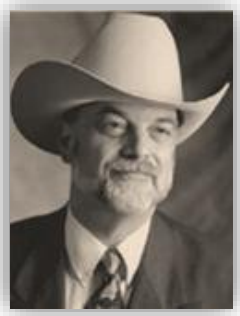

# THE PERSONAL WEALTH COACH®

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## TPWC Market and Economic Update

### The Markets

Traders were glad to see the US stock markets close early this shortened week as the S&P 500 Stock Index (SPX) closed down 3.58% at 2632.56. That close marks a 10.13% decline from its closing high back in late September. The year-to-date loss of 1.54% and even the one-year gain of 1.37% do not greatly subtract from the gloom. The good news is that the SPX is, by our reckoning, now low to fairly-priced and the abundance of pessimism is far more indicative of a market bottom than one that is spoiling for a crash. Our analysis suggests this correction remains just that and is primarily a result of a market correcting for its growth-stock asset-class excesses in preparation for a rotation to value-based, positive balance-sheet stocks.

While there are a host of issues that are proclaimed to be causes of the current malaise, the apparent keys remain a combination of an overstimulated economy that has nowhere to go but down, the rising interest rates that are associated with that economy, and a slowing growth in the world economy at least partially created by the threat of 25% U.S. import tariffs. If the tariff-war threat were to be lifted, there appears to be plenty of room for a market rally.

As would be expected when faced with the specter of a slowing economy, the yield on the ten-year U.S. Treasury note declined for the week to 3.048%, down a relative 14% from its 3.09% yield hit mid-day on Monday. Still, the T-note's yield (interest rate) remains about 32% higher than it was a year ago and bond prices have dropped. The big moves for the week came from West Texas Intermediate crude oil, down almost 12% for the week, and now down about 30% from its October $76.55 high, closing at $50.39. A falloff in demand coupled with high production has oil investors spooked.

Quite notably, the Barclay's US Aggregate Bond Index price return is now down 4.92% for one year, averaging a 0.95% average annual loss for the last three years, as rising interest rates drive down the market price of bonds. Still, the average bond is still priced at 104.67, meaning that it has a built-in loss of about 5% of principal at maturity, and that suggests that the bond market may be still a bit overpriced.

### The Economy

Moody's GDP forecast growth for this quarter is around 2.6%, still above both its long-term trend line and probable sustainability, but a lot lower than the 3.5% to 4% we saw earlier in the year as the tax-cut stimulus kicked in. The Conference Board's Index of Leading Economic Indicators was less positive for October at +0.1, compared with 0.5 and 0.6 for the last two months, but critically it was still positive. A positive number strongly suggests that no recession is likely for the next six months to a year. Quite notably, the coincident and lagging indicators at 0.2 and 0.4 were much higher, explaining the generally good economic numbers that are still coming in. Payroll and job creation numbers are still very upbeat. Moody's Economics is forecasting unemployment to drop to 3.3% in 2019.

The backside data to those positives are beginning to pile up. Housing starts are continuing to sag, and even existing home sales are lagging with building permits falling. More, core capital goods orders, that is purchases of equipment that make more things in the future, has drifted into neutral territory, while factory durable goods orders fell 4.4% in October.

A factor that must be considered in economic growth is infrastructure capacity. In many areas, including the labor market, commodity prices, and transportation capacity, our economy appears to be reaching its limits. More, attempts to grow transportation capacity are themselves constrained by the rising cost and shortage of labor as well as the 40% increase in steel prices since the import tariffs were imposed. Infrastructure projects run off local government fixed budgets and as prices rise municipalities can't adjust what they pay, so they cut projects.

Again, much of the business pessimism is simply an expression of fear about what could be crippling increases in prices on imported goods. The U.S. economy continues to roll along quite well as wages have risen faster than inflation and the tax cut generated increase in take-home income is still in its one-year stimulative phase. For better or worse, the good economic news is concentrated in the lagging indicators as the leading indicators appear to be shifting to neutral. That situation suggests that the economy is being primarily driven by momentum rather than by better future prospects.

Until next week, we remain your faithful servants,

Jeffrey W. McClure CFP®
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