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5 money moves a fiscal-cliff walker is making now

Stocks, gold, commodities shape economist's 'risk-on' portfolio

By Jonathan Burton, MarketWatch

SAN FRANCISCO (MarketWatch) — Maybe Bernard Baumohl hasn't peered out of his window lately. The economist's upbeat outlook for U.S. and global stocks and commodities isn't shared by many of his fellow fiscal storm watchers.

iPhone 5 may give GDP a big boost

The iPhone 5, which Apple plans to release this week, could boost the U.S. economy in a measurable way.

To Baumohl, chief global economist at The Economic Outlook Group in Princeton, N.J., the U.S. and other major economies are on the cusp of stronger growth.

Baumohl expects the U.S. economy to grow 3.2% in 2013, with unemployment falling to 7.2% by the end of next year. Even the comatose euro zone should see full-year growth of 1.5% in 2013, he predicts.

"The U.S. economy is fundamentally in better shape than it was four or five years ago," Baumohl said. "Corporate profit margins are the widest they've ever been. Companies are sitting on a pile of cash that is ready to be utilized. We have seen housing show signs of life, and real incomes have picked up because inflation has been modest."

He added: "The groundwork has been laid to get the economy going. The only thing missing is confidence." Read more: Economic Forecaster of the Month expects 'mediocre growth.'

That's an understatement. The global economy is being "held hostage" by some widely telegraphed uncertainties, Baumohl said. These include the threatened "fiscal cliff" of U.S. spending cuts and tax increases, November's U.S. presidential election, slowing demand from China, and the potential for military conflict in the Middle East.

Faced with such wild cards, he said, companies are reluctant to hire more workers even if they have a need.

And while he understands these worries are rooted in the current reality, Baumohl isn't basing investment strategies on them.

Instead, he said, investors ought to be looking past the gloomy unemployment figures and uninspired growth statistics.

The U.S. elections on Nov. 6. will be a turning point, no matter who wins, Baumohl said. "The decision-making process on capital spending and hiring will improve," he said, "and with that the economy too."

Bernard Baumohl.

So for all of you perched on the edge of the fiscal cliff, it's safe to come down, Baumohl claimed.

"We do not believe there is going to be a fiscal-cliff fall," he said. "It's not going to happen. The reason is that when push comes to shove — as we get closer to the end of the year — no politician wants to have blood on their hands for triggering another recession in the economy because they couldn't agree."

Congressional cooperation, if only to avoid the fiscal cliff, would nonetheless give the financial community a sense that Washington is addressing the budget deficit, Baumohl said.

"That perception," he said, "is going to lead to an improvement among consumers and businesses and set the stage for a more bullish stock market and possibly a more bearish fixed-income market." Read more: Fiscal-cliff tax hike won't kill dividend income.

Baumohl conceded that his optimism might raise a few eyebrows. "What are you talking about? We're having a serious global downturn" is a reasonable rejoinder, he said.

But, Baumohl added: "You've got to be forward-thinking. That means one has to move in early to be able to take advantage of the inflection points in the global markets. Anytime between now and the end of this year would be a good time to consider these investments."

1. Have confidence in commodities

Stronger global demand would give commodities a tailwind. Producers of industrial commodities such as aluminum and platinum are set to benefit in such an environment, Baumohl said.

One key sign of improvement, he said, would be an increase in temporary hiring and a pickup in the Cass Freight Index, which measures North American shipping volume and expenditures. Focus on weekly Federal Reserve, consumer and business data "to have your pulse on the most sensitive economic indicators," Baumohl said.

Such forward-looking measures are not suggesting a turn in the economy yet, Baumohl acknowledged.

"This is where the real challenge comes," he said. "The fact that you get these lousy numbers now is not indicative of what's going to happen in the coming weeks and months. The best that can be said is that the groundwork has been laid for the economy to turn around. What will finally do it will be a change in the confidence that the politics here in the United States and in Europe have finally moved progressively forward to deal with the problem."

2. Count on commodity-rich countries

If you're bullish on commodities, then the equity markets of commodity-producing countries also have a place in your portfolio, Baumohl said.

"Brazil is one of our favorites. It's amazing what the Brazilian government has done to beef up its economy," he said.

Added Baumohl: "The expectation is that with the global economy picking up speed next year, so will Brazilian exporters and in general the Bovespa (SAO:BR:BVSP) will bounce back."

Those same factors also favor equities in Australia and Canada, he said.

3. Gold has a Midas touch

Gold, said Baumohl, is a good insurance policy for any investment portfolio. A smattering of gold is an inflation hedge and offers a cushion against geopolitical risk, he said. Read more: Gold to hit $1,900 by early 2013, says Commerzbank.

Underlying Baumohl's gold call is a concern that an attack on Iran's nuclear program could cause oil prices to soar and halt the economic recovery.

“If we see oil prices remain above $150 [per barrel] for two or three months, that would be deleterious to the U.S. economy,” he said.

4. Support stocks; beware bonds

“Equities are going to look much better than bonds; Treasurys (ICAPSD:10_YEAR) may be extremely risky,” Baumohl said.

Stocks have been doing quite well for more than three years, in fact, and the S&P 500 index (SNC:SPX) is up more than 15% so far this year, including reinvested dividends.

But the advance comes on extremely light volume, and investors are locked into the perceived safety of cash and bonds. That defensive position could work against them as the economy improves, Baumohl said.

“Now we’re going to finally see reality set in so that equities will better reflect growing confidence and accelerated growth,” he said.

“Those holding on to Treasurys may be on the losing side. If you hold on to Treasurys at the end of the year, you have to be very careful. The time may be to sell or to sell short, as the economy shows more signs of vigor,” Baumohl said.

5. Watch Mario, not Ben

European Central Bank efforts to save the euro zone and the common currency (ICAPC:EURUSD) are coming to a head.

ECB President Mario Draghi’s plan to purchase shorter-term debt of peripheral euro-zone nations via the European Stability Mechanism faces a test on Wednesday, when Germany’s high court is expected to rule on the country’s participation in the ESM rescue fund. Read more: Germany's top court to decide euro-zone bailout fund's fate.

Baumohl said he believes the ECB has developed a stiffer backbone and that Draghi will prevail against opposition to the bond-buying from German Bundesbank President Jens Weidmann.

“If the European Central Bank finally pushes back against the Bundesbank,” Baumohl said, “we will begin to see some daylight.” Read more: Euro optimism won't last for long.

Coincidentally, Federal Reserve governors are gathering this week for a scheduled meeting, with many observers convinced that the central bank will inject another dose of fiscal stimulus into the U.S. economy.

But Baumohl suggested that developments in the euro zone hold greater sway over the global economy, including the U.S., than actions of the Fed and Chairman Ben Bernanke.

Said Baumohl: “Watch Mario, not Ben.”