DELTA FINANCIAL ADVISORS
Investment Counsel

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Economic Comments

The U.S.' central bankers took the expected move at the mid-June Federal Open Market Committee meeting and raised overnight interest rates by 0.25 percentage points to a targeted 1.0%-1.25% range. In subsequent comments, Fed Chair Yellen expressed the bank's position that recent weak inflation numbers merely reflect temporary factors such as falling prices on cellphone plans and smaller than normal increases in drug prices. For the remainder of the year, the Federal Reserve plans to raise its benchmark rate at least once more - which it says would push the rate to a neutral level that neither encourages nor discourages economic growth.

Some central bankers have worried that investors are not responding to the recent rate increases. In many cases, it has become both cheaper and easier to borrow money. Additionally, data suggests that investors are taking larger risks in the current low rate environment. This is the opposite effect of what was intended by the Fed's recent moves. Of added concern is the low level of inflation, with the latest reading on the Fed's preferred inflation gauge, falling to its lowest level in six months.

With a 1.4% year-over-year increase in prices for May, officials are questioning whether the Fed is moving too quickly in raising overnight interest rates. The Fed, tasked with promoting full employment and stable prices, continues to target a 2% annual inflation rate. The price index poked above that threshold in February for the first time in nearly five years but has settled lower each month since then. With the pace of price increases having slowed in recent months, the Fed has been forced to back away from its predictions that 2017 would finally be the year where inflation firmly achieves the desired 2% pace. All of these issues are creating complications for our central bank as it charts the course for interest rates.

At almost 9 years, the current economic expansion is now the third longest in U.S. history with only the expansions of the 1960 and 1990s having lasted longer. Final estimates on U.S. economic activity for the first quarter were recently raised to 1.4%, up from the prior reading of 1.2%. Meanwhile, initial projections for the just finished 2nd quarter are more robust at around 2.5%, although this estimate has suffered substantial reductions in recent weeks. While the June jobs report showed that hiring continued at a healthy pace of 220,000 last month, and appreciably ahead of expectations for 179,000 jobs being created, other recent indicators in areas like consumer spending, construction and auto sales have been decidedly less robust.

Although the 2nd quarter's

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projected GDP performance is meaningfully ahead of recent quarters' economic growth, it is still a far cry from the annual gains of 3 percent or more achieved a decade ago and much less than the 4 percent growth rate of the late 1990s. Nor are current levels of GDP growth strong enough to deliver big increases in household income, which has been stagnant for decades for all but the wealthiest slice of the population.

The diminishing economic expectations have been reflected in the dollar's slump in recent weeks. That is not necessarily a bad thing — a weaker dollar makes exports more competitive in foreign markets. It is, however, a sign of the world's take on the American economy, as well as an indication of improving prospects abroad, especially in Europe. U.S. consumer confidence, which surged initially following Donald Trump winning the presidential election, has moderated in recent months. The most recent University of Michigan survey had its June consumer-sentiment index reading at 95.1, down from 97.1 in May and a near-term peak of 98.5 in January.

Not all is gloomy, though, as the nation's unemployment reading was 4.3% in May, the lowest level in 16 years, and the just released June job's data coming in appreciably above expectations. While there is no sign that a recession is brewing, neither is there evidence for the kind of boom confidently projected by the President as he entered into office. Barring renewed momentum on the Administration's proposed infrastructure spending or tax reform, we do not currently anticipate a sharp acceleration in economic growth. However, in the same breath, nor do we anticipate a recession in the near future. The challenge to the current situation is that, for many, the current low growth expansion is not raising all economic boats but primarily the metaphorical yachts of the wealthy.

Analyst Corner

Nike, the goddess of victory, has not been winning many battles lately for her eponymous sports apparel, footwear and sports equipment company. In recent months, Nike's competitors have had the upper hand in this market segment. Nonetheless, our assessment is that Nike, Inc. (*NYSE: NKE*) remains an attractive franchise longer-term. Although the business is extremely competitive, we view NKE's size, brand image, key sponsorships, and manufacturing as competitive advantages that will enable it to maintain its global market leadership for years to come. Nike also recently announced a new relationship with Amazon. Nike will now sell some items directly on the Amazon website, rather than just selling through third-party retailers. NKE sports a pristine balance sheet and highly consistent revenue growth. When factoring in a rapidly growing dividend, we believe that Nike will prove to be a winning proposition for many investors.

Market Comments

Global stock markets collectively had their best opening six months in many years. All but four of the 30 major indexes representing the world's biggest stock markets have risen this year, a first-half performance unmatched since 2009, according to The Wall Street Journal. In the past 20 years, only four first-half rallies have been as widespread as the current global surge. Two of these rallies preceded sharp market crashes, while two others came at the beginning of multiyear bull markets. The broad breadth of the current rally is attributed to strengthening corporate earnings, improving economies and continued central bank support.

In the U.S., Wall Street closed out the quarter on strength with the market having now rallied more than 9.3% since New Year's Day. Leading the market's advance, the technology sector has rallied more than 17.2% as investors wagered on continued strong earnings growth in the sector. On the downside, investor excitement continued to wane for the energy sector in the face of abundant supplies and declining energy prices. As a result, the sector has sharply lagged the overall market with year-to-date losses of more than 12.6%, closely mirroring the year's decline in U.S. crude prices. For the first half of 2017, the S&P 500 posted its strongest gain in 4 years as the market was bolstered by solid corporate earnings and expectations for improved economic growth.

Through it all, the market's focus has remained on central bankers, a key theme for investors since the Financial Crisis. While the U.S. has raised short-term interest rates four times since the end of 2015, the European Central Bank and Bank of Japan have mostly remained accommodative, helping raise asset prices. U.S. government bond yields have fallen, the dollar has weakened and oil prices have declined. Many point to the pickup in earnings growth as a vital driver of global gains this year. In the U.S., first-quarter earnings from S&P 500 companies increased 14% from a year earlier, the best growth since 2011. According to FactSet, analysts now expect roughly double-digit profit growth this year, as well as in 2018.

A more contrarian position is coming from the Treasury market as long-term Treasury bond yields remain very low, suggesting that traders do not buy the idea that economic growth is poised to accelerate. The bond market is flashing warning signals that bad times may be ahead for the stock market and the economy. Simply put, while the Federal Reserve has been raising short-term interest rates since December, the bond market hasn't gotten the same memo. The longer-term rates that are set through bond market trading have, for the most part, been declining, though there was a brief reversal in the last few days. The disconnect over the last few months is a sign that bond investors believe economic growth and inflation are still weak and that the Fed's interest raising actions have been premature.

In the past, when disputes between the Fed and the bond market have persisted and grown, they have sometimes predicted problems ahead — like a plunging stock market and, eventually, a recession. In general, high stock valuations and less volatile trading this year have prompted concerns that investor complacency is setting in. Clearly, price to earnings ratios, a common stock valuation metric, are extended.

Nonetheless, with few attractive investment alternatives available, the careful accumulation of good-quality stocks still seems prudent to us. For now, the rally in risky assets like stocks continues unabated, while the conflict between the Fed and the bond market continues on. Fed officials indicate that they are determined to keep raising short-term rates and to begin reducing the Fed's bond holdings — perhaps preparing the central bank for action whenever the next recession comes. At a bare minimum, the central bank policy choices ahead are difficult.

For investors, there are ample reasons for caution. Now is not the time to be reaching for risk, but rather, to make sure that your investment approach is consistent with both your comfort and ability to assume risk.

Performance as of 6/30/17

	Close	Month	YTD	1 Year
DJIA	21,349.63	1.74%	9.35%	22.21%
S & P 500	2,423.41	0.62%	9.34%	17.90%
NASDAQ Comp.	6,140.42	-0.94%	14.07%	26.80%

	Quarter end yield	Prior Year end yield	Yield 1 year ago
10 yr. U.S. Treasury	2.30%	2.45%	1.49%

Planning Thoughts

Occasionally, the bureaucrats in Washington mess up and do something of actual benefit for taxpayers. 1031 exchanges are one of these rare beneficial "errors." Under Section 1031 of the United States Internal Revenue Code, a taxpayer may defer recognition of capital gains, and related Federal income tax liability, on the exchange of certain types of real estate. To qualify for this exchange, the properties exchanged must be used either for business or for investment. The properties exchanged must be of "like kind", *i.e.*, of the same nature or character, even if they differ in grade or quality.

To make these exchanges, an intermediary called a facilitator must be hired before at least one side of the property swap is conducted. If you are holding a business or investment property that is sharply appreciated and are looking to dispose of this property, a 1031 exchange could make a great deal of sense. Please do not hesitate to contact us if you would like to explore this tax saving opportunity further.

Partners

Gerard A. Plauché, CFA

Clifford F. Favrot, CFA CFP™

Ainsley D. Bishop

Frank A. M. Williams, Emeritus

Operations Manager

John T. Egnatchik

Office Manager

Angelle M. Verbois

Contact Us Toll Free:
1-888-522-9019

228 St. Charles Avenue, Suite 1100, New Orleans, LA 70130
504-522-9019 PHONE • 504-522-9676 FAX

www.deltafinad.com

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