THE PERSONAL WEALTH COACH®

An SEC Registered Investment Adviser

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TPWC Market and Economic Update

The Markets

Today the S&P 500 Stock Index closed at 2098.92, up 2.27% for the week, and 14.75% higher than it was on February 11th. It is still down about 1.59% from its all-time high hit in May and July of last year, but another week of this kind of performance would get it into record territory. That would leave the gain over the past several years at still low levels, but would break out of a psychological range that seems to reflect a sentiment that things are bad and getting worse when they actually are good and getting better.

The benchmark Ten-Year Treasury Note yield remained little changed at 1.85%, continuing to reflect the intense international buying pressure for dollar denominated safe investments.

The Economy

As we have remarked in the past, the buying pressure from overseas for U.S. Treasury securities holding down U.S. interest rates is at least partially generated by the weak outlook for both the European and Japanese economies where the interest rates are negative. While there is little evidence of a crisis that will take down either economy, there is ample data suggesting that both economies are unlikely to emerge from a longer-term decline in economic activity. The Eurozone GDP appears to be growing, but at an anemic annual rate of about 0.5%, and the longer-term outlook is not positive.

The French government attempted to pass a measure that would turn some of the employee hiring and firing decisions back to employers, but the economy has ground to a near halt as national unions have blockaded fueling stations and depots and blocked highways with barricades and burning tires. France, like several other southern European nations, faces an unemployment rate stubbornly stuck at or above 10%. Employers, recognizing that it is nearly impossible to lay off or fire a worker once hired, simply have stopped hiring. If the strike and protests continue, the hit to the French economy is likely to bring the Eurozone GDP back to zero in the second quarter.

The U.S. economic recovery continues. That is a strange statement in that most economic indicators are well ahead of where they were before the "great recession" of 2008/2009, but there is a general sense that somehow things never have recovered to the level we last saw in 2007.

Some of that “sense” is likely a result of the extremely negative political rhetoric this year, but at least part of the perception may come from housing. In the years leading up to the financial crisis, new home construction hit all-time highs in each consecutive year. Of course, far too many of those homes were either occupied by people who could not afford them or speculative investors had them built and others traded them, often with "nothing down," as speculative trading properties.

This week, the Census Bureau reported that purchases of new, single-family homes in April rose to a seasonally adjusted 619,000 purchases. That number is 16.6% higher than March, and more importantly, over 23% greater than purchases at this time last year. The median price of those homes also rose to $321,000. While the number of new homes sold is still about 100,000 below the monthly record set back in 2007, the median price set a new record.

As we have written before, the economic effect of building a new home has the highest dollar multiplier of any activity the Bureau of Economic Analysis tracks. A new home built and purchase process generate about $16 in the economy for every dollar spent by the purchaser. Record price levels provide an incentive for builders to build and indicate a robust demand for higher priced housing. All that suggests there will be more buying and more hiring soon.

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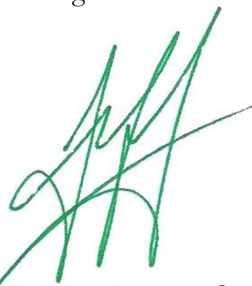
Supporting that report, the National Association of Realtors reported a 5.1% rise in pending home sales. That increase took the index of residential sales to 116.3, the highest since February 2006.

In other economic news, the number of newly unemployed persons applying for jobless benefits fell for the second week in a row. The number of new layoffs remains at about the lowest level in forty years. Durable-goods orders rose 3.4% in April. A surge in new civilian aircraft orders was the primary factor in that statistic, as business investment in new equipment remains weak. Business decision-makers are hesitant to commit to long-term investments or purchases until the Presidential race concludes. They have expressed fear that the economic policies of both Trump and Sanders could result in a dramatically negative financial impact on business profitability.

The price per barrel of oil rose to just under $50, while the price of gasoline and diesel in the United States held steady. There seems to be a general consensus that oil priced at between $50 and $60 is "just right." That level would serve to keep the cost of consumer and commercial fuel down at a level that should stimulate growth while providing sufficient revenue to enable the oil-related companies to pay the banks on their outstanding loans. It would not stimulate another round of drilling and associated equipment investment, but everyone knew that was temporary. The oil patch is a place of boom and bust, but the fear this time was that the bust was going to be more like an implosion.

Last, but certainly not least, the Commerce Department revised the first quarter's GDP growth estimate upwards to 0.8% from the previous 0.5%. While the difference might seem small, the internal numbers are encouraging. Corporate profitability, instead of falling, as the figures previously suggested, rose at a 1.9% rate. The details revealed that the dramatic slowdown in oil-related equipment sales and investment was the leading culprit in the weak growth. Another factor that may be strongly influencing the reported weak growth in the first quarter may be a need to change the seasonal adjustment included in the calculations. For the past three years, the first quarter GDP has come in near or below zero. In each case previously, the reported growth in the second and third quarters was unusually high, balancing out to an annual growth between 2.0% and 2.5% for the year.

We are going to go out on the metaphorical limb here and make a prediction. We believe that 2016 will be, in retrospect, the turning point, during which the economy did better than the market, and after which, the market suddenly became aware that the U.S. economy was actually in far better shape than many investors feared. When that awareness strikes, we believe our analysis that the stock market is about 26% undervalued will prove to be correct. Only time will tell, so keep watching.



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