THE PERSONAL WEALTH COACH®

An SEC Registered Investment Adviser

Jeffrey W McClure CFP® *Jacob A McClure* CIMA®

PO Box 1029 / 918 N. Main Street
Salado, TX 76571

(254) 947-1111
(800) 914-7526

Serving Investors Since 1982

www.tpwc.com

jeff@tpwc.com jake@tpwc.com

April 8, 2016

TPWC Market and Economic Update

The Markets

The S&P 500 closed out last week at 2072 and today ended at about 2048, a loss of about 1.14% for the week. That is still up about 12% from the bottom of 1829 on February 11. The stock market has been bouncing around since about the third week in March, moving a little higher, then a little lower, as hope and worry saw back and forth. A year ago the S&P 500 was at about 2,102, so we are still in negative territory for twelve months as well. In fact, one has to go back three years to see a reasonable return in the markets.

Global stocks dropped about half a percent for the week in dollar terms, despite a decline in the value of the dollar. The benchmark ten-year U.S. Treasury note hit a six-week low on Thursday of 1.685% before, like the stock market, rising a bit on Friday. Oil, too, rose a bit at the end of the week, but U.S. oil futures ended the week at $39.72, below the stock market's apparent comfort zone of around $40.

The Economy

There is little doubt that at least part of the fear part of the stock market equation continues to be generated by what seems to be an endless series of analysis on what would happen if various presidential candidates were to be elected or not elected. Many market participants have worked themselves into an anxious frenzy over the streams of negativity pouring out of campaign headquarters.

Two elements seem to drive market valuations more than anything else at present. One is the price of oil, and the other is interest rates. There is no clear logic as to why those two numbers are so influential, but in a time of confusion and, frankly, false claims and information, traders seem to need to cling to something. When the price of oil rises, so does the market. The same thing happens to interest rates. Historically, a falling price of oil has caused stocks to rise, and rising interest rates have caused stocks to fall. We are in a time when that relationship has been turned on its head.

If there is any logic to the new oil price relationship, it is that falling oil prices suggest a reduced demand, and thereby a slowing economy. That thought pattern is based on a fairly fixed supply of oil and the prices being driven by demand. The reality is that supply is driving the prices today, and that is hard to grasp for people who have been on the other end of that process for decades.

The low to negative interest rate environment we are in is a real indicator of things being not so good. Banks and other financial institutions have historically made their profits from the difference between the interest rate they pay depositors and investors and the interest rate they charge borrowers. Throughout much of the world that interest rate relationship is anywhere from zero to negative. Yes, that means that banks and bond traders are losing money. Some institutions are managing to stay afloat on the fees they charge, but in many cases, they are surviving on old loans or old bonds on which they are earning a higher interest rate than they could get on newer ones. That cannot go on forever, because bonds mature, and loans get paid off. The extremely low interest rates we see around the globe have already gone on longer and dropped far lower than anyone forecast. Sooner or later, the banks will run out of options.

As we enter the earnings-reporting season for the first quarter of 2016, be prepared for some bad news. The market is already reacting to the news before it comes. Financial companies are going to be pretty pessimistic. Heavy equipment manufacturers, too, are going be facing a half empty glass. Anything associated with oil is just going to be in pain.

Information contained herein has been obtained from sources believed to be reliable but is not warranted as to accuracy or completeness. Past performance is no guarantee of future returns. For tax or legal issues consult with a qualified tax advisor or attorney.

There is a good side to this, though. Oil prices are no longer falling. Since companies report earnings in terms relative to where they were before, the next quarter will look better. Interest rates will rise. It is not a matter of if they will rise, it is just a matter of when. Believe it or not, the presidential campaigns will eventually end. Of course, whichever party loses will proclaim the end of the world is at hand, but it won't be.

Remember that only seven or eight years ago the talking heads and the party out of the White House were howling about coming hyperinflation and runaway debt. What we see today is deflation, and we wish we had a little inflation. Deflation is mild in America and a real problem in Europe and Japan, but that is what we face. Yes, our federal deficit was $439 billion in 2015, but that was less than a third of the loss in 2009, and after adjusting for inflation, about what we saw in the Regan administration. The decline in the deficit drop is primarily because we experienced an 11% rise in personal income tax revenues and a 7.2% rise in corporate tax receipts last year. Those higher tax revenues were generated by more people making more money and by greater corporate profits.

The Commerce Department announced its third estimate of 2015's U.S. Gross Domestic Product (GDP) to be $17.947 trillion. While that is good news by itself, it also reveals that last year's deficit was 2.4% of GDP. Here is the clincher: The total growth in our GDP in 2015 was 3.5%. Simply put, if our economy is growing faster than our debt, we are winning. Another factor to take into account is that the Federal Reserve has about $4 trillion in securities on its books that it purchased during the financial crisis. At some point in the not too distant future, it is going to start selling those securities back onto the open market. The profits will go into the Treasury, offsetting trillions of dollars of debt.

We are indeed going through a transition, and it is not comfortable. Equity markets are stuck, and interest rates are, quite literally, the lowest they have ever been. Just as with the financial institutions, those who need to live on the proceeds of investment portfolios need to adjust their expenses or find new income. Still, we are not in or entering a recession or depression. We are recovering. Recovery takes time and it is sometimes painful, but it is a necessary process to reach health and expansion. Sometimes the hardest part is when we thought we were well and then find we aren't quite there yet.

Jeffrey W. McClure CFP®
M.S. Personal Financial Planning

Jacob A. McClure, CIMA®

Information contained herein has been obtained from sources believed to be reliable but is not warranted as to accuracy or completeness. Past performance is no guarantee of future returns. For tax or legal issues consult with a qualified tax advisor or attorney.