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

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TPWC Market and Economic Update

The Markets

Stock Market

The S&P 500 was up 0.62% this week, closing at 2,175.03. That puts it up almost 19% from mid-February and up just over 2% from its high last year.

If you have much of a memory of what was driving the SPX up and down in the past few months, it was oil. When oil would rise, so would the Index and when oil prices fell, so did the Index. The underlying belief was that if oil prices were down, then the economy was in the pits. This week, the S&P 500 rose even though the price of oil fell 4%. West Texas Intermediate (WTI) closed out the week at $44.56. The stock index rose despite an attempted coup in Turkey, reports of excess reserves of gasoline, and terrorist attacks in France and Germany, all of which would have caused a slump in the Index as recently as a month ago.

This is not a universal phenomena as the Europe 600 Index is down about 12% from last year at this time. The difference appears to be the American consumer. In the final analysis the profits made by corporations have little or nothing do to with manufacturing indexes, productivity, employment, or any of those other statistics analysts fret about from day to day. Profits, and thereby stock values, are driven by the purchases by the end-users for whom corporations create goods and services. It also doesn't make any difference whether the end purchase is of a manufactured item or a service provided. The issue is if the corporation can create those goods and services at a price that will cause the end-purchaser, the consumer, to buy them while at the same time allowing the corporation to be able to make a profit. If they can do that, then their stock earnings rise. If they can't, they fall.

That is exactly what a regulated free enterprise system like ours does best. And, that is why the S&P 500 Stock Index is up when almost all the rest of the world is down.

Bonds

The benchmark ten-year Treasury note had almost no change this week, yielding 1.566%, down from 2.256% at the beginning of the year. Here is another statistic that once meant one thing and today is meaningless. Historically, a 31% decline in the 10-Yr T-Note yield would signal a stock market collapse as it would indicate a failing economy. Today it simply means that the rest of the world believes that U.S. Treasury securities are exactly the place they want to be.

There is a very personal risk here though. Many, and I do mean MANY, investors are "rate-reaching." They consider the stock market risky and safe investments like 5 year CDs yielding 1.21% to be worthless. The false belief that the "insiders" are getting a better deal makes them ripe for a sucker investment when a salesperson or an internet advertisement promising 4% or even as much as 8% gets their attention. High-yield (junk) bonds after all are yielding around 14% per year. The average corporate 30 year bond is yielding 2.28% for shorter-term bonds and 4.10% for maturities over 10 years. There is a very good reason for the higher yield on, for example, longer-term, high-yield bonds. It is because there is a quite real chance that the investor will get back substantially less than he or she paid for that bond. Even the average corporate bond runs the very real risk of some crisis putting the corporate backer of the bond into receivership and thereby stopping the interest payments and resulting in a return of the bond purchase price at a level less than that for which it was purchased.

In short, as one purchases a debt, whether in the form of an annuity, bond, or any other interest bearing instrument, the higher the interest that instrument offers than a similar maturity Treasury, the greater the risk that the purchaser will lose a substantial portion of their investment. Don't be fooled by the term "guaranteed" either. No guarantee is stronger than the guarantor. Unless that guarantor is either the U.S. government or an agency thereof, the risk of loss remains.

The Economy

Existing home sales, which constitute 90% of all U.S. home sales, increased 1.1% in June to put them at 5.57 million, the highest rate since 2007. The difference between sales in 2016 and 2007 is that the sales this year are real sales for homes in which people actually intend to live. Just as importantly, 33% of those homes were by first time home owners. Housing starts rose 4.8% in June and are up 13.2% year to date.

The Federal Reserve Bank of Chicago reported that total economic growth in the U.S. economy was 0.16% higher over the last three months than the long-term historic average. The Conference Board's Index of Leading Economic Indicators, which samples elements of the U.S. economy that historically have been predictive for the next six months, rose 0.3% in June. That rise effectively forecasts an increase in economic activity for the next year at 3.66%. As the prediction is for six months, that amounts to a rise in U.S. economic activity of 1.81% by the end of January, 2016.

There is nothing earth shaking in any of those numbers. What is important about them is that they all indicate slow but steady growth in the American economy over the next six months to a year. Like the violent crime and murder rate in the United States, the facts belie the rhetoric. According to the FBI, as of the end of 2014, the last year for which the data is currently available, the violent crime and murder rate in the U.S. since 1995 had declined by about 50%. During that same 20 year period our GDP has more than doubled. The current figures indicate that not only have we halved violent crime and doubled our economic output, we are on course to continue to do the same over the next twenty years.

Another repeatedly validated statistic is that the number of illegal immigrants in the United States peaked in 2006 and has been declining since. That means that there are actually more unauthorized immigrants leaving the U.S each year than are coming in. In short, things are getting better. Sure there are individuals whose skill set is no longer in demand either because of moving that skill-set requirement overseas, or more often, being replaced by a machine. That is the nature of progress and it is sad but necessary. Not much has changed since John Henry tried to compete with a machine that could drive steel railroad spikes faster, cheaper, and never got hungry or tired. We survived that economic revolution and came out far better for it. We will and are doing the same now.

During this election cycle, don't let the intense and commonly misleading rhetoric distract you from the facts. We are, by any measure, the strongest major economy in the world, and, in real terms, the fastest growing. The negativity of the news is not necessarily a reflection of reality as much as it is a race for profits and power. Bad news is very profitable for any form of the news media and the meat of political candidates. That they are shouting it over and over, does not make it true. In fact, all this negativity is a strong indicator that we are in a long-term bull market for stocks.

As always we welcome your comments in any form, so keep them coming!

Until next week, we remain your faithful servants,

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

Jacob A. McClure, CIMA®