Brendel & Fisher

FINANCIAL ADVISORS

March 6, 2017

Greetings:

Stocks roared to new highs following President Trump's speech on Tuesday continuing their now four-month bull run that has taken the Dow up 14 percent. On CNBC and elsewhere some market "pros" say Election Day had nothing to do with it. A coincidence? No connection? Really? They go even further, insisting that there are reasons stocks should be selling off. Among those are valuations, which by historical measures appear to be a little high. Or are they? More on that in a moment. The inevitable interest-rate boosts are also cited as a reason stocks should sell off. But...

On a few occasions recently I've made the point that it is hardly a certainty that long term interest rates will be steadily rising. Yes, short-term rates will rise, in all likelihood again this month, but long-term rates (the cost of capital, mortgages, present-value computations) are far more important. The 10-year Treasury note is a proxy for long-term rates. Its yield has fallen from more than 2.70 percent a few months ago to 2.47 percent, exactly where it began the year. Our many preferred stocks have been inching higher and yielding less and less. Utilities, which are said to move inversely to interest rates, have strengthened and are close to their all-time high. Most of the bond funds have done very well the past six months. How can this be?

Connecting those and other dots should leave the bond crowd puzzled. The market has a message -- long-term rates won't be rising far and won't be rising fast. Why? For starters, foreigners wanting dollar exposure have been huge bond buyers and that's worked out well for them. Maybe demand for credit will remain tepid, though I suspect not as Dodd-Frank bank limitations are eased. Or economic growth won't accelerate as many (I included) expect. The bottom line is that the market's behavior (rising stock and bond prices) implies, among other things, a low-rate environment well into the future and better days ahead for the economy. I wonder why.

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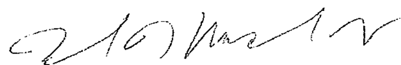
The key uncertainty is the outlook for GDP growth because almost everything keys off of it. GDP growth has historically averaged 3 percent, but it has been less than 2 percent for more than a decade (1.6 percent last year). If words alone could boost it back to 3 percent (never mind 4), we'd be there today. But growth primarily depends on two elements -- productivity and labor. The former has averaged 2 percent growth annually in the past, but recently it's been closer to 1 percent. New technologies (robots, the cloud, etc.) could boost it as smart phones and other innovations did the past decade and before them computers, transportation systems and much more. Still, as we have become more a service economy and less an industrial one, productivity gains are harder to realize and not even so easy to measure. More efficient new plants and equipment will help productivity growth. That's where tax cuts and incentives come in. Bring them on. Labor is easier to measure. As the population ages, more and more Americans retire and automation replaces others, hours worked and the number of people in the full-time workforce will face downward pressures. Immigrants will partially offset this trend. Partially.

Given the above, while GDP growth can accelerate and I expect it will, going from 2 percent (or less) to 3 or more is a stretch. Fine, growing at even 2.5 percent would bring tangible results. Just what impact tax cuts and tax reform will have is impossible to say until details emerge if even then, other than that it must be positive for GDP growth. Tax cuts always are. This month's surge in consumer confidence to a 15-year high shows that people on the street expect better days ahead and know why. So do investors and many CEOs, though of course not the gloomy media. U.S. stocks have added more than $3 trillion in value since Election Day. Coincidence? Some say so. Nothing to see here, they say, move along. Wrong. Credit the game-changing pro-business, pro-investor, pro-growth Trump agenda, just the opposite of the Obama approach and even during the later Bush years.

More soon.



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