THE DANA VIEWPOINT

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Replace and Refurbish

The stock market has been on a tear lately. Perhaps we should say since the election. There has been much gnashing of teeth by both bulls and bears alike. The bulls are nervous that the market has moved too far too fast and may run out of steam any day, and they should lock in profits before year end. Their decision is complicated by potential tax reform. Will it go through this year, next year, or ever? The bears cannot believe the stock market has climbed this far this fast, and wonder if they should be holding short positions in anticipation of a major sell-off. Short-term stock market moves are really difficult to predict; frequently the market has a tendency of exceeding expectations, and occasionally it truly appears to defy all odds. This has been a good bull market in that it has been rotational in nature. Certain industry groups will advance, while others that have recently advanced will fall back somewhat and consolidate their recent gains. This way we have been able to avoid a bubble in the general market, unlike the blow off in the past stock market of 2007/2008. Even with this orderly advance, the overall market could use a rest, and historically October is a good place for one, possibly setting up a year-end rally.

Two economic indicators that have not said much for years may now be pointing to somewhat stronger growth. The ISM Manufacturing index recently made a recovery high over 60 for the first time in about 13 years, and the service index also touched a new recovery high for the first time in 12 years. They had been flat all these years, consistent with the slow economic recovery we've experienced. The Atlanta Fed recently revised its third quarter GDP (Gross Domestic Product) up to 2.7%. No doubt some of this growth is due to the near-term impacts of Harvey and Irma. Houses need to be replaced, as do mobile homes. Furniture and appliances also need to be replaced. In talking with an appliance dealer, he indicated that their biggest selling item was refrigerators because people drove north from southern Florida and returned home 4-5 days later to find meat and produce rotting in their refrigerators/freezers. They could not get rid of the stench and had to purchase a new one. Auto carriers are everywhere as old flooded vehicles need to be replaced. Then there are grocery stores that may have had generators, but lost meat, produce, and frozen foods, not to mention items that were damaged by water. Pharmacies were another hard-hit business. These and other businesses had to refurbish their inventories. All this adds up to growth in our GDP on a near-term basis. Longer term, reduced wages will result in lost income.

The whine that you may be hearing in various parts of the country is the annual moaning by

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retailers about the poor outlook for holiday sales this year. They may have more to worry about this year, what with Harvey and Irma, but somehow Americans manage to dig deep no matter the circumstances and come up with funds for the gift giving season. Americans will do so again and worry about next year, well, next year.

What's happening at the Federal Reserve? The Fed is so focused on inflation that they are devising new formulas for gauging inflation using unemployment numbers. It is not worked out yet, but they are looking at a projected inflation rate of 2.4%. Stay tuned.

There is an old saying that "if the price is right, the shoe fits." The Fed seems determined to raise short interest rates at least 25 basis points by December. Some members want to raise rates by 50 bps. The San Francisco Fed President thinks short rates should be 2.5% now. With Fed funds currently around 1%, that would require several more rate increases to get there. The Federal Open Market Committee (FOMC), a branch of the Federal Reserve that meets periodically to review overall Fed policy, is also in favor of higher short rates. So the pressure is on the Fed to find a way to justify raising rates more than just 25 bps. The September payroll report was weak, but the household survey was strong (lower unemployment). A rise in interest rates will be beneficial to retired folks living on Social Security and some form of retirement fund, but it will need to be more than 25 bps. The stock market would not be hurt by a small increase in interest rates either. We would need short rates at least at 2% to move some equity money to bonds. And a rise in interest rates would improve profit margins at lending institutions, but would not hurt the mortgage market that much. If people want a house, they will pay the going rate. As far as Fed meetings go, the next two meetings should be quite interesting.

Random Thought for October 2017: "You must have economic freedom before you can have political freedom".

Thomas Paine from his book *Common Sense*, which was one of George Washington's favorite books.

20700 SWENSON DRIVE • SUITE 400 • 53186 • P.O. BOX 1067 • BROOKFIELD, WI • 53008-1067 • 262.782.3631 • FAX 262-782-0581
365 ERICKSEN AVENUE.N.E. • SUITE 312 • SEATTLE, WA • 98110-1888 • 206.855.8781 • FAX 800.560.6227

E-Mail: dia@danainvestment.com
Web Site: www.danainvestment.com