



# The News You Need to Know



*Left to right: Andrew Woolley, Andrew Barninger, Christopher Miller, Steven Bell and Alan Loss.*

**We hope that an occasional update on the US and world economies is useful for considering investments in context. Data and statistics may seem dry, but if interpreted properly they can give investors some very valuable and practical insights. We are here to help do that!**



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## Quarterly Economic Update

A review of Q3 2017

### THE QUARTER IN BRIEF

Encouraging economic data and a series of unsettling news headlines vied for Wall Street's attention in the third quarter, and ultimately, investors were not shaken. The S&P 500 rose 3.96% over three months, getting a lift from upbeat manufacturing and consumer confidence readings as well as earnings news. Away from our shores, the economies of China and the euro area showed improvement, and foreign stock benchmarks rallied along with ours. The quarter was filled with major news stories, yet the bulls sauntered through the disruptions.<sup>1</sup>

### DOMESTIC ECONOMIC HEALTH

Consumer confidence barometers were among the most impressive economic indicators last quarter. By August, the Conference Board's index topped 120, far above its origin score of 100; it was at 119.8 in September. The University of Michigan's consumer sentiment gauge ended Q3 exactly where it ended Q2 – at a solid mark of 95.1, rebounding from a July dip to 93.4.<sup>2,3</sup>

Inflation showed definite signs of picking up, or at least, nearing the Federal Reserve's 2.0% target. The Consumer Price Index showed a 12-month advance of 1.7% in July, then 1.9% in August. In both those months, core prices rose 1.7% year-over-year. The Producer Price Index displayed but a 1.9% yearly advance in July, which rose to 2.4% a month later.<sup>2</sup>

With personal wages improving annually at a decent 2.5%, did personal spending increase? Not as much as economists hoped. The gain was 0.3% in July, but merely 0.1% in August.<sup>7,8</sup>

Other data points from Q3 included a minor retreat for manufacturing production (down 0.1% in July and 0.3% in August), a rise and fall for industrial production (up 0.4% for July, down 0.9% just a month later), and a fall and rise in durable goods orders (which sank 6.8% in July but rose 1.7% for August).

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Retail sales were 0.3% higher in July and declined by 0.2% for August.<sup>2,8</sup>

Few investors thought the Federal Reserve would tinker with interest rates in the third quarter, and it did not. It did announce a strategy to cut its \$4.2 trillion balance sheet at its September policy meeting. Beginning in Q4, the Fed will allow \$10 billion in bonds per month to run off, and the pace will accelerate to \$20 billion per month in Q1, \$30 billion per month in Q2, etc., to a monthly goal of \$50 billion.<sup>9</sup>

Cybercrimes were also conspicuous in the quarter. Credit reporting titan Equifax had its databases hacked, leaving the personal information of more than 140 million Americans at risk. Whole Foods and Sonic also suffered major identity theft breaches.<sup>10</sup>

## GLOBAL ECONOMIC HEALTH

News about the European economy was increasingly positive, even as Spain's Catalonia region threatened to secede and Brexit negotiations continued. By August, euro area joblessness had fallen to 9.1%, an 8-year low; unemployment was down to a record-low 5.6% in Germany. Euro area consumer confidence rose to a high unseen since prior to the credit crisis, as the summer ended. In September, the European Central Bank forecast growth of 2.2% for the region, which could lead the ECB to wind down its longstanding bond-buying effort.<sup>11</sup>

Late in the quarter, China's official statistics bureau projected 6.9% GDP for the year; Nomura, JPMorgan Chase, and Citibank upgraded their forecasts for China's 2017 growth to 6.8%. When it came to India, the outlook was far less rosy; as Q3 ended, the Asian Development Bank cut its GDP forecast for India's current fiscal year by 0.4% to 7.0%, and Fitch Ratings slashed theirs by 0.5% to 6.9%. Particularly alarming was news that the Indian manufacturing sector had advanced only 1.2% year-over-year through July.<sup>12,13</sup>

## WORLD MARKETS

As September's final trading day ended, 13-week (quarterly) gains were widespread among foreign benchmarks. The MSCI Emerging Markets index surged 7.02% in Q3.

Quarterly improvements also occurred for the CAC 40 in France, which added 4.08%, and the DAX in Germany, up 4.09%. Canada's TSX Composite rose 2.98%; Japan's Nikkei 225, 1.61%; India's Sensex, 1.45%. The United Kingdom's FTSE 100 gained 0.82%. Australia's All Ordinaries was an exception, putting up a Q3 loss of 1.11%.<sup>15</sup>

## REAL ESTATE

Prospective home buyers looked around and saw fewer homes on the market in the third quarter, along with fewer homes they could actually afford.

Between June 29 and September 28, fixed-rate home loans grew slightly more expensive, according to Freddie Mac's Primary Mortgage Market Survey. On September 28, the

survey showed the following interest rates: 30-year fixed, 3.83%; 15-year fixed, 3.13%; 5/1-year adjustable, 3.20%. The numbers from the June 29 snapshot: 30-year fixed, 3.88%; 15-year fixed, 3.17%; 5/1-year adjustable, 3.17%.<sup>20</sup>

## LOOKING BACK...LOOKING FORWARD

Tech shares and small caps outran the blue chips across summer, but not by much. During a fine quarter for U.S. stocks, the Russell 2000 nearly matched the gain on the Nasdaq, rising 5.33% and taking its YTD advance to 9.85%. On September 29 at the closing bell, the key benchmarks settled as follows: Dow Jones Industrial Average, 22,405.09; S&P 500, 2,519.36; Nasdaq Composite, 6,495.96; Russell 2000, 1,490.86; CBOE VIX, 9.51.<sup>1,21</sup>

% CHANGE	Y-T-D	Q3 CHG	1-YR CHG	10-YR AVG
DJIA	+13.37	+4.94	+23.49	+6.12
NASDAQ	+20.67	+5.79	+23.28	+14.05
S&P 500	+12.53	+3.96	+17.12	+6.50
REAL YIELD	9/29 RATE	1 YR AGO	5 YRS AGO	10 YRS AGO
10 YR TIPS	0.49%	0.02%	-0.77%	2.27%

Sources: wsj.com, bigcharts.com, treasury.gov – 9/29/17<sup>1,21,22,23</sup>

Indices are unmanaged, do not incur fees or expenses, and cannot be invested into directly.

These returns do not include dividends.

Investors think of the fourth quarter as a “sweet spot” for the market, and they can cite history to affirm their belief. Since 1950, the S&P 500 has advanced in 79.1% of fourth quarters. Its average Q4 performance from 1950-2016: +3.9%. Both the Dow and S&P are entering the quarter on 6-month winning streaks, and bulls seem to be okay with the prospect of a Q4 rate hike and the Federal Reserve thinning its bond holdings. Then again, there is no sure thing on Wall Street. As an example, September has long been characterized as a bad month for equities, but that was not the case this year. Confidence is certainly abundant and anticipation is high as a new earnings season begins, and if history repeats itself, 2017 will go into the books as a strong year for U.S. equities.<sup>24</sup>

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