DELTA FINANCIAL ADVISORS
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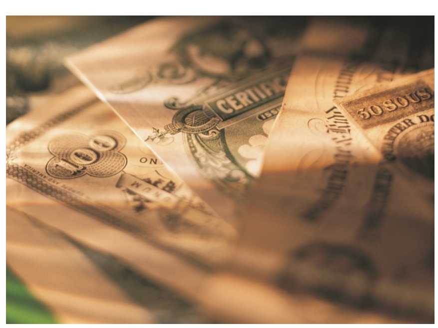
Economic Comments

Mixed signals regarding the near-term future of interest rates are coming from the Federal Reserve and the financial markets. While the fixed income markets are strongly projecting rates to remain unchanged through at least early January, the Federal Reserve Board is singing a different tune. While the central bank has proved more reticent in raising interest rates than anticipated, Chair Yellen continues to share her belief that overnight interest rates will be raised before year's end.

At the mid September meeting of the interest rate setting Federal Open Market Committee, the FOMC, only one committee member openly pushed to raise the target for overnight interest rates. The overall tone of the meeting's statement was dovish with an emphasis being placed on weakening overseas economies and the recently unsettled financial markets. While viewing the U.S. economy as stable, if not improving, American business activity remains short of where the central bank believes it should be.

The Fed pushed out to 2018 its projection of when the economy will re-achieve its desired inflation rate of 2%. The challenge in the Fed's current high wire act on interest rates is that while plentiful jobs are considered to be an unmitigated positive, too many jobs can quickly create upward pressure on labor prices or, in other words, inflation. Historically, labor costs have started accelerating once unemployment goes beneath 5.0%. The great unknown here is whether the current historic lows for labor force participation are temporary or structural in nature. Given the current historically low labor participation rate, an influx of new workers would stymie any sharp increase in labor costs.

A significant roadblock in the Fed's path to higher rates is the dimming inflation outlook, which could make it more difficult for the central bank to achieve its inflation target of 2 percent. A gauge of these expectations, the yield difference between 10-year Treasuries and 10-year inflation protected Treasuries indicates that forecasts for U.S. inflation over the next decade are now at 1.48%—near their lowest level since 2009. However, with inflation being perceived as too low, this is a mixed blessing. In short, the current excessively low inflation rate is helping to give the Federal Reserve the leeway to delay raising interest rates—possibly until early 2016.



Clouding the current economic picture has been new data released at the quarter's close. Contrary to the recent upward trend in jobs creation, the Labor Department's September report indicated that a relatively tepid 142,000 jobs were created—well beneath expectations for 200,000 new positions. Furthermore, new payrolls for the prior 2 months were revised downward by a total of 14%. With these updates, overall payroll increases have now averaged just 167,000/month over the last quarter—considerably below the 221,000/month average seen in the June quarter. All is not lost though. The influential Institute of Supply Management's September index reading on hiring rose, suggesting that the slower rate of hiring in the past two

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months may only be temporary.

Despite the reduced payroll growth, American consumers have maintained some optimism as spending has picked up momentum recently amid lower energy prices. Additionally, auto sales, often used as a proxy for consumer confidence, have achieved a run rate of nearly 18 million vehicles/year—an historic high. Another bright spot comes from new residential construction which recently hit its highest level since before the Financial Crisis.

While the most current jobs report was disappointing, the 2nd quarter's estimate of economic activity was sharply revised upwards to an annual pace of 3.7%, a significant increase from the initial estimate of 2.3% growth. The quarter's jump in activity was driven by strong business investment in factories and other hard assets. Somewhat offsetting this good news was the Conference Board's index of leading indicators August reading which rose only minimally, thereby signaling that growth could be modest through the remainder of the year.

Adding to current economic headwinds have been the dollar's surge against foreign currencies over the last several quarters. The latest Labor Department reports show weaker exports and diminished factory activity—all evidence that the greenback's strength is having negative effects on the domestic economy. The challenge is that a stronger dollar not only makes American-made products more expensive and therefore less competitive overseas, but the currency shift also favors foreign manufacturers as they can afford to sell their goods for less in the United States than domestic producers.

On the flip side, a key benefit of a stronger dollar is lower prices domestically for imports, especially for energy and consumer goods. In fact, in a late September speech, Chair Yellen, cited the dollar's strength as a key reason that inflation has remained beneath the central bank's 2 percent target.

As we look forward, expectations for global economic activity have faded somewhat. The International Monetary Fund's latest update reduced projections for global growth to 3.1% this year with its expectations for the key emerging markets arena having been reduced for both the remainder of 2015 and all of 2016.

Chair Yellen appears to now be less concerned about being too far behind the curve on a booming U.S. economy, but rather more focused on being behind the curve on a weakening global economy. While challenges remain domestically, we nonetheless believe that the underlying strength of the U.S.'s current expansion remains unimpaired.

Analyst Corner

With the industrial sector having performed poorly this year, some new investment opportunities in companies such as Emerson Electric (*NYSE: EMR*) have arisen. A manufacturer of diverse electronic and electronic products/systems, the company's share price has declined appreciably since early 2014. Both declining energy prices and the unsettled economies in the emerging markets have put a damper on recent revenues and profits. However, with a quality line of diversified products and strong management, we believe the negative investor sentiment is overblown. Moreover, the company sports a very strong balance sheet, robust returns on investor capital and a hefty dividend yield of more than 4%. While the near-term may be a bit rocky with its current headwinds, EMR should prove an attractive longer-term holding for many investors.

Market Comments

While the post Financial Crisis bull market is still alive, a breather from the ongoing advance was taken as the summer waned. Faced with slower Chinese and emerging market demand, a strong greenback and an uncertain U.S. interest rate outlook, investors re-evaluated their perspective on risk in late August. In a matter of days, skittish stockholders sent the U.S. market down more than 12% from its mid May high.

With market corrections typically occurring every 18-24 months, the August sell-off was well past due as the last correction, defined as at least a 10% decline from recent highs, had not occurred in over 4 years. Leading the precipitous fall was the energy sector with a decline of more than 21% year-to-date. The sole market sector with gains in 2015, consumer discretionary, with an advance of more than 4%, typically does well in times of a strong economy - somewhat counter to the spirit of the market's recent angst!

As spoken to earlier, the fixed income market continues to disagree with the Fed on the near-term direction of interest rates. In the face of the recent market turbulence and September's lackluster jobs report, the 10-year Treasury's yield fell to almost 2% - a signal that bond market is increasingly skeptical that the Federal Reserve will in fact raise interest rates before year's end.

Policy makers and investors alike are grappling with weak demand for goods and services, falling commodity prices and stubbornly low inflation - all factors that are positive for bonds. As a result, the general consensus amongst investors, if not policymakers, is that the U.S. central bank will be hard pressed to implement rate increases before year's end. Contrary to Chair Yellen's recent proclamation that there would be at least one overnight interest rate hike before year's end, traders now estimate less than a 30% likelihood of this scenario occuring.

As the third quarter's earnings season gets underway, forecasts for S&P 500 earnings now call for a 3.9 percent decline year over year with half of the market's sectors estimated to post lower profits. Driving this somber view are falling oil prices, a strong U.S. dollar and weak global demand. However, if the energy sector's 65% profit decline were to be excluded, overall corporate profits would be forecast to advance 3.7%. While it is unusual to remove one market sector from this assessment, the 55+% decline in energy prices does deserve some appropriate consideration.

If in fact the projected earnings decline does occur, it would be the second quarterly profit decline for the S&P 500 since the third quarter of 2009. The picture in the near term is not expected to substantially change as the ratio of companies reporting negative outlooks versus positive outlooks is at almost 20% above the historic norm.

Subsequent to this downward adjustment in stock prices, the S&P 500 index now sells for roughly 16 times its expected earnings for the next 12 months, lower than this year's peak of 17.8 but still higher than the historic mean of about 15. To put this in perspective, and based on current earnings, the index would have to drop to a level of 1,800 to bring valuations back to the long-term average.

However, given the historically low levels of inflation and of interest rates, we feel current valuations to be imminently reasonable on a relative basis even if they are more expensive based on historic norms. While we believe that the markets will continue with a bias towards elevated volatility in coming months, we also find there to be substantial reason to believe the current bias towards rising prices remains in tact. Nonetheless, we encourage ALL investors to insure that they are assuming that risk which is appropriate to their circumstance and not a lot more!

Performance as of 9/30/15

	Close	Month	YTD	1 Year
DJIA	16284.70	-1.35%	-6.95%	-2.11%
S & P 500	1920.03	-2.47%	-5.29%	-0.61%
NASDAQ Comp.	4620.16	-3.27%	-2.45%	-2.82%

	Quarter end yield	Prior Year end yield	Yield 1 year ago
10 yr. U.S. Treasury	2.06%	2.17%	2.51%

Planning Thoughts

As times change, people often struggle to keep up with new circumstances. Unfortunately, fraudsters have been very adept in keeping current. In recent quarters, financial fraud has unfortunately boomed. However, through several simple steps, many of the bigger potential fraud risks can be largely mitigated. For instance, if you receive a phone call from your credit card company, only call back the number listed on the back of your card. Also, sign your credit and debit cards with "See ID" rather than your signature. By doing so, few fraudsters will be able to replicate your signature. When going online, make sure that you only make purchases from reputable websites. Before making an online purchase, check to make sure that there is a padlock icon located at the top of the browser window and that "https" is indicated in the address bar - these two measures confirm that the page you are on is secure and that your information is encrypted. Of course, never share your credit card information online unless you are actually making a purchase.

Always be suspicious of emails from your bank or credit card company requesting account information - they should already have this data! Contact the company directly (and not through the unsolicited e-mail) to confirm the request. To limit dangerous e-mail, do not click on or respond to unsolicited junk e-mail in any fashion. While these measures are by no means exhaustive, these simple preventative measures can reduce your risk of potential fraud substantially. Although e-mails, electronic commerce, and communications have been a boon for many consumers, these technological advances have come with their own new set of daunting challenges.

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