THE PERSONAL WEALTH COACH®

An SEC Registered Investment Adviser

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TPWC Market and Economic Update

The Markets

Stocks

The S&P 500 Stock Index (SPX) executed an impressive sell-off on Friday, taking the index down, for the week, about 2.39% and ending at 2,127.81. Such dips are normal and expected in any September. The news media generally credited the decline to comments by members of the Federal Reserve Board justifying a potential increase in the interbank lending rate. Of more interest is the uncomfortable reality that the SPX, representing the "stock market", while still up about 16% from mid-September of this year, is now down 0.14% from where it was in May of 2015. It appears that summer has finally arrived on Wall Street.

There is some evidence that at least part of that decline is a result of "short-sellers" selling borrowed stock in advance of the Federal Reserve meeting next week so that they would benefit if the Fed raises rates and the market declines in reaction. The good news is that those borrowed shares must be redeemed at some point, so those same borrowers will need to purchase back their sold stock and thereby raise the value.

For us, a very interesting trend is reflected in the one week rise in the MSCI Emerging Markets Index (MSCI-EM). It was up 4.06% for the week, but more significantly, is up 17% for one year. 16.77% of that rise has been this year. At the same time, the MSCI-EM remains in a low trailing price to earnings ratio of about 11.6. Compare that to the U.S. trailing PE ratio of about 17.6, and the normally high flying emerging markets look pretty conservative. Emerging markets often lead U.S. domestic stocks in that the profitability of a lot of emerging markets companies are dependent on purchases from U.S. companies. Those purchases are in the form of parts to be assembled here, or commonly, goods to be sold here in the near future by U.S. companies. Only time will tell the final outcome, but here we seen another reason that diversification is a good thing.

Bonds

The yield on the U.S. 10-year Treasury Note rose to 1.67% this week, up about 15% from its close last week. The value of a fund that invests almost exclusively in that particular Treasury Security (VGIT), was down about 1% for the week.

In short, this was a week where there was not much place to hide from a decline, albeit a relatively small one. A portfolio with a significant position in emerging markets would have seen a reduced loss, but it would be a foolish move to have more than a moderate percentage of one's portfolio in emerging markets because of their historical volatility. Another way of seeing it was that this is turning into a fairly typical September.

Jeffrey Gundlach, a bond manager with a relatively good record, suggested this week that interest rates may have hit their bottom last month. He warns that bond positions may take a significant hit in the next few years. He also stated that corporate bonds are "in a bubble" as conservative investors have bought them up to the point that any increase in interest rates may launch a selloff. Because the number and depth of "market makers" in bonds has declined sharply in the last several years, the potential is there for some headline and very scary news if such a selloff takes place. If more bonds are placed for sale than the market makers can find willing buyers to purchase them, a relatively sudden collapse in bond prices is a very real threat. If such a thing happens, do not panic. It is not the end of the world, although it would be scary. Such things are not unusual in a market inflection and that particular scenario has historically been followed by a bull market in stocks as investors realize that bonds can be dangerous too!

The Economy

There were no big events in the economic world this week, but articles in various financial publications did raise some interesting points. Several articles this week have unknowingly agreed with us that the lack of business investment is both reducing GDP growth and is a result of election uncertainty. Another article in the *Wall Street Journal* noted that we now have an absolute record for the number of unfilled job openings in the United States. As of the end of July, there were 5.9 million job openings, but the number of hires to fill those jobs was only 5.2 million. There are now about 132 persons for every 100 listed jobs available, down from 665 job seekers for every 100 openings in 2009.

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The primary reason for the difference appears to be skill qualifications. There is a sizeable number of people looking for work, but the jobs available appear to be ones they are not qualified to do. As we reported last week, the jobless rate is directly proportional to the education rate. People with better educations are far more likely to be hired than those with just a high school or lower qualification. This is unlikely to get any better until or unless some program is created to provide those who are without marketable skills some means to become qualified. The traditional low-skilled jobs are not coming back. If a machine can do a job for less cost than a human, it will.

Another factor of some interest, at least to us, is that the "voluntary quits" rate, those who resign, generally to move to another job, is at 2.1%, while layoffs remain around 1%. Voluntary quits is an indicator of the health of the labor market in that it takes a lot of job confidence to quit work to move to a better job. Meanwhile total hires are running at 3.2%, or a bit more than the layoff and voluntary rates combined. Those numbers suggest that employers are hiring more people than they are losing, but doing so in a cautious manner.

Total consumption in the United States rose last month to 0.3% or an annualized rate of about 3.6%. Consumption is about 70% of our GDP, so that is an important number. At the same time, last month, total payroll income rose about 0.4%, suggesting that consumers are not overspending their paychecks. Another good sign is that the consumption seems to be mainly in longer lasting things like digital devices (computers, tablets, phones, and the like), big-screen TVs, furniture, and automobiles. Those types of purchases are generally intended to last for several years, and as most of those are bought on credit with payments, so are the payments. When there is widespread commitment to several years of payments and ownership, it is an indication that the purchasers are confident about their economic security.

We still expect a reaction following the election. What that reaction will be is an open question. If a host of new proposals outside of the existing economic environment appear to have a chance of being enacted, then we could get a correction accompanying a recession. Alternatively, if we get positive leadership and a reduction in uncertainty, investors are likely, in our opinion, to increase equity values even as business owners and managers raise long-term investment in capital items. Meanwhile, we need to have patience. The economy is doing well and looks to have a lot of potential to do better in the near future. It and the stock market are codependent, so the outlook is good.

Until next week, we remain your faithful servants,

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