THE PERSONAL WEALTH COACH®

An SEC Registered Investment Adviser

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May 5, 2017

TPWC Market and Economic Update

The Markets

Today the S&P 500 Stock Index closed at 2,399.28, up 0.63% for the week. As is common, almost all that rise was in the last hours of the day today. It is up 7.17% so far this year and up 16.63% from where it was this time last year. Standard and Poor's is estimating earnings (profits) for its member companies to be up 13.9% in the first quarter. That quarter was a welcome relief as Thomson Reuters estimates that corporate earnings will be up 10% for one year once all the numbers are in.

One of the more pleasant aspects of this market, at least to us, is that the Lipper Mid-Cap Value Fund Index, up 18.36% for one year, is nicely outperforming the S&P 500. Our research consistently shows that the value category has outperformed the market over the long-term, and Mid-Cap Value has been the sweet-spot. It is nice when theory and reality mate up so nicely.

Another area that has done well this last twelve months is Europe. From this time last year, the STOXX Europe 600 is up 18.96% in Euro terms. That is partly offset for US investors as the Euro declined 3.56% against the dollar for the same period. Still, it is becoming more apparent each week that Europe is recovering. Given that one of the reasons for the slow growth we have seen in the U.S. economy and markets over the past several years is that the rest of the world has been lagging, good news for European stocks is good news for us.

Despite rising inflation in the United States and Europe and the international tensions that would be widely believed to make the price of that precious metal rise, gold fell 3.18% this week to close at $1,229.20, and with the last two weeks included, is down almost 5% in less than a month. Again, gold is displaying a marked tendency to move with bonds. The ten-year U.S. Treasury Note, the benchmark for bonds, fell this week as its yield rose to 2.35%.

The Economy

This week's headline economic news was released by the Bureau of Labor Statistics (BLS) today. The U.S. economy added 211,000 jobs last month driving the unemployment rate down to 4.4% from last month's 4.5%. 4.4% is as low as unemployment got in 2007, just before the "great recession" and is close to the 4% rate we last saw in early 2000, just before the tech/dot-com bubble popped that year. With this report came an adjustment to last month's estimate that puts a bit of a damper on any excess exuberance we might have. Last month the BLS reported we only created 89,000 jobs in March, but today it revised that estimate down to 79,000.

The employment numbers reported today reinforce the Federal Reserve's message this week that while they are not raising rates again this month, we should expect to see a couple more increases this year. 4.4% unemployment is very close to what economists refer to as "full employment." Historically, employers start to see fewer applicants than they have jobs at about that level, so they tend then to start raising wages to compete for the scarcity of qualified workers. Further evidence of that problem showed up in the National Federation of Independent Business' report that 30% of its members had one or more critical high-skilled position for which they were unable to find workers. The Fed in its press release stated that it expected growth to rebound after the disappointing 0.7% GDP growth in the first quarter.

With all that good news came another damper. Worker productivity declined at an annualized rate of 0.6% in the first quarter, per the BLS. Notably, the drop was centered in the durable goods area, the same area where there appears to be the most hiring. At the same time unit labor costs rose at a 3% rate. The culprit appears to be weak business investment. Business are profitable, as shown by the record corporate profits being reported for the first quarter, but those businesses are continuing to stockpile cash rather than invest in new plants and equipment. S&P Global Market Intelligence reported that a survey of 219 of the S&P

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500 companies found that spending on things such as equipment and buildings was only up 1.5% in the first quarter, and in many sectors, was *down* for the quarter. The reason behind that reluctance to invest appears to be the same as we have commented on before: *uncertainty*. Business decision makers don't know what their healthcare expenses will be a year from now, nor do they know what taxes they will need to pay. Uncertain, erratic, and sometimes contradictory guidance from Washington has got them spooked. Exporters and importers, which is most of the S&P 500, do not know if there will be an import tax or if trade wars will be started.

Here is the oddity about all that. Rising profits, which have been evident from U.S. listed and based corporations, are a result of rising productivity. If workers at those corporations are turning out less and less production per employee while the cost of employment is rising, we should see companies with falling profits. The answer to that quandary may be outside the U.S. There is at least anecdotal evidence that as businesses are unable to find qualified workers in the U.S. and there is a crack-down on H-1B work visas for highly skilled workers, companies are choosing to create new facilities outside the U.S. That is not to say they are laying off American workers, but that new facilities with higher productivity are not opening here, but rather in other countries.

That is not a bad thing for investors. As we have seen, in the first quarter of 2017 growth in the US Gross Domestic Product was barely above zero, but corporations are reporting record profits, up 13.9%. What is not so obvious is that much of that new profit is coming from overseas facilities.

Things are not all bad, even in the productivity arena. US worker productivity is still up 1.1% from this time last year, and if we get tax reform that supports business investment, we could see a major rebound. What business leaders will need to see to get them to start investing is both tax and trade policies that are business-friendly. The tax outline that came out of the White House neglected to note whether the long-term capital gains rate would still apply or at what rate a business could deduct the cost of new investments, such as buildings and equipment that might raise productivity. If, and this is a big "if," a clear tax reform plan can be drafted that appears likely to pass, we could see a real business investment boom. If that tax plan provides for American companies to return overseas earnings home without facing large scale confiscation, that boom could well be the kick off for an historic bull market.

In short, the stage is set for an historic business expansion in the United States. What is missing are two things. First, well-thought-out leadership guidance and second, skilled workers. The skilled workers are available if employers can bring them here with H-1B visas, but that too depends on Washington. Whether we get the guidance and leadership that would be ideal, American corporations are demonstrating their ability to cope and make profits. With the rest of the world now on the way to economic recovery, American based corporations should profit nicely. The lingering question is whether they will base that growth here or elsewhere.

Until next week, we remain your faithful servants,

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