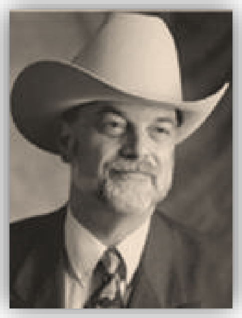

jeff@tpwc.com

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Jeffrey W McClure CFP® | Jacob A McClure CIMA®

PO Box 1029 / 918 N. Main Street
Salado, TX 76571

(254) 947-1111
(800) 914-7526

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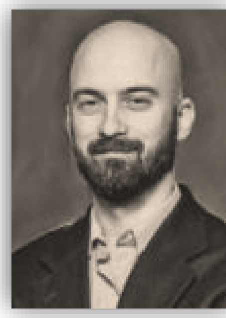

jake@tpwc.com

February 9, 2024

TPWC Market and Economic Update

The Markets

Apparently, we have reached the end of 2024 here in early February. Late last year the most optimistic analysts predicted that by the end of this year the S&P 500 Stock Index (SPX) would reach the unheard of high of 5000. This week ended with our venerable if often misleading SPX closing at 5026.61, a rise of 1.37% for the week, 5.38% this year, and almost 23% higher than where it was a year ago. The rise was credited to the better-than-expected corporate earnings reports that have been pouring in. Our other tracked index, the CRSP US Mid Cap Value Index, only inched up 0.30% to 2491.17. It, like the rest of the market outside a select group of large-cap tech companies, appears to not be joining in the celebration as it plods ahead, emulating the legendary turtle rather than the equally famous hare.

The benchmark 10-year U.S. Treasury note yield crept a bit higher to 4.17%, about 12% higher than it was at the beginning of the year, but substantially lower than it was last October when it touched 5%. The rest of the Treasury yield curve remained about where it has been with the highest rates at the one- and two-month points, above 5.5%, and the 30-year bond at 4.37%. West Texas Intermediate crude oil inched upward to $76.49, higher than at the beginning of the year, but about 4% lower than it was a year ago.

The Economy

The economic news this week was at least as much about what didn't happen as what did. The most forecast recession in memory, or possibility in history, just keeps putting in a "no-show" as the U.S. economy appears to be, if anything, accelerating. Given that our economy is behaving so oddly when compared to the recent decades, it may be wise to step back and look at the causes of what was and what may possibly be coming down the road.

Over the last decade or two we have gotten used to things being a certain way and there was little evidence that things would change. As so often is the truth, now we realize that the steady-state assumption was based on some false assumptions. Inflation stayed stubbornly below 2%, interest rates remained historically low, and an ever-increasing portion of what we purchased here in the United States was made in China in whole or in part. So, what changed? As we discussed in our TPWC Podcast scheduled to be available this weekend, China is the biggest thing that changed. The astonishingly low level of inflation we experienced in the early 21st century was primarily generated by the same forces that produced a similar low-price increase in the 1920s. In that century following the banking crisis of 1908, we saw a large-scale influx of immigrants from Eastern Europe and displaced farm workers willing to work for ultra-low wages combined with the advent of internal combustion engine driven automobile and trucks. The combination of low labor costs, widespread industrialization, and a greatly decreased cost and increased speed of transportation resulted in prices for goods and services falling in real terms, but as our wealth increased, our buying largely kept up with the increasing supply. The end of World War I combined with a global pandemic triggered a supply interruption, triggering a burst of high inflation, which dissipated in a few years. With the rise of authoritarian governments in Eastern Europe, the supply of low-cost labor dried up. What followed was a surge in technology-based productivity gains and soaring wealth in the investment markets, during what came to be known as "The Roaring 20's."

In the late 20th and early 21st century, there was a large-scale movement of low-cost labor from agriculture to factories in China. Part of why that happened when it did was a massive decline in transportation costs as largely automated container ships and ports came online. Additionally, aviation technology advances allowed relatively low-mass goods to be manufactured in Asia and flown to America and Europe for a small fraction of their historical shipping costs. Just as in the previous century, large scale industrialization in a previously low-income area was enabled by the ability to get manufactured goods to where the buyers were at low cost. Following the banking crisis of 2007-2008, just as the world economy appeared to be recovering, first a pandemic swept across the world, then a war broke out in in Europe further depressing economic growth. Once again, supply disruptions created a burst of inflation. Again, too, followed a dramatic reduction in the availability of low-cost labor as the government in China turned to authoritarianism and plans for the conquest of neighboring territory.

If that historical pattern continues, and we more and more suspect it will, then what lies ahead in this decade is an accelerating economy accompanied by slowly rising longer-term interest rates and a repeat of the roaring 20s. Only time will tell. What we can say with some certainty is that the U.S. economy is still charging forward and seems to have no shortage of momentum and fuel to carry it further down the road.

Until next week, we remain your faithful and obedient fiduciary servants.

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

Jacob A. McClure, CIMA®