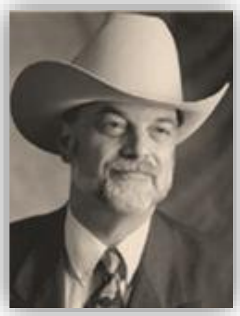

THE PERSONAL WEALTH COACH®

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

Nothing to see here folks. Just move on. The S&P 500 Stock Index (SPX) did about as close to nothing as was possible since last week as it fell 0.01% to 2,183.87 from last week's close of 2,185.05. Oil prices bobbed around, but like stocks, there was nothing new. One has to go back a year to see the real effect of all the bouncing around. The SPX is up about 6.4% from where it was a year ago. It is still only up about 2.4% from a year ago May, and up nearly 20% from its low on February 11. It remains within 1% of its all-time record high.

One interesting aspect of this week's market action was that, for no particular reason that can be discerned, the ten-year U.S. Treasury Note yield rose from last week's 1.51% to 1.58%. That minor move, coming at such a low point in the interest rate environment, caused a decline in the price of newly issued ten-year Treasuries of about 4%. When we have seen that benchmark hit record lows that we believed were about as low as it can get, but then get lower the next week, an actual rise in rates is quite mesmerizing. The interest rate rise was fairly uniform across the yield curve from the two-year out to the 30-year, with the increases growing with the time to maturity, and the prices dropping accordingly. Whether or not that is an indicator of things to come will have to wait for the future, which is always uncertain.

It sure looks like the summer doldrums have finally arrived. Historically in most years stocks start a decline in June, take a hit at the beginning of July and then swoon around September and October. This year stocks rose into August. A good question is, "Why?" Corporate earnings have declined on average for three quarters, productivity is down, and wages are up. That doesn't sound so good for stocks. Read on for more on this.

The Economy

Even as the trailing numbers from the last three quarters are dismal, with the U.S. GDP only growing just above zero, there are forces beneath the surface that may just bode well for the economy and for stocks. Economic activity in the manufacturing sector expanded in July for the fifth consecutive month, while the overall economy grew for the 86th consecutive month. The new manufacturing orders index came in for July at 56.9 and the production index was at 55. Any reading in those indexes above 50 indicates growth. 12 of the 18 industries measured by the Institute for Supply Management (ISM®) reported significant growth. It appears that a combination of the Brexit and oil price collapse had industrial managers worried and fearful that a global recession was in the works, but instead they are mostly reporting rising orders and negotiations for more into the future. U.S. retail sales, as we reported earlier, are rising at a 2.6% annualized rate, but during the first quarter businesses cut inventory. They apparently are beginning to make the orders needed to not only meet sales demand but to bring inventory back up.

The ISM® also reported that as it becomes less likely that Donald Trump will be elected, business owners and managers are becoming more optimistic. Many small and medium-sized businesses rely on China and Mexico for the parts they assemble in manufacturing, and for the whole item in clothing and other sales. A trade war with those two countries would be a disaster for those businesses. As a result, they have been hoarding cash and letting their inventories dwindle.

Still, the improvements are marginal. A fundamental change will need to take place to get things rolling like we saw in the 1990s. The savings binge Americans, both corporate and household, have been on continues. Saving money sound virtuous, but excess savings drive interest rates down, and because the money is neither being spent or loaned out, does nothing to create economic growth.

Another issue confronting us can be seen all up and down the I-35 corridor. Traffic is jammed. Getting goods, services, and perhaps most importantly, the people who want to spend some money from one place to another is being constrained. Here in Salado, a dash up to Temple to get a restaurant meal was once normal, but our anecdotal information suggests that the common stand-still traffic between here and there make folks reluctant to try. Businesses across Salado bemoan the torn up highways, and just hope to hang on until the completion date, but that completion date just got extended indefinitely. One of the biggest problems even when infrastructure upgrade and repair starts has been the budgetary conflicts in Congress. Full funding for the I-35 corridor here in Central Texas would have produced a completion date about five years ago. In the interest of cutting the budget, the funding was spread out over many years, and that is how long it has taken.

This effect is not just here. Across the country, again in the name of budget cutting, deferred maintenance and expansion has been the rule in the many arteries that carry commerce. Just trying to get a product from the manufacturer to the sales floor has become a major challenge.

The good news is that both Presidential candidates have pledged to increase infrastructure spending, and as we reported earlier, both parties have dropped the concept of cutting spending from their platforms. These things take time though. We strongly suspect that the high levels of growth we saw in the past are going to be a while coming. Again the good news is that the consensus appears to be that the "deferred maintenance" era may be behind us. We suspect that the next several years will see some significant changes in the economy. A lot depends on who we elect and whether the log-jam can be broken.

The International Monetary Fund has changed its forecast from a 20% probability of world recession in the next year, issued early this year, to a new estimate that equates to no chance of a global recession over the next year. It is times like this that we get surprises to the upside. Russia appears to have moved tens of thousands of troops and extensive armor and artillery into positions near Poland and Ukraine. As bad as a Russian move on western Europe would be for those on the battlefield, it could unify Europe and get money moving again both here and there. That is the kind of surprise that marks inflection points in markets.

Based on our long experience, we are optimistic. The summer doldrums are on us and everything looks gloomy and doomy. We have seen many summers like this as we have watched the Dow Jones Industrial Average move in fits and starts from 1,000 back in 1982 to today's 18,553. It and the SPX are up over 6% each from last August. This is a slow race, but we believe staying with it is the secret to an eventual win.

Until next week, we remain your faithful servants,

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

Jacob A. McClure, CIMA®