On September 7th we were one of three investment professionals interviewed on Seeking Alpha's Marketplace about the markets, the Federal Reserve and other topical issues. Please enjoy our contribution to the conversation.

Summary

The Fed's annual Jackson Hole Symposium is over; what should investors look out for now? For the near term, interest rates will continue their steady, gradual rise, says Chairman Powell. Our authors agree. The markets' trajectory keeps going up - when will it fall, and what will be the catalyst? Look for opportunities in high yield and China.

With the Federal Reserve's 2018 Jackson Hole Economic Symposium now over, markets continuing to hit new highs, and the economy seemingly humming on all cylinders (lots of people are employed, corporate profits are strong, and the Q2 gross national product was just north of 4%), we thought it would be a good time to check in with some of our macro-minded experts on Marketplace to get their take on interest rates, inflation, and where the economy might be headed next (just how close are we to a recession, anyway?). The authors we spoke to agree that rates will continue to rise gradually and steadily in the near term; that inflation risk, while small at this point, would be problematic for investors; and that, as common sense would dictate, the timing and severity of recessions is tough to pin down. They also propose some timely investing ideas to consider in the current environment, including high-yield instruments and a contrarian play on Chinese stocks. To find out more about how our authors are thinking about the current state of the economy and what investors should be watching for, keep reading.

Seeking Alpha: Federal Reserve Chairman Jerome Powell said at Jackson Hole that he expects rate hikes to continue. Do you foresee the two planned additional hikes coming this year? When do you think the Fed will stop raising interest rates?

Lance Roberts: The Fed under Jerome Powell has been very clear that they intend to keep raising rates at a gradual but steady pace. Real rates remain very low and stimulative relative to the extent of the economic recovery. That should fuel rising levels of inflation, especially given the recent rounds of fiscal stimulus at a time of full employment. The current circumstance offers further incentive for the Fed to maintain the path of rate hikes. Powell likely wants to build room to employ traditional monetary policy stimulus while the economy is giving him the latitude to do so. Ultimately, the stock market is the Fed?s barometer on terminal Fed Funds and will tell Powell when enough is enough.

SA: Why are market expectations different from the Fed?s expectations, according to the Fed?s most recent dot plot?

LR: We recently wrote extensively about this divergence in an article we penned for our Marketplace community: "Everyone Hears The Fed... But Few Listen." One of the key takeaways from the article was as follows: ?Market participants and Fed watchers seem to have been too well-conditioned to the PhD-like jargon of Greenspan, Bernanke, and Yellen and fail to recognize the clear signals the current Chairman is sending.? In short, since the financial crisis, the market has become accustomed to a Fed that has failed to deliver on rate hike promises. That seems to have changed with plain-speaking Chairman Powell.

SA: What?s the deal with inflation? Is the Fed being too complacent about inflation risk and their ability to ?control it? at all costs? What are the odds of inflation upside?

LR: Yes! Yes! And who knows. First, it is important to clarify that rising prices are a symptom of inflation caused by too much money in the economic system. Given the actions of central bankers over the past 10 years, there is no question that condition exists on a global scale as never before. The manifestation has been different in this cycle than in the past and is showing itself in asset prices as opposed to the costs of goods and services. The biggest risk, albeit small at this point, is the combination of inflation and recession (stagflation). In this event, the Fed would be forced to reduce liquidity and raise rates. This is a scenario that has not been witnessed in decades and would be a difficult combination for most stock/bond investors.

SA: There's a chart we saw recently that shows the S&P 500 steadily climbing to dizzying heights over the past decade. At what point do you think the Fed tightening will derail the S&P 500 and the bull market?

LR: Market valuations are clearly at historical peaks. It is being driven largely by behavioral tendencies and importantly central bank liquidity. As the Fed further reduces liquidity and the ECB and BOJ begin to take similar steps, the odds increase that equity markets falter. We are already seeing the effects of reduced liquidity in Turkey and other emerging market nations. That said, picking a date is a fool's game as this market seems to be very good at ignoring reality.

SA: Recession: are we there yet? How close (or far) are we from an economic slump?

LR: We have had some close calls since 2010, especially in late 2015 and early 2016, but central bank intervention has delayed the rhythm of these cycles. In the same way, however, that suppressing forest fires eventually result in even more uncontrollable outbreaks, this seems to be a similar likelihood for the global economy. Debt (and leverage) is the lowest common denominator as a determinant for a recession and, again, the level of interest rates will eventually be the trigger. Rate hikes naturally are bringing us closer to that point, but the trigger is unknowable. Watch real rates, the yield curve, and credit spreads.

SA: The US dollar is key for many asset classes and critical for potential emerging market issues. What?s your outlook for the US dollar both near and long term?

LR: Given the global demand dynamics and the pressures being imposed by a Fed that maintains a path of rate hikes, the dollar should sustain it recent strength and continue to move higher in the short to intermediate term. Long term, the dollar outlook is problematic due to the amount of U.S. debt outstanding, the extent of money printing that will likely have to occur in order to avert a default and the converging global efforts by major economies (especially China) to reduce their reliance on dollar-based transactions.

SA: What would you say to investors who are looking to protect themselves against potential market and inflation risks?

LR: We own house and car insurance for events that are highly unlikely. Why shouldn?t we consider owning financial insurance, especially when the risks of a significant drawdown are substantial? As Falstaff said in Shakespeare?s King Henry the Fourth, ?*Caution is preferable to rash bravery.?*