THE PERSONAL WEALTH COACH®

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TPWC Market and Economic Update

The Markets

The venerable S&P 500 Stock Index (SPX) turned in an anemic 0.02% return for the week ending on 10/19 at 2767.78 but at least the score was not negative! That put it down 5.53% for one month, and down 1.22% for three months. It remains up 2.52% for the year to date and 7.48% from a year ago. If you see lower returns on your statements it may be because the SPX was at 2873 back on January 26, over 100 points higher than this week's closing. On the other side of the ledger, long-term U.S. Treasury Bond Funds are down 3.28% year-to-date according to Lipper. The combination of week stock returns and negative bond returns makes for negative numbers in any balanced portfolio.

Global growth was the big worry this week as investors began to calculate the net effect of the threatened end-of-year full application of tariffs combined with rising interest rates. In what we have described before as the "great economic experiment," the U.S. lowered taxes and increased federal spending, effectively creating a massive fiscal stimulus in the midst of a nearly fully recovered economy. The stimulus has driven consumer spending, employment, and corporate profits to record highs. The overstimulated economy has started to become inflationary, requiring the Federal Reserve to begin to raise interest rates to slow it down. At the same time, the U.S., the largest consumer of products in the world, began to impose tariffs, potentially creating a further slowing effect on global growth rates. Because we are interdependent with the other economies in the world, that global slump has the potential to feedback to us and that is the source of the investor fear being expressed now. The recent slump in market values was most severe in the large, high-growth stocks that have left value stocks in the dust this year.

The ten-year U.S. Treasury benchmark note ended the week yielding 3.193%, up nearly one percent from this time last year. Spot gold prices were at $1,226 down around 8% this year and West Texas Intermediate Crude Oil closed at $69.30 down 3% for the week but still up around 35% for one year. The WSJ Dollar Index rose 0.20% for the week and is up 4.55% year-to-date. More importantly to the evolving trade war between China and the US, the dollar is up 6.56% against the Chinese Yuan year-to-date, making Chinese exports about 7% less expensive in the U.S. and largely negating the 10% tariff on many Chinese imports.

The Economy

Perhaps the most insightful news about the U.S. economy can be gleaned from the earnings report released this week by Procter & Gamble Company (PG). First, the company reported its strongest quarterly sales growth in five years. Very notably that rise in sales came after PG has raised prices across the board. Second, the company report stated that the growth was from increased consumer demand rather than from some introduction or modification of business methods. PG reported that sales declined overseas because of the rising dollar but the about 7% increase in domestic sales were more than enough to offset the losses. Note that PG has been unsuccessfully attempting to encourage more buying by discounting its products in recent years, but this year raised prices and shortly saw a jump in purchases.

That combination of a price increase for the same product and a rush to buy it before the price went up more is a hallmark of inflation and a reversal of recent consumer trends. This change in mindset is why the Fed appears to be focused on continuing the quarter-point rate increases at least well into 2019. It takes six to 18 months for rate increases to historically have demonstrated their impact on the economy. The Federal Reserve Board is well aware of that delay and wants to start the slowing process well before inflation gets out of control.

Home sales continued to slow across the economy, with the average home price up about 4.2% but mortgages up to about 5%. At the same time the Philadelphia Fed reported their October 2018 Manufacturing Business Outlook Survey suggests that manufacturers are optimistic about the future but have seen orders starting to decrease. Another sobering aspect of the report is that about half of the reporting companies in the Philadelphia area report they are operating at above 80% of capacity. That is another indicator that the economy is running at or above full capacity.

New claims for unemployment insurance declined last week to the lowest level since 1973! Near record unemployment also is showing up in the cleanup efforts in the southeast U.S. Recovery companies are reporting that they are running behind normal schedules due to a critical shortage of workers. The U.S. has now run for a couple of years hiring more new workers than our economy is creating. Increasingly it is becoming apparent that the pool of unreported unemployed is running dry. That means that wages will soon be going up as companies compete for the same workers and that is yet another signal that inflation is a threat.

Until next week, we remain your faithful servants,

Jeffrey W. McClure CFP®
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