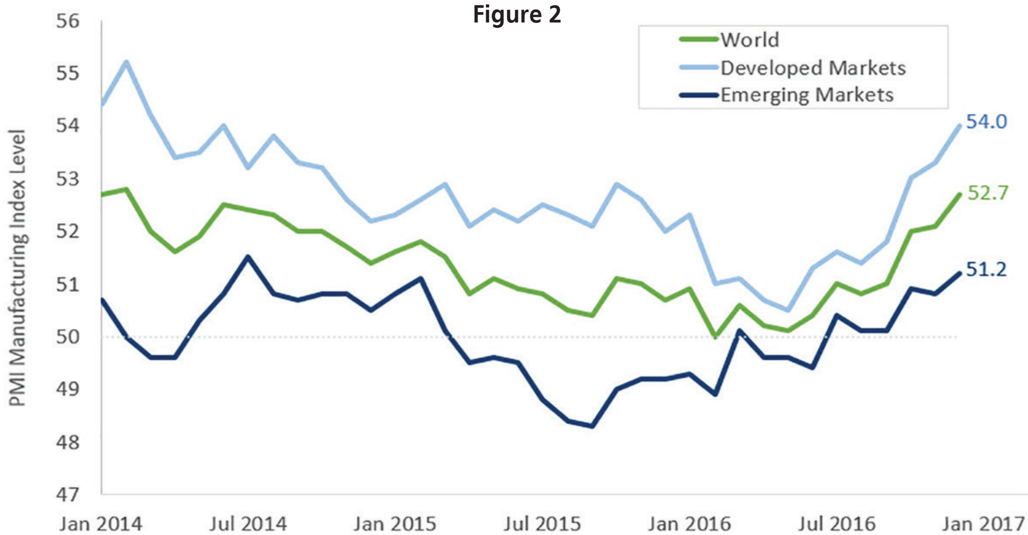
Figure 1



Source: Bloomberg.

52.7 That is the level of the JPMorgan Global Manufacturing PMI (purchasing managers' index) for December, its fourth straight month of higher readings and the highest overall number since 2014. This is further confirmation that the global economy continues to expand.

Figure 2

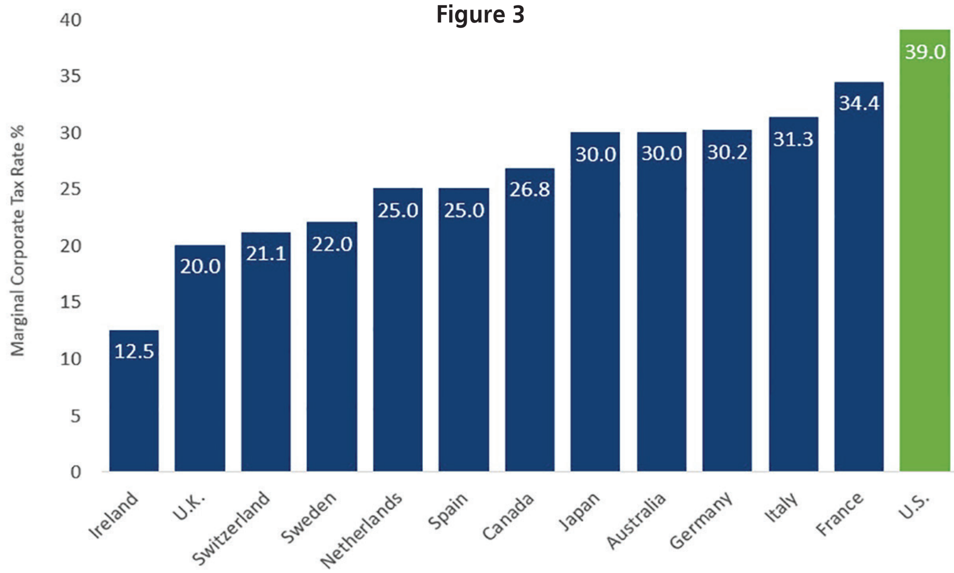


Source: IHS Markit, Institute for Supply Management, Caixin, JPMorgan, Bloomberg.

As a reminder, figures above the 50 level suggest expansionary activity, while those below 50 indicate contraction. We are encouraged that both developed market and emerging market countries are cumulatively above this critical level.

39.0 This is the country's top marginal corporate income tax rate; a composite of the 35% Federal tax rate and an average state tax rate of 4%.

Figure 3



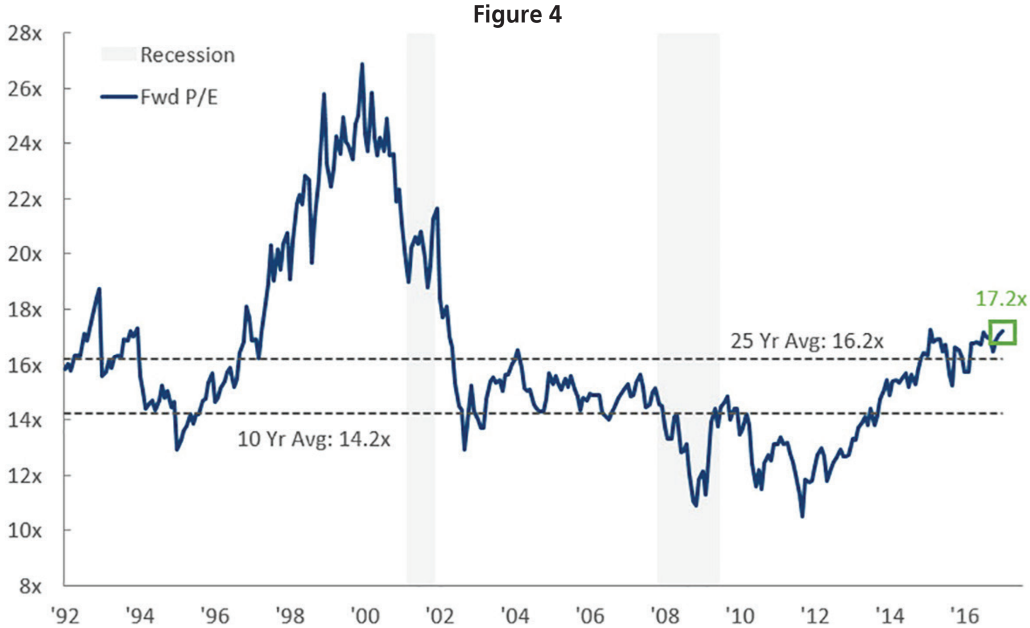
Source: Organization of Economic Co-operation and Development, Bloomberg.

Relative to the world's developed economies, the U.S. currently imposes the highest combined rate to corporate income. President Trump's avowed agenda encompasses a slash to the Federal corporate tax rate, down to 15%, which would likely be a significant boost to corporate earnings in future years.

17.2x That's the forward price-to-earnings (P/E) multiple at which the S&P 500 currently trades, which remains above the 25-year average of 16.2x for the 10th consecutive month, and well above the 10-year average of 14.2x.

Considering the comparison to average long-term P/E multiples, it is hard to call U.S. equities "cheap". However, as we've previously articulated, valuation metrics have proven to be an unreliable indicator of near-term price movements, as fully valued markets can continue to rise over months and even years.

Figure 4



Source: National Bureau of Economic Research, Bloomberg.

This is even more true given the uncertainty surrounding the positive impact of the new President's tax policies and "pro-growth" agenda on corporate America. In other words, S&P 500 earnings could well grow swiftly enough where current valuations are more than justified.

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Figure 1: Source: Bloomberg. Data as of 1/19/2017. Based upon daily closing price of the CBOE Volatility Index
Figure 2: Source: IHS Markit, Institute for Supply Management, Caixin, JPMorgan, Bloomberg. Data as of 12/31/2016. Based upon manufacturing PMI.
Figure 3: Source: Organization of Economic Co-operation and Development, Bloomberg. Data as of 12/31/2016. Based upon marginal corporate income tax rates per country.
Figure 4: Source: National Bureau of Economic Research, Bloomberg. Data as of 1/12/2017. Price to Earnings is price divided by consensus analyst estimates of earnings per share for the next 12 months. Average P/E ranges from 1/1/1992 through 'Data as of' date.

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