

# MONTHLY ECONOMIC UPDATE

July 2017

## MONTHLY QUOTE

“Nobody goes undefeated all the time. If you can pick up after a crushing defeat, and go on to win again, you are going to be a champion someday.”

- Wilma Rudolph

## MONTHLY TIP

If a car accident leads to a talk with your insurer, do not take blame for the crash, even if you think you were at fault. An investigation may reveal otherwise. Saying you were at fault could prompt a premium increase you might not deserve or a smaller settlement than circumstances merit.

## MONTHLY RIDDLE

What can appear white and yellow at the same time, yet not appear to the world most of the time?

## Last month's riddle:

Poke your fingers in my eyes and I will open wide my jaws. Linen, hair, or paper, I can reduce it all. What am I?

## Last month's answer:

A pair of scissors.

## THE MONTH IN BRIEF

June brought some definite headwinds to Wall Street, but the broad stock market still advanced. The S&P 500 added 0.48% across the month, even with tech shares selling off. As anticipated, the Federal Reserve raised the federal funds rate by another quarter point. Last month was a trying one for European stocks as well as oil and many other commodities. The latest round of U.S. economic indicators contained some disappointments; though, manufacturing and home sales surprised to the upside. All in all, increased volatility, terrorist incidents, and political happenings did not have much of an effect on investor confidence.<sup>1</sup>

## DOMESTIC ECONOMIC HEALTH

Hours before the June Federal Reserve policy meeting, traders put the odds of a rate hike at 99%. The central bank did not challenge that expectation. On June 14, it took the benchmark interest rate north to a range of 1.00-1.25%. As it did so, it made one unexpected move: it set a rough start date for unwinding its balance sheet. The Federal Open Market Committee's latest policy statement said that process would begin "this year." Initially, the Fed plans to let \$6 billion in Treasury notes and \$4 billion in mortgage bonds mature each month, with the amounts gradually rising to \$30 billion per month in Treasuries and \$20 billion per month in mortgage-backed securities.<sup>2</sup>

Judging by the latest reading on the Consumer Price Index, the Fed might have to address low inflation again. The annualized inflation rate fell 0.3% in May to 1.9%, beneath the Fed's long-established 2% target. Through May, core consumer prices had only advanced 1.7% in a year. In contrast, producer prices were up 2.4% in 12 months, even with the headline Producer Price Index flat in May.<sup>3</sup>

The Department of Labor's latest employment report also fell short of expectations. The May job gain was merely 138,000. While the headline jobless rate hit a 16-year low of 4.3%, that was partly due to a reduction in the labor force. The U-6 rate (which measures both unemployment and underemployment) fell to 8.4%, a 10-year low. Wages were up a decent 2.5% in 12 months.<sup>4</sup>

The Fed rate move and the latest inflation and jobs data did not upset Main Street. The Conference Board's consumer confidence index, already remarkably high at 117.6 in May, climbed to 118.9 in June. (The University of Michigan's household sentiment index came in at a final June mark of 95.1, down 2.0 points from the end of May, but up 1.6 points from June 2016.)<sup>3,5</sup>

Consumer wages were up 0.4% in May according to the Department of Commerce, yet consumer spending rose just 0.1%. May retail sales figures were troubling – overall retail purchases decreased by 0.3%, while core retail sales (minus gas and autos) were flat. Statistics like these did not exactly signal strong second-quarter growth for the economy. Looking back at the first quarter, the Bureau of Economic Analysis upgraded the Q1 GDP number to 1.4% from its previous 1.2% estimate.<sup>3</sup>

On the factory front, the Institute for Supply Management's manufacturing purchasing manager index rose slightly to 54.9 in May; an index above 50 indicates sector expansion. The Institute's non-manufacturing PMI, which tracks service sector growth, arrived at a mark of 56.9 in May. Federal government reports showed that industrial output was flat in May, while manufacturing output fell 0.4%. Looking to the near future, durable goods orders slipped 1.1% in May with core orders at just 0.1%.<sup>3,6</sup>

## **GLOBAL ECONOMIC HEALTH**

In the Asia-Pacific region, China saw another increase in manufacturing output. Its official purchasing manufacturer index rose half a point to 51.7 in June; economists surveyed by Reuters had forecast a slight retreat to 51.0. The P.R.C.'s official service sector PMI also strengthened 0.4 points to a mark of 54.9. China's government estimated its first-quarter growth at 6.9%, topping a recent Reuters poll estimate of 6.8%. The nation's debt level continued climbing, however – according to a Nomura estimate, it reached 251% of GDP during the first quarter. India was set to institute a new national goods and services tax as part of Prime Minister Narendra Modi's financial reforms; business owners feared a near-term economic slowdown preceding Modi's envisioned boost in government revenues.<sup>7,8</sup>

Commenting on the eurozone economy in late June, European Central Bank President Mario Draghi said “the threat of deflation is gone and reflationary forces are at play,” noting that the region is enjoying “above-trend” expansion. Investors and economists alike took these words as a hint that the ECB would cut back its bond buying this year, perhaps as soon as September; some were worried that the ECB would commit a policy error and make hawkish moves too soon. For the record, euro area inflation ticked down to 1.3% in June per Eurostat's flash estimate.<sup>9,10</sup>

## **WORLD MARKETS**

June was a rocky month for European equities. All of the major European exchanges gave up ground. The hardest fall among them was taken by the IBEX 35. Spain's main index lost 3.98% in June. France's CAC 40 tumbled 3.49%. In London, the FTSE 100 lost 2.84%. The regional FTSE Eurofirst 300 retreated 2.76% as did Russia's Micex; Germany's DAX lost 2.17%.<sup>11</sup>

With its minor June gain, our own S&P 500 also outperformed some other foreign indices. June brought a 1.66% loss for Brazil's Bovespa, a 1.24% decline for Canada's TSX Composite, and an 0.76% retreat for India's Sensex. Some key Asian indices did much better than our broad equity benchmark: Japan's Nikkei 225 advanced 1.81%; Korea's Kospi, 2.05%; Taiwan's TSE 50, 3.35%; China's Shanghai Composite, 2.60%. Other June gains: Hong Kong's Hang Seng, 0.24%; Mexico's Bolsa, 1.18%; Australia's All Ordinaries, 0.14%; MSCI World, 0.25%; MSCI Emerging Markets, 0.54%.<sup>11,12</sup>

## **COMMODITIES MARKETS**

Many commodity prices fell in June. Three key commodity futures advanced for the month – copper gained 4.46%; wheat, a remarkable 18.56%; soybeans, 2.97%. Beyond that, losses prevailed.<sup>13</sup>

Sugar took the largest June descent, dropping 15.27%. Cotton stumbled 8.60%; cocoa, 6.81%; unleaded gasoline, 5.99%. Light sweet crude fell 4.73%; WTI crude ended the month at \$46.33 a barrel on the NYMEX. Silver sank 4.00% to a June 30 close of \$16.57 an ounce. Smaller retreats were taken by coffee (3.06%), platinum (2.57%), gold (2.21%), heating oil (1.80%), the U.S. Dollar Index (1.38%), natural gas (1.27%), and corn (0.40%). When Wall Street's trading day ended June 30, gold was worth \$1,241.40 an ounce.<sup>13,14</sup>

## **REAL ESTATE**

Home sales accelerated again in May. The National Association of Realtors announced a 1.1% gain for resales, partly reversing a 2.5% April retreat. The Census Bureau found new home buying up by 2.9% after a 7.9% dip in the fourth month of the year.<sup>3</sup>

May saw a notable falloff in groundbreaking and permits for new projects, however. Housing starts weakened 5.5%, according to the Census Bureau, with permits down 4.9%. NAR's pending home sales index also declined in May – just 0.8% compared to its 1.7% slip in April. While these real estate indicators fell, house prices, more or less, held up. April's 20-city composite S&P/Case-Shiller home price index (arriving last month) advanced 0.9%, meaning it was up 5.7% on a yearly basis.<sup>3</sup>

The Federal Reserve has gradually lifted the federal funds rate, but mortgage rates are more affected by 10-year Treasury yields – and as 2017 has proceeded, those yields have not dramatically risen. Between Freddie Mac’s June 1 and June 29 Primary Mortgage Market Surveys, popular home loans grew cheaper. Average interest rates on the 30-year FRM fell from 3.94% to 3.88%, and for the 15-year FRM, rates lessened from 3.19% to 3.17%. Only average rates on the 5/1-year ARM increased across June, rising to 3.17% from 3.11%.<sup>15</sup>

### LOOKING BACK...LOOKING FORWARD

The Russell 2000 rallied nicely last month, advancing 3.25% to a June 30 close of 1,415.36. Blue chips also did well – the Dow Jones Industrial Average gained 1.62% in June, more than tripling the 0.48% rise for the S&P 500. The Dow ended June at 21,349.63; the S&P, at 2,423.41. As institutional investors thinned their holdings in the tech sector, the Nasdaq took a monthly loss of 0.93%, finishing June at 6,140.42. Renewed volatility sent the CBOE VIX 7.40% higher across June; it ended the month at 11.18.<sup>16,17,18</sup>

% CHANGE	Y-T-D	1-YR CHG	5-YR AVG	10-YR AVG
DJIA	+8.03	+19.07	+13.15	+5.92
NASDAQ	+14.07	+26.80	+21.84	+13.59
S&P 500	+8.24	+15.46	+15.58	+6.12
REAL YIELD	6/30 RATE	1 YR AGO	5 YRS AGO	10 YRS AGO
10 YR TIPS	0.58%	0.48%	-0.46%	2.65%

Sources: barchart.com, bigcharts.com, treasury.gov – 6/30/17<sup>18,19,20,21</sup>

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.

There was no “June swoon” on Wall Street; how will July unfold? Can the market keep grinding higher and dismiss perceptions that it is overvalued? A strong jobs report and encouraging fundamental indicators could reassure investors worried about economic sluggishness. Distinct recession signals seem wholly absent, and 2017 may simply see a repeat of the economic pattern characteristic of the past few years, in which slow first-quarter expansion gives way to improved Q2 and Q3 growth. During the past 30 years, the market has traditionally underperformed in summer compared to other times of the year – but when stocks have done well in the first half of a year, they have tended to upend those low expectations. With bulls still firmly in charge on the Street, July could bring investors some modest gains.<sup>22</sup>

**UPCOMING ECONOMIC RELEASES:** Across the rest of July, Wall Street will consider these major economic news items: the Department of Labor’s June employment report (7/7), a new Federal Reserve Beige Book (7/12), the June PPI (7/13), July’s preliminary University of Michigan consumer sentiment index, June retail sales and industrial production, and the June CPI (7/14), June housing starts and building permits (7/19), June existing home sales (7/24), July’s Conference Board consumer confidence index and the May S&P/Case-Shiller home price index (7/25), a new Federal Reserve policy statement and June new home sales (7/26), June durable goods orders (7/27), the federal government’s initial estimate of second-quarter economic growth and the University of Michigan’s final July consumer sentiment index (7/28), and then, June pending home sales (7/31). June consumer spending and consumer income data appears at the start of August.

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The Nikkei average is the most watched index of Asian stocks. The Korea Composite Stock Price Index or KOSPI is the major stock market index of South Korea, representing all common stocks traded on the Korea Exchange. The FTSE TWSE Taiwan 50 Index consists of the largest 50 companies by full market value, and is also the first narrow-based index published in Taiwan. The SSE Composite Index is an index of all stocks (A shares and B shares) that are traded at the Shanghai Stock Exchange. 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 Mexican Stock Exchange, commonly known as Mexican Bolsa, Mexbol, or BMV, is the only stock exchange in Mexico. The All Ordinaries (XAO) is considered a total market barometer for the Australian stock market and contains the 500 largest ASX-listed companies by way of market capitalization. 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