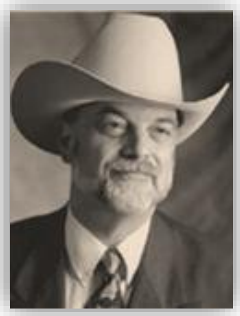

THE PERSONAL WEALTH COACH®

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TPWC Market and Economic Update

The Markets

The S&P 500 Stock Index (SPX) turned in another stellar week, gaining 1.16% to close at 2904.98. While that was not as high as it was at the end of August it did manage to hold above the 2900 level, shrugging off bad news as it remains fixated on corporate earnings and ignoring the threats of trade war damage and slowing retail sales. The 10-Year U.S. Treasury note, the benchmark for bonds, jumped up to close the week at 2.997%. That was a good thing, because the 2-Year Treasury climbed to 2.782%, further flattening the yield curve. The average 30-year mortgage followed suit, rising to 4.68%, up from 3.83% a year ago.

West Texas Intermediate Crude Oil (WTI) rose with the market, ending the week just two cents short of $70 per barrel as concerns about tropical storm Gordon forced offshore rigs to shut down. Gold fell another 0.29% to close at $1,189.30 as the dollar continued to rise against the Chinese Yuan.

The Economy

U.S. retail sales, the biggest driver in the economy, rose 0.1% in August but more significantly, were up 6.6% from last year. The caution in that report was that a 0.4% increase for the month was widely anticipated. Looking under the hood, a big drag was auto sales, which dropped 0.8% for the month. A factor in that decline may be that auto loan interest rates are up a full percentage point from this time last year, effectively increasing the cost by a substantial amount.

Another major driver in the economy, industrial production, was 4.9% higher in August from a year ago, continuing a rise that kicked in back in 2016. In a point of irony that economists often see, the biggest recent gains in factory production were from automobile vehicle and parts production, the same area that slumped last month in retail sales. Expect to see that area shrink in the upcoming months as automobile inventories pile up.

In yet another bit of good news, the Consumer Price Index only rose 0.2% in August but was up 2.7% from a year ago. As average hourly wages rose 2.9%, that means that the average worker in the U.S. saw a real wage increase of 0.2% over the last year. That may not sound like much, but wages have struggled to keep up with inflation for the past several years. Despite the meager rise in real wages, a University of Michigan survey puts consumer confidence the second highest it has been since 2004.

A less obvious effect of those increases is that the Federal Reserve governors seem to be more and more confident that short-term interest rates will need to continue to be increased over the next year. This month there is a near consensus belief that the Fed will raise interest rates another quarter percent and will continue to do so each calendar quarter over the next year. If that is correct, the current 2% short-term rate would grow to 2.5% by the end of the year and be at 3% by this time next year. At that point, either car and mortgage loan rates will be much higher or the yield curve will be approaching the dreaded inversion that generally forecasts a coming recession.

Those rising interest rates are already starting to have an effect as U.S. home loan originations fell to a four-year low in the second quarter, down 16% from the first quarter and 27% from a year ago. The Fed's purpose in raising interest rates is to slow down the economy before it overheats, and it seems to be working.

The U.S. economy continues on a roll, and economists generally agree that much of that is due to increased federal borrowing, spending, and tax cuts. The Treasury Department officially announced that the federal deficit for the first 11 months of fiscal year 2018 was $898 billion, 33% larger than the deficit at this point last year. While that may not be a great thing for the longer term, even the economists at Dismal-Science.com put the chances of a recession in the next twelve months in the low single digits.

Until next week, we remain your faithful servants,

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

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