THE PERSONAL WEALTH COACH®

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June 7, 2019

TPWC Market and Economic Update

The Markets

In a bad-news is good-news week, the S&P 500 Stock Index (SPX) turned in a spectacular showing ending on June 7 with a rise of 4.41% to close at 2873.34. Even with a 4% gain in one week, it still has a long way to go in order to effect a recovery to the 2954 level where it was just over a month ago. The one-year trailing return remains at a tepid 3.39%. That generous weekly gain was credited almost solely to the suggestion by Federal Reserve members that because of the bad employment news they were seriously considering cutting short term interest rates.

The benchmark 10-year U.S. Treasury note closed at 2.085%, well below the 90-day T-bill yield of 2.304% making the yield-curve solidly inverted. The inverted yield curve has now persisted for two weeks and has steepened. The low yields at three and five years were even more pronounced, dropping into the 1.8% range. Even the 30-year bond, commonly immune to short term fluctuations, declined to 2.6% from the over 3% yield it has maintained for several years. West Texas Intermediate Oil (WTI) bucked the trend and rose 1.37% for the week to close at $54.11 but remains down over 12% for one month and nearly 18% from a year ago.

The Economy

The headline economic news this week was that the U.S. economy created a net 75,000 jobs in May after a long run of averaging job creation around 200,000 per month. Accompanying that announcement was the news that wage growth slowed to 3.1% year over year. Neither of those numbers is negative as the economy did create new jobs and wages did grow, year-over-year, but the reduction in the rate of growth of both elements in the labor market was unexpected and relatively dramatic. Unemployment remained at a near-record low of 3.6%.

Other economic news confirmed that things are slowing. At mid-week oil was down over 20% from a year ago, technically signaling a bear market in the black, gooey liquid, but then it rebounded to a mere 18% drop. The Institute for Supply Management's Purchasing Manager's Index (PMI) declined from last month's 56 to just over 50. Readings above 50 indicate growth while readings below 50 signal a contraction. Even in the jobs report a worrisome note was that manufacturing employment has not grown so far this year.

Just as the market responded positively to bad (jobs) news because it improved the chances of a Fed rate cut, there was some good news this week that really was bad news. The U.S. trade deficit declined by about a tenth of a percent. Unfortunately, that decline was relative as both imports and exports fell 2.2% in May. Anecdotal information suggests that the trade slowdown continued into June. Trade creates jobs and a reduction in trade tends to erase them. Economists have been anticipating a slump in hiring resulting from the tariffs and this may be the beginning of that move.

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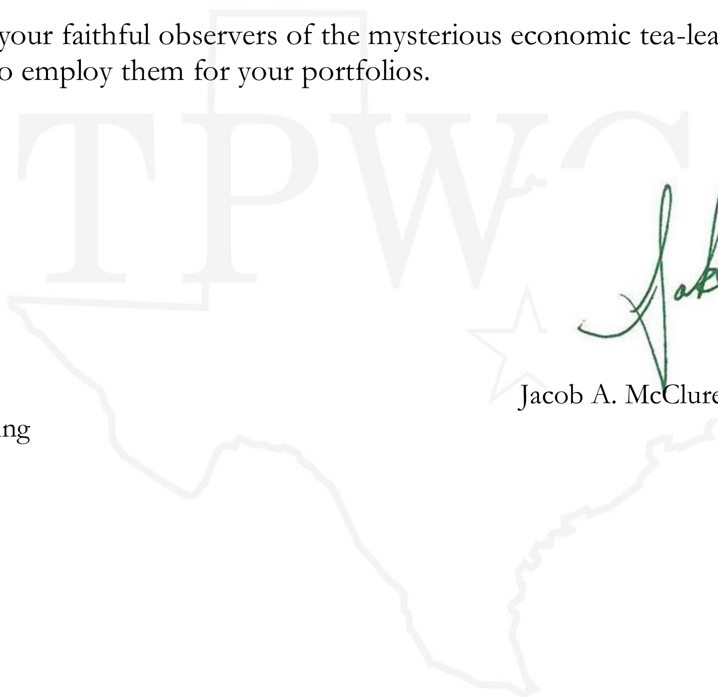
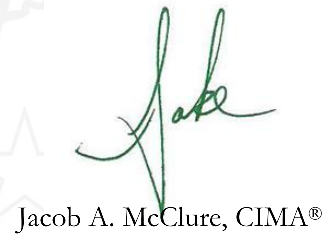
When reading the jobs report tea-leaves, it is good to bear in mind that employment is a lagging indicator. Employers, particularly at large corporations, are slow to start hiring after a recession and slow to start layoffs when things turn south. Hirings and layoffs are both expensive propositions when done on a large scale. In the last two recessions unemployment was at the lowest point in the cycle even as we later determined with 20:20 hindsight that the signs were clearly in place for a slowdown. We aren't at that point yet, but if the yield curve continues to be inverted and the Federal Reserve starts cutting rates, the pattern will start to look very much like the year before the last two downturns. While the overall picture is still slightly positive, very notably ADP reported that small businesses laid off about 50,000 more people than they hired last month. Small businesses tend to lead the way both on the upside and on the downside.

A recession is not likely soon and we will need more than a single month's weak data to sound the alarm, but the expectation of a high-growth 2019 is largely vanishing under the weight of the trade wars and inventory buildup in anticipation of higher tariffs. This month could easily mark the turning of the tide as sentiment changes. There is still room for a relaxation in trade policy to trigger one last leg of this expansion and bull market, but the odds do appear to be growing slim.

Until next week we remain your faithful observers of the mysterious economic tea-leaves as well as seekers of better investment funds and way to employ them for your portfolios.





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