

MONTHLY ECONOMIC UPDATE



September 2017

MONTHLY QUOTE

"I will love the light for it shows me the way, yet I will endure the darkness for it shows me the stars."

- *Og Mandino*

MONTHLY TIP

Credit card debt is an ongoing financial drain too many people accept. Paying off a credit card with a 12-20% APR is a win akin to getting a 12-20% return on your money.

MONTHLY RIDDLE

It has the scent of green paint, it pours like black paint, and it is the same color as a yellow bus. What is it?

Last month's riddle:

It always arrives consistently, and its appearance makes us nearsighted. What is it?

Last month's answer:

Night.

THE MONTH IN BRIEF

August brought an overwhelming natural disaster, a threat of war from a foreign dictator, and violence in the streets – so it is little wonder stocks went sideways. The S&P 500 eked out an advance of 0.05% for the month. Economically speaking, there were some positives: improvements in consumer confidence and consumer spending, continued strength in manufacturing, and a comeback for retail sales. The economies of the eurozone and the Asia-Pacific region showed more upside. In the commodities market, gold and gasoline grew more valuable, while the price of oil fell. A seller's market seemed firmly in place in residential real estate. Investors hung on through the turbulence.¹

DOMESTIC ECONOMIC HEALTH

Americans spent more this summer and felt optimistic about the state of economy. The evidence? The July gain in personal spending and the lofty reading on the Conference Board's August consumer confidence index. Consumer spending improved 0.3% in July as consumer incomes rose 0.4%. That seemingly had an effect on retail sales, which, in July, had their best month in some time: they advanced 0.6%. The CB index went north to a mark of 122.9, up 2.9 points from its notably high July reading. (The University of Michigan's consumer sentiment index finished August at 96.8, above its final July reading of 93.4, but slightly lower than its preliminary August mark of 97.6.)^{2,3}

Another important index registered an impressive reading in August: the Institute for Supply Management's purchasing manager index for U.S. manufacturing. Already at 56.3 in July, it improved to 58.8 last month, indicating strong expansion for the factory sector. At the start of August, ISM's non-manufacturing sector PMI bore a July reading of 53.9, 3.5 points lower than its June mark; that was still well over the 50-level, delineating growth from contraction.^{2,4}

August also brought news that the economy had grown 3.0% in the second quarter. That word came from the Bureau of Economic Analysis, which revised its first estimate of Q2 growth up from 2.6%.²

The Department of Labor's latest jobs report found payrolls expanding by just 156,000 new positions in August; June and July gains were respectively revised downward to 210,000 and 189,000. Yearly wage growth stayed at 2.5%, a remarkably weak number given the country's 4.4% unemployment rate. The U-6 rate measuring "total" unemployment remained at 8.6%. (Before the Great Recession, it was as low as 8.0%; that difference may indicate the nation is not yet at full employment.)⁵

While the Federal Reserve would like yearly inflation to reach 2.0% as it tightens monetary policy, it is not yet getting its wish. Neither the Consumer Price Index or the Producer Price Index displayed a 2.0% annualized reading in July. The PPI came close at 1.9%; the CPI was at 1.7%. Core consumer inflation was also at 1.7%. Producer prices actually retreated 0.1% in July.³

Regarding the economic impact of Hurricane Harvey, Moody's Analytics projects the toll will be between \$40-\$50 billion, with property damage representing more than 80% of that cost. This staggering amount would still be far less than the \$130 billion in financial damage from Hurricane Katrina in 2005.⁶

GLOBAL ECONOMIC HEALTH

The euro is having a great year. At the end of August, the currency had gained 14% on the dollar YTD. Its performance is not dissuading stock investors: so far, this year, €20 billion of the €60 billion that left European equities in the past two years has flowed back in, and as CNBC notes, European corporations saw profits rise 25% in the first quarter alone. Eurostat, the European Union's statistics office, recorded a 0.5% GDP advance for the eurozone in Q1 and 0.6% growth for Q2. UBS economists now think the euro area will achieve 2% GDP this year and 1.6% next year – an improvement over their previous projection.⁷

Reports revealed that the economies of four Asian nations had a superb second quarter. Malaysia's yearly GDP reached 5.8%; Thailand's, 3.7%. GDP surpassed 6% in both the Philippines and Vietnam. The major reason for such robust expansion: a surge in exports. Good news came from China as well: in August, its official factory PMI increased 0.3 points to 51.7, topping Bloomberg's forecast of 51.3. The country's official service sector PMI declined 1.1 points, but still looked healthy at 53.4.^{8,9}

WORLD MARKETS

Looking around the world, three stock benchmarks had a great August – Brazil's Bovespa, Argentina's Merval, and Russia's Micex. The Merval rose 9.30%; the Bovespa, 7.46%. The Micex was Europe's top gainer, adding 5.35%. Both the Shanghai Composite and Hang Seng also performed well – the premier P.R.C. index advanced 2.68%, while Hong Kong's benchmark improved 2.37%. MSCI's Emerging Markets Index rose 2.01% for the month. Smaller gains were registered by the United Kingdom's FTSE 100 (0.80%), Canada's TSX Composite (0.45%), and Mexico's Bolsa (0.39%).^{10,11}

August did see some losses. India's Sensex took one of the harder falls, slipping 2.41%. Spain's IBEX 35 was not far behind, down 1.93%. India's narrower index, the Nifty 50, retreated 1.58%; Japan's Nikkei 225 lost 1.70%. The FTSE Eurofirst 300 lost 1.03%, and Germany's DAX declined 0.52%. Two tiny losses were taken by France's CAC 40 (0.16%) and the MSCI World index (0.07%).^{10,11}

COMMODITIES MARKETS

Cotton and unleaded gasoline outdid the other major commodities last month. Prices of both futures surged late in August: the former commodity rose 19.63% for the month; the latter, 12.12%.¹²

All in all, it was a rather good month for metals. Gold gained 2.98% to an August 31 COMEX settlement of \$1,326.20. Silver rose 3.64% to close at \$17.56 on the same day. Copper advanced 6.00%; platinum, 5.95%. As for the greenback, the U.S. Dollar Index retreated 0.37%. Ag commodities had it tough: cotton aside, wheat dropped 13.91%; corn, 11.19%; sugar, 6.71%; coffee, 8.27%; cocoa, 5.85%; soybeans, 5.69%. WTI crude was the loser among energy futures, sinking 8.37% on the NYMEX to a settlement of \$47.05 on August 31. Heating oil advanced 0.84%, and natural gas gained 4.73%.^{1,12}

REAL ESTATE

An imbalance between supply and demand kept home buying in check in August. The National Association of Realtors stated that existing home sales fell for a second straight month in July, slipping 1.3% to the lowest annualized rate of 2017. The cause can be traced to two year-over-year developments: a 9.0% reduction in the supply of homes on the market paired with a 6.2% rise for the median sale price (\$258,300 in July). One positive: home sales were still 2.1% improved for the year ending in July. After a 1.9% advance in June, new home buying declined 9.4% in July according to a Census Bureau report.^{3,13}

Between July 27 and August 31, the average interest rate on a conventional mortgage dropped a tenth of a point to 3.82%. That factoid comes from Freddie Mac, which also found average interest rates descending on the 15-year FRM (3.20% to 3.12%) and the 5/1-year ARM (3.18% to 3.14%) across that time frame.¹⁴

Rounding up other key real estate indicators, the NAR's pending home sales index was down 1.3% for July; the 20-city S&P/Case-Shiller home price index displayed a 5.8% annual advance, rising 0.1% in its June edition. As for construction activity, the Census Bureau reported a 4.8% dip for housing starts and a 4.1% fall for building permits during July.^{2,3}

LOOKING BACK...LOOKING FORWARD

While the S&P 500 had to rally on the last day of the month to post its 0.05% August gain, the two other major stock benchmarks fared better. The Nasdaq Composite rose 1.27% in August; the Dow Jones Industrial Average, 0.26%. As for the Russell 2000, it fell 1.39%. The CBOE VIX was up 3.22% for August. At the closing bell on August 31, here was where they all stood: DJIA, 21,948.10; S&P, 2,471.65; COMP, 6,428.66; RUT, 1,405.28; VIX, 10.59. Across the 52 weeks ending August 31, the PHLX Semiconductor Sector Index returned 39.05%, far outpacing other equity indices and market sectors.¹

| % CHANGE | Y-T-D | 1-YR CHG | 5-YR AVG | 10-YR AVG |
|------------|-----------|----------|-----------|------------|
| DJIA | +11.06 | +19.28 | +13.53 | +6.43 |
| NASDAQ | +19.42 | +23.31 | +21.92 | +14.76 |
| S&P 500 | +10.40 | +13.85 | +15.14 | +6.77 |
| REAL YIELD | 8/31 RATE | 1 YR AGO | 5 YRS AGO | 10 YRS AGO |
| 10 YR TIPS | 0.36% | 0.11% | -0.68% | 2.34% |

Sources: barchart.com, bigcharts.com, treasury.gov – 8/31/17^{1,15,16,17}
Indices are unmanaged, do not incur fees or expenses, and cannot be invested into directly. These returns do not include dividends. 10-year TIPS real yield = projected return at maturity given expected inflation.

September might pose some difficulties for the markets. By September 30, Congress must pass a budget or face a federal shutdown; additionally, Treasury Secretary Steven Mnuchin has stated that the U.S. will hit its debt ceiling on September 29. Tensions over these matters in Washington could greatly affect Wall Street. North Korea remains a threat. The Federal Reserve may begin shrinking its \$4.5 trillion bond portfolio before Q3 ends, and the European Central Bank might soon scale back its easing effort. It could be that the bulls will saunter past all this, but there are certainly enough caution flags to make institutional investors think twice this month. Perhaps a retreat can be avoided as the third quarter concludes.¹⁸

UPCOMING ECONOMIC RELEASES: What else will investors watch in September? The key news releases include: July factory orders (9/5), the August ISM service sector PMI and a new Federal Reserve Beige Book (9/6), the August Producer Price Index (9/13), the August Consumer Price Index (9/14), August retail sales, industrial output, and the initial University of Michigan September consumer sentiment index (9/15), August housing starts and building permits (9/19), a Federal Reserve rate decision and August existing home sales (9/20), August new home sales and the latest Conference Board consumer confidence index (9/26), August hard goods orders and pending home sales (9/27), the third estimate of Q2 growth from the Bureau of Economic Analysis (9/28), and then, the August personal spending report, the August PCE price index, and the final September consumer sentiment index from the University of Michigan (9/29).

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The Hang Seng Index is a free float-adjusted market capitalization-weighted stock market index that is the main indicator of the overall market performance in Hong Kong. The MSCI Emerging Markets Index is a float-adjusted market capitalization index consisting of indices in more than 25 emerging economies. The FTSE 100 Index is a share index of the 100 companies listed on the London Stock Exchange with the highest market capitalization. The S&P/TSX Composite Index is an index of the stock (equity) prices of the largest companies on the Toronto Stock Exchange (TSX) as measured by market capitalization. The Mexican Stock Exchange, commonly known as Mexican Bolsa, Mexbol, or BMV, is the only stock exchange in Mexico. The BSE SENSEX (Bombay Stock Exchange Sensitive Index), also-called the BSE 30 (BOMBAY STOCK EXCHANGE) or simply the SENSEX, is a free-float market capitalization-weighted stock market index of 30 well-established and financially sound companies listed on the Bombay Stock Exchange (BSE). The IBEX 35 is the benchmark stock market index of the Bolsa de Madrid, Spain's principal stock exchange. Nikkei 225 (Ticker: ^N225) is a stock market index for the Tokyo Stock Exchange (TSE). The Nikkei average is the most watched index of Asian stocks. The Nifty 50 (NTFE 50) is a well-diversified 50-stock index accounting for 13 sectors of the Indian economy. It is used for a variety of purposes such as benchmarking fund portfolios, index-based derivatives and index funds. The FTSE Eurofirst 300 measures the performance of Europe's largest 300 companies by market capitalization and covers 70% of Europe's market cap. The DAX 30 is a Blue-Chip stock market index consisting of the 30 major German companies trading on the Frankfurt Stock Exchange. The CAC-40 Index is a narrow-based, modified capitalization-weighted index of 40 companies listed on the Paris Bourse. The MSCI World Index is a free-float weighted equity index that includes developed world markets, and does not include emerging markets. The US Dollar Index measures the performance of the U.S. dollar against a basket of six currencies. The PHLX Semiconductor Sector IndexSM (SOXSM) is a modified market capitalization-weighted index composed of companies primarily involved in the design, distribution, manufacture, and sale of semiconductors.

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