DELTA FINANCIAL ADVISORS
Investment Counsel

July 2016

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Economic Comments

The Federal Reserve's Open Market committee held off from raising overnight interest rates further at its mid-June meeting due to continued concerns about global growth, coupled with the recent voter approved British exit from the European Union, colloquially called "Brexit." Output growth, hiring, business investment, and corporate profits have stumbled or slowed in recent months, leaving the U.S. central bank unsure when it will raise short term interest rates again. The Fed's tone on the economy has changed notably just in the last few weeks. As recently as May, many officials thought the moment was becoming ripe to increase short term interest rates a second time since their initial upward move in December. In recent comments, Chair Yellen shared that the Fed will raise rates gradually, cautiously, and without a set timetable. Additionally, Fed officials reduced their estimates of how the benchmark Federal Funds overnight interest rate is likely to move in the years ahead. Looking ahead two years, they still see the benchmark rate below 2.5% at year end 2018.

Assessing recent economic performance, final numbers for the 1st quarter's economic growth showed economic activity to have grown by 1.1 percentage points, up 0.6 percentage points from April's initial estimate. Growth in consumer spending for the 1st quarter, which accounts for more than two-thirds of economic activity in the United States, was revised down to a 1.5 percent growth rate, the slowest pace in two years. The downward revision reflected weak spending on services like transportation and recreation. In comparison, the 2nd quarter expectations are that U.S. economic output rebounded. One foreshadowing indicator was April and May retail sales which suggested that consumer spending had rebounded from its 1st quarter slump. Supporting the consumer rebounds were an advance in wages along with continued low energy prices, low interest rates and ongoing job gains.

Despite the diminished expectations for near-term rate increases, Chair Yellen expressed optimism for GDP growth in the 2nd quarter with the Federal Reserve Bank of Atlanta estimating a 2.6% advance. The Fed Chair stated her belief that the likelihood of a U.S recession in 2016 is "quite low." Yet not all economists agree with her assessment as a recent Wall Street Journal poll found that 21% of the economists polled felt that the U.S. would be in recession within a year; this figure was up significantly from the 10% reading from a similar survey conducted last year. Of particular support to 2nd quarter output appears to have been the resurgent housing sector.

Data released in late June showed house prices rose 5.4% in April from a year ago with sales of existing homes rising to their highest level in more than nine years. On a broader perspective, home prices climbed to a new peak in May, the latest sign of rising demand amid steady job creation and low interest rates. The rejuvenated housing market has provided a boost to the economy, helping offset a slowdown in business spending and the continued downturn in the energy sector. Spending on home construction and remodeling grew at the fastest pace in more than three years at the start of 2016, helping support an otherwise anemic quarter.

One area that needs to be

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closely monitored in coming weeks is the bellwether durable goods orders. As June ended, the U.S. Commerce Department reported that new orders for durable goods — airplanes, industrial machinery, and other products that are designed to last at least three years — decreased a seasonally adjusted 2.2% in May from the prior month. This decline was a sharper fall than the 0.4% decline that most analysts had expected. This recent weakness could be exacerbated in the coming months by "Brexit" fueled uncertainty and the renewed strength in the dollar.

Until recently, inflation had been on a modest upswing. Excluding the volatile food and energy components, the Fed's preferred measure of consumer prices was up 1.6% in May. While short of the central bank's 2% inflation target, this rate of price increase was stronger than the 1.3% experienced in the year earlier period. With "Brexit" having caused renewed strength in the greenback, and likely to be another drag on already tepid global growth, import prices will remain depressed thereby reducing near term inflation.

Counter balancing these "Brexit" caused issues, a tightening labor market has begun putting upward pressure on wages. The median hourly wage was up an average of 3.5% in the three months ending in May from year earlier levels - the strongest gain since early 2009. With productivity low, partly because investment in technology has recently been soft, companies' labor costs are rising — some portion of which they will probably pass along to consumers in the form of higher prices. Additionally, the June reading for the Conference Board's consumer confidence survey showed that confidence increased to an eight month high in June. Diminishing this luster, though, was that the survey was conducted before the critical EU referendum in Britain.

As we look forward, the Fed has indicated that it would fight any potential slowdown with renewed purchases of mortgages and Treasury bonds along with promises of continued low rates. The central banker emphasized that there is no intention on the Federal Reserve's part to follow Japan and Europe's recent policies of negative interest rates. On balance, we believe that the U.S. economy will remain on a path towards growth, albeit at a slower rate than typically seen in prior economic recoveries. While the U.S.' growth remains sub-optimal, it is appreciably above the growth seen in other developed economies. Compared to its peers, and to quote Erasmus of Rotterdam, "in the land of the blind, the one-eyed man is king."

Analyst Corner

The precipitous decline in petroleum prices has decimated all areas of the energy sector. Nonetheless, this market segment remains a critical component in a balanced investment portfolio. In recently assessing the sector, one company, Schlumberger Ltd, stood out for its geographically diversified business, more consistent business, and its high quality balance sheet. The world's leading oilfield service company, NYSE traded "SLB." operates in more than 85 countries globally. Although positioned to profit as energy prices stabilize and/or rebound, SLB's business is more stable than most in this recently volatile sector. Even though the energy sector has experienced a steep slide over the last 18 months, we believe SLB to be an attractive addition to many portfolios.

Market Comments

As the 2nd quarter progressed, focus on the pending "Brexit" vote dominated global markets with frequently changing poll data causing both sharp market advances and declines. As the vote approached, market volatility escalated with the market's fear gauge almost doubling from its early June levels. After two days of sharp declines following the pro-exit vote, investors reversed course. At quarter's end, the S&P 500 found itself up modestly for the month of June and up almost 2.5 percentage points for the full 2nd quarter. So far in 2016, the key theme for investors has been a search for bond-like performance amongst stocks. As a result, the sleepy utility and telecom sectors have thrived with the telecom segment leading the market's modest overall advance with gains of almost 25% year to date. Meanwhile, the market laggard has been the financial sector which has struggled in the face of tepid economic growth and modest net interest margins, combined with the new uncertainties of the fallout of Britain's exit vote.

The ongoing tepid global economy and a flight to quality following the Brexit vote, drove the 10-year U.S. Treasury's yields to re-test their record lows of 2012. Standing at 1.49% on June 30th, these interest rates are amongst the lowest seen in modern times – yet they pale in comparison to the negative interest rates now found in much of developed Europe and Japan. Amidst the uncertainty generated by the British vote, government bonds rose sharply globally in June and had their strongest advance since December 2008. A key reason for the drop in yields is that many fixed income investors now believe that global central bankers will be forced to pursue looser monetary policies after the unexpected exit vote. In particular, the Bank of England, the European Central Bank, and the Bank of Japan have indicated their bias to further ease monetary policies while the Federal Reserve has largely put off its plans to raise the overnight Federal Funds rate until the end of this year, at the earliest. In general, the message from global bond markets this quarter has been that inflation is not a threat. Bond market investors came into the second quarter with low expectations for how much inflation there will be in the years to come. Now, if anything, they expect even less of it. Expectations embedded in Treasury inflation-protected securities suggest inflation will average just 1.5% over the next 10 years versus a forecast of 1.62% at the end of the first quarter.

Looking at stocks and stock valuations, as interest rates fall risks tend to rise because a greater proportion of stock returns has to come from capital appreciation. That is likely to make future investing results even more hostage to a continued bull market than investors have recently been accustomed. To stay safe, a more cautious investor could get out of the markets until rates finally rise. But, as Antti Ilmanen of AQR Capital Management recently shared, "contrarian timing is hard to get right and expensiveness can last for quite a long time, and you can end up not just a few months early, but many years early." In the nearer term, for the market to go up there needs to be some sort of positive surprise, such as better than expected economic news or corporate results. Another signal of additional advances could be reduced interest in the more stable market sectors, such as utilities and telecoms, and renewed strength in the recent laggard sectors of finance and technology.

After a seven year bull market, nobody knows with any certainty when we will next have an appreciable market decline or advance. While much angst has been expressed about the impact of Great Britain departing the European Union, nothing about the vote suggests that the fundamental of capitalism has changed. As a result neither should your confidence in very long-term ownership of the pieces of the for-profit enterprises (i.e. shares of stock) that will benefit from your long range perspective. At a minimum, increased market volatility in the near term is a virtual certainty. What we do know is that when the long expected market decline does eventually occur, patient investors will still have the advantage of buying more shares as stock prices move lower. We encourage all investors to come up with a reasonable strategy and to stick with their strategy through both good and bad times.

Performance as of 6/30/16

	Close	Month	YTD	1 Year
DJIA	17,929.99	0.95%	4.31%	4.50%
S & P 500	2098.86	0.26%	3.84%	3.99%
NASDAQ Comp.	4842.67	-2.13%	-3.29%	-2.89%

	Quarter end yield	Prior Year end yield	Yield 1 year ago
10 yr. U.S. Treasury	1.49%	2.27%	2.34%

Planning Thoughts

Maintaining the security of financial and personal data has become increasingly important. In recent years, criminals have increasingly focused their efforts on more lucrative activities such as identity theft, credit card theft and unauthorized bank transfers. In order to minimize these risks, we encourage everyone to maintain current anti-virus software and to frequently change their passwords for their financial accounts.

To help further in this effort, we are pleased to announce that we have recently **implemented a new encrypted secure e-mail system** to enhance the protection of our clients' data. When relaying confidential information of any kind, Delta is now using an AppRiver.com secure mail system. To establish a secure mail account with us, you will initially receive an e-mail whose subject line starts "Secure message from Delta Financial Advisors…." which asks you to establish a secure mail account with AppRiver.com. Once the new account is established, you will be able to send and receive information via secure e-mail with assurance that your confidential data remains protected. If you have any questions about the set-up process, please give us a call so we can walk you through it.

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