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TPWC Market and Economic Update

The Markets

The good old S&P 500 Stock Index put in a good year. For the week, it declined 1.10% to close at 2,238.83, and on some other week that 1.1% decline would be worrying, but this is the time of year we tally up the calendar. From one of its worst starts in its history the Index rose 9.54%, and that was increased to around 12% with reinvested dividends. Still, while the Dow Jones Industrial Average of 30 stocks and the S&P 500 have similar long-term returns, the Dow won the race this year, rising 13.42%. It was a good year for U.S. Stocks. The year's returns in stocks by size reflected the very long-term norm. The S&P Small Cap 600 rose 24.74% in 2016, while the Mid Cap 400 turned in an 18.73% gain. Despite seeming to be a year of strange events, 2016's stock returns were, for lack of a better word, "normal."

That is not to say that either the mid or small cap gains are likely to be repeated any time soon, but Portfolio Theory is founded on the premise that smaller, publicly traded stocks will, over the long term, rise more than their larger cousins. A second premise is that, again over the long-term, value stocks will outperform growth stocks. That too was reflected in this year's numbers. Small-cap value, mid-cap value, and large-cap value constituted three of the top performing categories at Morningstar this year.

As the year ends, we thought once again to provide the other than calendar returns as measured from recent high and low points in the S&P 500 Index. The Index ended the year up 22.4% from its low in mid-February, but only 5.07% ahead of its high in May of 2015! That just goes to show that "when" can be a critical point in measuring returns. The Index has had a three-year trailing return this year that has ranged from a slight loss to a gain of over 24%. Again, a truth can be seen here. Three years seems like a long time, but in the stock market it is "short-term." Yes, historically stocks have had a much better return than any other liquid or even readily available asset class, but to see that return in a portfolio sometimes takes years of waiting.

The Ten-Year U. S. Treasury Note ended the year yielding 2.45%, slightly below its high yield for the year after declining to 1.344% in early July. For the year, Treasuries were up 0.8% if all interest was reinvested. Gold spot prices peaked at $1,889.7 in 2011, and closed today at $1,152.06 according to goldprice.org. The metal was up 8.5% for the year, but was down over 15% from its 2016 high in July. Oil appears to have stabilized at around $53 per barrel.

(All pricing information and returns taken from the Wall Street Journal Digital Edition or Morningstar.com unless otherwise noted.)

The Economy

We here in the United States seem to alternate between fearing that China will overtake our economy and panicking that the Chinese economy will collapse. The first worry is not one we here at TPWC share, and apparently neither do Chinese billionaires. Chinese investment in the United States tripled to $45.6 billion from 2015 and the Chinese government is reportedly taking extraordinary actions to restrict the outflow of money from China. The decline in the Yuan against the dollar this year appears to have occurred despite strenuous efforts of the Chinese central bank and government to stop the fall.

Wealthy Chinese have found ingenious ways to get money out of China and into the United States as dollars. One Chinese industrialist was reported to have had his Mexican subsidiary buy an extra $2 billion in aluminum ingots from his Chinese parent company as a means of bypassing the $50,000 per year limit in currency transfers allowed by the Chinese government. Others have been reported to have had their American subsidiaries sue their Chinese parent company to be required to transfer funds from China to America.

The bottom line is that China is no super-country. It is not on the way to collapse, but those Chinese who can, would rather have investments and cash in the United States than in China. That strongly suggests to us that the "smart money" is betting on the U.S. to be the better investment for the foreseeable future.

The United States ended the year with an unemployment rate of 4.6%, wage growth, as reported by the Atlanta Fed, at 3.9%, and an accelerating GDP. In 2017 we will face the reality of what new ideas from the White House and a Republican dominated government can do, but when we compare the 10% unemployment, anemic growth, and instability of the similarly-sized European Union to the United States, we look good. We are confident that there are some bumps in the road ahead, but fundamentally, at least in our opinion, we are living in the healthiest economy in the world, and for that we should give thanks.

Until next week, we remain your faithful servants,

Jeffrey W. McClure CFP®
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