

Economy Report

Reported by :

Mike Lathigee

ECONOMIC ANALYST

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GREETINGS**Bullish Reason to Remain in the Stock Market!****Thursday, September 18th, 2014**

In this month's Economic Outlook Newsletter I will give you both "BULL" and "BEAR" arguments regarding the direction of the economy. I have tried to present different views of some of the topics that are impacting the world's money flow, and as always, I will provide some suggestions for action steps you can consider taking to position yourself for the changes I see ahead.

World Events Drive Investors to a Safe Haven

The recent turmoil caused by the terrorist group ISIS, the fighting in the Ukraine, and the Ebola outbreak have had a positive effect on US stocks and bonds. Investors in Europe and Asia view US investments as a safe haven for investment and are creating a strong demand for the US stock market. The possible deflation in Europe is another key reason these US assets are looking more attractive.

The US stocks look healthier right now than offerings from the rest of the world. After a negative first quarter in GDP, the American economy has bounced back. Recent earnings growth has been decent and the job market is improving. We will see a full scale recovery when the job reports starts to hit 300,000+ on a monthly basis. At that point, the Feds will likely end their easing program and interest rates will move higher.

The US consumer drives two-thirds of the US economy and weak oil prices are good for the consumer, giving them more money to spend. Oil prices fell to the lowest level in 15 months pressured by the prospect of a slowing demand for oil in China and Europe. China's factory sector growth slowed to a three month low last month, which also supported the decline in oil prices. Meanwhile, a strong US dollar and ample oil supplies undermine high US oil prices.

Interest rates are keeping the cost of borrowing very low for consumers. Bond sales are a surprise as investors keep buying bonds and the 10-year Treasury, which hovers at around 2.34%. This is a drop from the 3% rate at the beginning of 2014. Many Wall Street professionals are forecasting no rate hikes until the middle of 2015 – and then only a gentle increase. This would be very bullish for the stock market.

It appears that even when the Federal Reserve stops buying US Treasuries it is likely Europe, Japan and China will continue accumulating US bonds. I see this continuing at least through the end of 2014 and into 2015, which will also help keep US interest rates low.

The interest rate situation and the strengthening GDP and job growth give legs to a bullish outlook on the stock market and US economy. As the market continues to move up almost everyone is calling for this bull market to continue.

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outlook on the stock market and US economy. As the market continues to move up almost everyone is calling for this bull market to continue.

Although these are positive signs, we must balance them with other aspects of the economy. It is important that investors make decisions based on a balanced perception of what is going on.

A Bearish Outlook on the Economy

My main concerns about the bullish optimism we are seeing are around the quality of solid economic fundamentals supporting this market. Or perhaps I should say the lack of solid fundamentals. There are definitely economic numbers that cause concern.

Basically, the US economic recovery is threatened by oil prices remain high, (although prices are in a downward pattern which I discussed earlier they are still high by historical comparison). In addition a weak labor participation rate and a continued regulatory environment that makes it difficult for small business to survive, much less thrive are all reasons for concern about the US economy.

Job Supply and Demand

Although the US economy is creating around 200,000 jobs per month the quality of those jobs is problematic. There are too many people without jobs and the labor participation rate is at its lowest level in decades. That means that when a large num-

number of unemployed people enter the work force, we are going to see downward pressure on wages. In addition, despite the fact the Fed has been injecting cash into the system for five years, wages are not increasing. So we have stagnant wages causing consumers to have less money to spend.

Weak Consumer Spending

In the first quarter the economy actually shrank. As I've stated, the consumer drives two-thirds of the US GDP and consumer spending is still weak.

Quantitative Easing

The five year quantitative easing program whereby the Fed's buy back treasuries to drive interest rates lower and keep liquidity in the system has done little to improve the lives of everyday Americans. These low rates have in fact had the unintended consequence of creating an asset bubble in not only stocks and bonds, but in Real Estate as well.

Home Sales and Real Estate

Although home sales seem stable at this time, there very little discussion about who those buyers are. My concern is that much of this real estate activity originates from investors, speculators, and overseas buyers. The EB5 Visa application program is especially troublesome as it opens the doors to a lot of investment money from questionable sources ready to buy up land at these lower values.

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**Interest Rates and Mortgages**

Even though rates are already at historic lows, US mortgages dropped even further this month – to their lowest level in over a year. But that still wasn't enough to move potential purchasers to buy houses. According to Mortgage Bankers Association total mortgage application volume rose just 0.2% this month over the previous month.

Low Interest Rates Sound Good – Don't They?

As I have said many times in the past low interest rates are fueling corporate buy backs, which forces stock prices up further, but does nothing to help the economy or get Americans back to work.

The Fed's easing program has been great for the wealthy, but it continues to widen the spread between the middle class Have-Nots and top 1% Haves. As the Feds have poured free money into the economy the Federal Reserve has created bubbles in the stocks and real estate markets, benefitting the banks, financial institutions and the top 1% of the population.

According to the Federal Reserve's own numbers in 2013, the top 3% of the population owned 54.4% of all of America's wealth. That is substantially higher from the 44.8% held in 1989.

At the same time, the Middle Class economy has stagnated and in many cases declined. It has also put many people at risk: cheap

money is forcing retirees and others who cannot live off interest rates the banks offer into the stock market. These worried investors are moving into risky assets, such as high risk bonds and equities.

Interest rates cannot stay low forever. In 2008 low rates caused a housing bubble to explode and take the entire system with it. If interest rates remain at zero and asset prices continue to be bid-up without resulting in fundamental economic improvement, then we will see a sequel to 2008 that will be much worse.

The factors that will cause interest rates to go up faster would be strengthening in jobs reports or a higher move in inflation. If inflation moves up fast enough it will cause a major sell off in stocks.

My biggest concern is that these prolonged low interest rates have created a MEGA BUBBLE in real estate and the stock market. The rebound to the negative side will be an extreme correction caused by higher interest rates. I believe that the next financial crisis will be much more severe than the one we felt in 2008.

Almost every investor knows the name George Soros as he is one of the best known investors on the planet. Soros increased his short position on the S&P 500 from 2.96% to 16.65% of his entire portfolio. That is approximately a \$2.2 billion dollar increase in his short position. The interpretation I give to his action is that he believes we are going to see a major correction.

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**US Debt Continues to Grow**

The US debt situation hasn't found much discussion in the news lately, but the Fiscal Cliff we heard about so many times in the past has not gone away. I am very concerned for my children as there is still no effort being made to get control of this debt. America continues to spend more than it takes in revenue.

Neither the President nor Congress will act to curtail spending and balance the budget. Even though their job description demands that they do so! Without some immediate controls America will continue to add trillions of dollars to the debt until creditors will only lend to America at very high interest rates.

At the same time, consumers are urged to spend to spend to shore up the GDP but the problem is we have a much weaker consumer. It is a vicious economic Catch-22 and we must find some way to break the cycle.

Canada Feels the Strong US Dollar

For our Canadian followers, who live in a rich resource based economy, the strong US dollar has been horrible for commodity stocks. We saw gold hit a one-and-one-half month low this past week and crude oil plunged by more than 3%. Broadly speaking, commodities tend to move inversely to the dollar. This makes sense, given that as each dollar becomes worth more, it should take fewer of them to buy the same amount of hard assets. Most commodities are priced in US dollars.

So, What Are My Conclusions?

I believe the stock market will remain strong for the balance of 2014 and into 2015. However, as other economies around the world start improving and demand for US bonds weaken, then we will see an exodus out of stocks and interest rates will move up.

I suggest having almost all of your money out of the stock market by late 2015 and immediately take profits from your stock portfolio.

If interest rates move up too quickly, then we are going to see an economic tsunami greater than the one in 2008. For this reason I suggest a flight to safety by owning some precious metals. In particular buy silver, which is at historic lows in relation to gold.

Normally, silver trades at a ratio of about 10-to-1 of the price of gold. Right now the ratio is closer to 60-to-1. Investing 5% of your entire portfolio into precious metals will act as a hedge if we see extreme events.

Only buy Real Estate for cash flow reasons. If your real estate does not produce positive cash flow, then it is a liability. Buying real estate in anticipation of capital appreciation is not a smart move at this time.

Hold On To What You Have

Your financial advisors are stealing too much money from your 401ks and your IRAs and for Canadians, your RRSPs. The 1% fee they take yearly over a period of decades erodes your gains by an average of 50% over time.

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Annual Club Event

Economic Summit II
Nov 15th-16th, 2014

In addition to paying attention to what you are paying in fees, do your own research on your investments and understand what you are buying. Remember that historical earnings are just that – historical. Past performance of a fund or stock is no guarantee of future performance.

That said, it is in your own best interest to be more independent when managing your money and that means you need to know the big picture. You need to understand that without objective information, you are at the mercy of whoever frightens you the most, whoever tells you what you want to hear and promises you a pain-free, effortless guarantee.

Put another way, I always have told my staff, “If you don’t have a plan of your own you will become part of someone else’s plan”. This sums up 95% of the type of relationship that investors have with their financial advisors.

There is no painless solution to the economic problems we face. I believe the next market correction will end badly for investors who have not prepared and if investors don’t plan they will watch most of their life savings wiped out. But there are prudent moves you can make to help yourself.

I do my best to research a wide range of indicators and data banks to see the global economic picture. I’ve been researching and following the global economy for a long time and I try to stay objective when I make my own investment decisions and when I share what I find. I consider it my calling to dig up the facts and get them out where my readers can see them and make their own decisions.

That’s it for this month. I will continue to follow these topics and add more to the picture next month. Until then, stay calm and take informed actions.

Michael Lathigee
Economic Analyst

P.S. Don’t forget our upcoming Annual Club Event. www.econosummit.com. We have members and speakers flying in from around the world. This year’s focus is a 2 day overview of what is happening in the world and the economy and how it impacts investors on an individual basis and what they can do to profit and in some instances take a defensive position to protect their portfolios.

Some of our attendees are staying a few extra days to enjoy Las Vegas so we have negotiated “positively insane” rates in a world class resort. We are able to get these rates because for 5 years we have done all our events at the Orleans Hotel and Casino Resort and the resort has lent the club support for its event.

November 13: \$38

November 14: \$69

November 15: \$69

November 16: \$32

Mention the following code when you book your room: **A4LVL11**