



THE DANA VIEWPOINT

January 14, 2016

Dow: 16,379

Headwinds

What a terrible start to the New Year. The Dow Jones Industrial Average was down 6.2% for the first week of 2016. That is the largest first week drop since 24 stockbrokers signed an agreement creating the New York Stock Exchange in May, 1792 at 68 Wall Street underneath a buttonwood tree. Some market historians like to say “as goes the first week in January, so goes the rest of the year.” However, it’s just a number and the stock market doesn’t know January from June.

You have to love the pundits on the business news channels as they scratch their heads trying to give investors a reason for the market drop. It seems when the stock market drops like the past week, they talk faster and louder. Many are asking how this can happen as the December jobs report was very favorable. Yes it was. The economy created 292,000 new jobs in December and the previous two months numbers were revised upward making the last three months average new jobs creation 284,000. The unemployment number held at 5% and the employee participation rate even ticked up to 62.6%. Investors are not concerned about those numbers this month as they are looking at other issues that may have a greater impact on the stock and bond markets. Some of those issues are as follows:

1) The Middle East - Primarily because of a lack of U.S. leadership, many countries in the Middle East seem to think they can do whatever they want and there will be no consequences. Of course, Russia is muddying the waters by backing Assad in Syria in conjunction with Iran while claiming to be fighting the Islamic State. This is a highly religious and political area and this is not a political letter. However, because of the highly volatile nature of the participants and the proliferation of nuclear weapons, it is a major concern for investors. Now North Korea is saying they tested a hydrogen bomb. Maybe they did and maybe they didn’t. The point is, the world is a dangerous place right now to the point homeland security becomes a major concern with investors. While the outcome here is totally unpredictable, the U.S. is still the safest place to park your money as we are still the world’s largest and healthiest economy and still the world’s strongest military force if push comes to shove.

2) China - This may be the most immediate market challenge. There is no doubt China is overextended and is now left with a high debt to GDP ratio (estimated at about 250%) and a huge residential and commercial building inventory. The good news is that Chinese officials have recognized their problems and held a major three day conference to discuss these issues. According to the Wall Street Journal, China may move away from being manufacturer to the world and focus more on their vast consumer population. Chinese consumers are crying out for better “quality of life” products. They see a huge unmet demand and have decided that what they need to do is carry out supply side reforms. The goal is to transform their economy to be driven more by consumption and less

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by debt and investment. They are willing to take short term pain for long term gain. The plan calls for reducing industrial overcapacity and cutting their stockpile of unsold homes. The plan also calls for lowering costs for businesses. They also plan to cut taxes. Government will become smaller and less intrusive. This plan has been outlined, but is not carved in stone. Let's hope they follow through and the rest of the free world takes note. One advantage China has is that they are not encumbered by a burdensome entitlement program.

3) Black Gold - Who would have thought declining oil prices would be a negative for the market? Lower prices at the gas pump means more cash in the consumers' pockets to be spent elsewhere. It also means lower costs for businesses, especially in the transportation industry, thus higher profits and more job opportunities. Right now, however, investors are looking at declining oil prices and eroding demand as signaling a recession. Oil is a commodity and commodity prices can fluctuate wildly. Investors are also looking at the bankruptcies in the oil patch and the thousands of lost jobs. The major oil firms have vowed to hold their dividend payouts at current levels, but it is a concern for investors seeking income. The price of oil will find its own level, be it \$30 a barrel or lower. Supply and demand is one of the laws of the universe.

There are other headwinds of course – debt, the Fed, entitlement programs and others, but investors are focused more on the aforementioned issues. The bull market has had an incredible run (March 2009 – May 2015), and it is in need of a rest. The decline in stock prices actually began in May of last year when the Dow peaked at 18,300. Recently the Dow has been trading around 16,400. That's a 10% correction; not a bear market, just a correction. There is a Wall Street axiom that says, "never try to catch a falling safe, let it bounce a few times." We will continue to bounce around near term until the market finds a level of good support and stock prices resume an uptrend like they always have. It's a good time to review your portfolio, check the fundamentals, and look for new opportunities.

Random Thought for January 2016: "True genius resides in the capacity for evaluation of uncertain, hazardous, and conflicting information."

Winston Churchill

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