# THE PERSONAL WEALTH COACH®


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**TPWC Market and Economic Update**

## The Markets

The S&P 500 Stock Index (SPX) along with the rest of the equity indices proved as February began that they can move downward as well as up. The SPX ended the week down 3.85% to close at 2762.13. The Index remains up over 20% for the last 12 months and is up 3.31% year-to-date and those are still impressive numbers.

Bonds did very much the same thing. You may remember that just over a month ago, the yield on the benchmark 10-year U.S. Treasury note was about 2.4%. It closed out the week yielding 2.838%. In practical terms, the total return of the Bloomberg-Barclays US Aggregate Bond Index has dropped 1.42% in the last month. Considering that its three-year average total annual return was only 1.05%, that is a big hit. Gold, not wanting to be left out, dropped 1.43% to $1,334 with most of that decline hitting on late Friday.

These reversals are linked and appear to be largely driven by a Treasury announcement that it would substantially increase the total value of bonds it would be selling each quarter to cover the revenue reduction associated with the tax cuts that just went into effect. Comments by investors suggested that the realization is hitting home that the government will be needing to borrow a couple of trillion dollars more than was previously anticipated. Higher bond sales (borrowing) tend to drive interest rates up.

You may remember that Bitcoin was trading just short of $20,000 in late December as we predicted a hard fall would come, probably sooner rather than later. On Friday the price dropped to about $7,700 before bouncing back into the $8,000 range. Any way you look at it, the price is now down around 60% in a month.

## The Economy

The Labor Department announced that the U.S. economy created 200,000 net new jobs in January. At the same time average wages clocked in 2.9% higher than they were last January. As might be expected with a lot of new hiring going on, productivity slipped a bit. Core inflation, the way the Federal Reserve views it, came in at about 1.9% per year based on the trailing three months' data, very close to the Fed's 2% target. That leaves the Fed room to continue to raise short term rates this year and continue to liquidate their bond holdings, putting more upward pressure on rates. While we won't likely see it soon, rising rates combined with limits on tax breaks for houses has the potential to reduce future home values.

The drop in the stock market and relatively sudden spike in interest rates had some analysts on edge, but the ECRI Weekly Leading Index, a set of leading economic indicators that warn of impending recessions at least six months before the fact, continued to rise at a 7.3% annualized average rate. In bad news for exporting companies, the dollar rose 6/10 of one percent during the week. It is still down about 7.5% against a basket of world currencies for one year.

One of the mysteries of this expansion has been why wages (and inflation) have not risen more. Some economists are suggesting that the number to look at is not the unemployment rate, but rather the labor-force participation rate. The argument states that there are a lot of people who are not reporting that they are actively looking for work, but would work if the right job with the right conditions came along. If that is true, it would explain why wages are only now beginning to rise as well as the lagging productively numbers. If the supply pool for hiring is larger than we thought and many in that pool would be willing to work for lower wages if the job was convenient and close to home, then employers would not need to offer higher wages. If that is so, then when the pool begins to run low, wages will need to rise as employers compete for scarce workers. Higher wages can lead to higher prices and thereby higher inflation. Higher inflation leads to higher interest rates.

The problem with higher interest rates is that the additional $2 trillion or so the Treasury is planning to borrow to cover the tax cuts may be a lot more expensive than Congress assumed. If so, we may be looking at a real problem with federal debt in about seven years.

Until next week, we remain your faithful servants,

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