Presents:

MONTHLY ECONOMIC UPDATE

August 2015

MONTHLY QUOTE

"Mistakes are part of the dues one pays for a full life."

– *Sophia Loren*

MONTHLY TIP

Buying a new car means buying a rapidly depreciating asset. Buying a quality used car is often the better financial option.

MONTHLY RIDDLE

You can get into it easily if you are not careful, even though it lacks physical form. Getting out of it can be very difficult, even perilous. What is it?

Last month's riddle:
I have a lot of problems, but I have no voice and I never complain, even when I am cracked open. To a student I may cost a princely sum, but not as much as some of the sums written inside me. What am I?

Last month's answer:
A math textbook.

THE MONTH IN BRIEF

The debt crisis in Greece, the stock swoon in China, renewed dollar strength, unimpressive quarterly results from some of the blue chips … there were considerable headwinds on Wall Street in July, and yet the S&P 500 overcame them, rising 1.97% for the month. Other important global benchmarks also advanced, but retreats plagued the emerging markets. Key commodities posted big losses. The housing market remained hot. The latest U.S. economic indicators sent mixed signals, making analysts wonder if the Federal Reserve would refrain from raising short-term interest rates in September.[1]

DOMESTIC ECONOMIC HEALTH

As the quarter ended, the Bureau of Economic Analysis unveiled its initial estimate of second quarter growth: a decent 2.3%, much improved from the first quarter's 0.6% GDP. Durable goods orders had rebounded from a May setback with a 3.4% overall gain in June; while that news was welcome, the Institute for Supply Management's much-watched factory PMI declined from 53.5 to 52.7 in June. ISM's non-manufacturing PMI had risen to 56.0 from a May mark of 55.7.[2,3]

Consumers were less confident in July as news of the debt crisis in Greece and the stock market gyrations in China reached Main Street. The Conference Board's consumer confidence survey fell all the way down to 90.9 from its final 99.8 June mark; the University of Michigan's consumer sentiment index performed better, coming in at 93.3 compared to its final June reading of 96.1.[2]

Was moderate inflation returning? On one level, the answer was no. In June, yearly consumer inflation stood at 0.1%, and that was the first year-over-year advance in the Consumer Price Index recorded since December 2014. On another level, legitimate inflation pressure was evident. The headline CPI advanced for a fifth consecutive month in June, the 0.3% rise coming after a 0.4% advance for May; a 0.2% June gain in core CPI meant core consumer prices (minus food and energy) were up 1.8% year-over-year. Wholesale inflation was also picking up: the Producer Price Index rose 0.4% in June after its 0.5% May gain.[2,4]

June retail sales and personal spending numbers were released by the Commerce Department, and they were disappointing. Consumer spending improved just 0.2% in June compared to 0.7% in May, and consumer purchases fell 0.3% after May's 1.0% rise.[2]

The latest Labor Department report showed no letup in the pace of hiring, with employers adding 223,000 new workers in June. (Monthly job gains averaged 221,000 in the second quarter.) The upside: the headline jobless rate fell to 5.3% while the U-6 rate measuring the underemployed and unemployed declined to 10.5%. The downside: that happened in part because the labor force participation rate dipped to 62.6%, a low unseen since 1977.[5]

Given this mixed bag of late spring and early summer statistics, investors wondered if the Federal Reserve might hold off on a rate hike until late in the year. One factoid arriving in late July was of particular interest: the Labor Department's Employment Cost Index showed only a 0.2% rise in wages and benefits in Q2 compared with the 0.7% advance in Q1. On the other hand, Commerce Department data showed personal wages up 0.4% in June, replicating the gain of May.[2,6]

GLOBAL ECONOMIC HEALTH

The Greek debt drama receded from the front page, only to be replaced by alarm over continuing stock market volatility in China. Greece did effectively default on its July 1 debt payment, weighing on global markets; in a July 5 national vote, the Greek people followed the call of Prime Minister Alexis Tsipras to reject further austerity measures that would come with a third bailout package. No matter: days later, Tsipras accepted them anyway, caving in to his creditors as Greece had no other financially reasonable options. This third, $95 billion bailout came at a steep price: the sale of state assets via a privatization fund as well as higher sales taxes and reduced pension payments. Yet as July wound down, Tsipras was still threatening a "Grexit" unless some of the nation's debt was forgiven, and called on his own Syriza party to vote on whether it wanted to reject the already agreed-upon deal. Greece's blue-chip stock index instantly fell 22.8% when it reopened to begin August.[7,8]

Speaking of stock plunges, the Shanghai Composite (SSE) lost almost 15% in July. Chinese authorities suspended all IPOs as the month started and authorized a 120-billion-yuan market stabilization fund through which brokerages pledged to buy shares. With prices dropping in the Chinese housing market, a bursting stock bubble was the last thing Chinese investors needed. In July, the average SSE-listed stock traded at 27x company profits; in April, Bloomberg reported that Chinese tech stocks were trading at an average of 220x reported profits, surpassing even the 156x average P-E ratio seen for U.S. tech shares in March 2000.[9,10]

WORLD MARKETS

European stocks did very well in July; when Greece agreed to the terms of a third bailout, they got a boost. Monthly gains were as follows: CAC 40, 6.10%; ISEQ, 5.64%; FTSE MIB, 4.80%; IBEX 35, 3.82%; DAX, 3.33%; FTSE 100, 2.69%. The STOXX Europe 600 gained 3.95% and the Europe Dow rose 3.01%. Russia's RTS index failed to join the party, falling 8.63% last month.[1]

As referenced, the Shanghai Composite plunged, falling 14.34%. Three other notable Asian benchmarks also declined last month: the Hang Seng went -6.15%, the Jakarta Composite -2.20% and the Kospi -2.12%. The Asia Dow also gave back 3.38%, but results were better elsewhere in the east. The S&P/ASX 200 advanced 4.40%, the Nikkei 225 1.73%, the Sensex 1.20% and the KSE 100 3.90%. The Dow Jones Americas managed a 1.00% July advance, but other western indices lost ground: IPC All-Share, -0.67%; Bovespa, -4.17%; TSX Composite, -0.58%. The Global Dow rose 1.19% for the month, the MSCI World index 1.73%; the MSCI Emerging Markets index slid 7.26%.[1,11]

COMMODITIES MARKETS

June gains were largely wiped out by July losses in this sector. The U.S. Dollar Index improved notably, advancing 1.86% for the month to 97.44; that put even more pressure on energy futures, ag futures and metals affected by supply gluts and other factors. WTI crude dropped 20.85% on the NYMEX in July, closing out the month at $46.77; natural gas slipped 3.86%, RBOB gasoline 14.87% and heating oil 15.87%. The key crops were red across the board: cotton fell 7.11%, sugar 3.34%, coffee 3.64%, soybeans 7.05%, corn 10.04%, wheat 18.79%, and cocoa 2.23%.[12,13]

Gold and silver respectively ended July at $1,095.00 and $14.76 on the COMEX. Gold futures gave back 6.51% for the month, silver futures 5.87%. Copper futures sank 10.14% last month, platinum futures 9.60%.[13]

REAL ESTATE

How did homes sell in June? Reports issued in July by the Census Bureau and National Association of Realtors showed new home sales tapering off (6.8%) but resales increasing further (3.2%). NAR's pending home sales index tracking housing contract activity slumped 1.8% for June, compared to an 0.6% May gain.[2,14]

The median price of an existing home hit $236,400 in June, up 6.5% in 12 months.

New home prices, on the other hand, retreated 1.8% year-over-year to $281,800 in June. May's S&P/Case-Shiller home price index was up 4.4% over the past year, 0.1% better than the previous edition.[2,14]

As for groundbreaking, housing starts were up 9.8% during June and building permits 7.4%, taking the pace of starts and permits to levels unseen since 2007. Permits for single-family construction reached their hottest pace since the start of 2008.[15]

Back on June 25, Freddie Mac's Primary Mortgage Market Survey, calculated average interest rates on the various types of home loans as follows: 30-year FRM, 4.02%; 15-year FRM, 3.21%; 5/1-year ARM, 2.98%; 1-year ARM, 2.50%. In the July 30 roundup, only the mean rate for the 1-year ARM had increased, to 2.52%. At the end of July, rates averaged 3.98% on the 30-year FRM, 3.17% on the 15-year FRM, and 2.95% for the 5/1-year ARM.[16]

LOOKING BACK…LOOKING FORWARD

When the trading day ended on July 31, the Dow settled at 17,689.86, the Nasdaq at 5,128.28, and the S&P at 2,103.84. To reach those respective settlements, the Dow rose 0.40%, the Nasdaq 2.84%, and the S&P 1.97% for the month. The Russell 2000 did not gain any ground in July (-1.22% to 1,238.68) and neither did the CBOE VIX (-33.52% to 12.12). July saw the Dow Jones Internet index jump 12.86%.[1]

% CHANGE	Y-T-D	1-YR CHG	5-YR AVG	10-YR AVG
DJIA	-0.75	+6.80	+13.80	+6.65
NASDAQ	+8.28	+17.36	+25.49	+13.36
S&P 500	+2.18	+8.97	+18.20	+7.03
REAL YIELD	7/31 RATE	1 YR AGO	5 YRS AGO	10 YRS AGO
10 YR TIPS	0.46%	0.29%	1.14%	1.95%

Sources: wsj.com, bigcharts.com, treasury.gov – 7/31/15[1,17,18]

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.

Will August simply see investors biding time until the Fed does or does not make a move in September? Inertia would please many market-watchers, as the S&P 500 has lost an average of 2.4% during the last five Augusts. (In August 2014, the benchmark rose 3.8% in contrast.) If we get a bunch of strong economic indicators, a recovery for oil prices and some nice earnings surprises, stocks might rally out of the anticipated summer doldrums. If certain economic indicators suggest it is a bad idea to raise interest rates next month, Wall Street also might be encouraged (albeit not quite in the way investors and economists would prefer). While playing defense is pretty common in the eighth month of the year; being patient might be a good tactic as well as fall isn't too far away.[19]

UPCOMING ECONOMIC RELEASES: What will Wall Street scrutinize in August besides earnings? The important stateside economic reports and indicators include June's ISM non-manufacturing PMI and the June ADP employment numbers (8/5), the June Challenger job cuts report (8/6), the Labor Department's July employment report (8/7), June wholesale inventories (8/11), July retail sales and June business inventories (8/13), the preliminary August consumer sentiment index from the University of Michigan, the July PPI and July industrial production (8/14), July housing starts and building permits (8/18), June's CPI and the July Fed policy minutes (8/19), July existing home sales and the Conference Board's July leading indicators (8/20), the June S&P/Case-Shiller home price index, July new home sales and the Conference Board's August consumer confidence index (8/25), July durable goods orders (8/26), July pending home sales and the second estimate of Q2 GDP (8/27), and then the final August University of Michigan consumer sentiment index and the July consumer spending report (8/28).

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