Weekly Market Review

***e*Research Corporation** is pleased to provide a review of the markets by Eddy Elfenbein of **Crossing Wall Street**.

Mr. Elfenbein introduces his commentary with the following quote from James Bullard, the President of the St. Louis Federal Reserve.

"If you've followed my forecasts, you've probably lost a lot of money."

Read Mr. Elfenbein's analysis and market comments on the following pages.

Information about **Eddy Elfenbein** and **Crossing Wall Street** is provided at the end of this article. You can also learn about **Crossing Wall Street** by going to its blog website at: http://www.crossingwallstreet.com/.

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June 16, 2017

Crossing Wall Street: Weekly Market Review

by Eddy Elfenbein

BW: We have taken only an extract of Mr. Elfenbein's latest weekly article. If you wish to read the entire article, which includes stocks in his recommended portfolio, there is a link provided below.

Well…it happened. As expected, the Federal Reserve raised interest rates this week. I don't like it, but we can't always choose the ideal environment to invest in. If you wait for things to be perfect, then you would never be in the market.

This was an important meeting for the Fed because they also explained what they intend to do with their enormous balance sheet. This has been a big concern on Wall Street.

Additionally, the central bankers updated their economic projections. I should explain that the Fed has a pretty dismal track record of predicting where things will go, but it is still useful to look at their outlook for the economy.

Fortunately, the stock market continues to hold up well. The S&P 500 closed at another all-time high on Tuesday. However, there has been a significant weak link in the market recently, and that is big-cap tech stocks. Don't feel too bad for these guys. They have been running up the score lately, so I can't say it is not wholly surprising to see them face a little pain.

The Federal Reserve Raises Interest Rates

On Wednesday afternoon, the Federal Reserve released its latest policy statement. The central bank said they raised their range for the Fed funds rate to between 1% and 1.25%. That is an increase of 0.25%. This was the second rate hike this year, and the fourth of this cycle.

As I have said before, I think this move is a mistake, and I will not belabor the arguments against the increase. It happened, and we have to move on. I will note that there was one dissenting voice, Neel Kashkari of the Minneapolis Fed, who agrees with me.

On Wednesday morning, just hours before the Fed's statement, the government released the inflation report for May. The report again showed that there is absolutely no threat of inflation on the horizon. If anything, the rate of inflation has fallen off sharply over the last three months. It is hard to justify rate increases to fight off an inflation threat that does not exist.

During May, the headline rate of inflation fell by 0.1%. Economists had been expecting no change. Some of that was due to falling prices for gasoline. That is why we also want to look at the "core rate," which excludes volatile food and energy prices. But the core rate for May only rose by 0.1%. There is simply not much inflation out there right now.

You may recall that March was the weakest month for core inflation in over 30 years. As with all stats, we do not want to be fooled by one-point trends. There are always outliers, so we want to see more evidence. Indeed, that evidence came in the last two months. Core inflation for April and May were the second- and third-weakest of the last three years, trailing only March. So it is not only that inflation is low: it is actually going lower!

More troubling is that we have seen a swift reaction in the bond market. On Tuesday, the yield on the 10-year Treasury dropped to 2.1%. That is the lowest point all year. After the election last year, Treasury yields soared on economic optimism, but that has largely faded in recent weeks. The spread between the two-year and ten-year Treasuries is now less than 80 basis points.

In the Fed's policy, they acknowledge the recent weakness in the economy, but they seem to feel that it will soon pass. I hope they are right, but I just do not see the evidence just yet. In fact, this week's retail-sales report was another dud. Economists had been expecting a gain of 0.1%. Instead, retail sales fell 0.3% in May. This was the biggest drop in 16 months.

But the Fed thinks they have only started raising rates. According to the latest Fed projections, they expect to raise rates one more time this year. After that, the outlook becomes a lot less clear (the blue dots get much more dispersed).

The Fed sees three more hikes in 2018, and possibly three more in 2019. That means it is possible that the 2/10 spread could be negative as early as next year. Still, I don't want to be too alarmist. By the Fed's own projections, they see real interest rates staying negative for another 18 months. My point is that we are not in the danger zone just yet, but we can see it on the horizon.

The Fed also unveiled its plans for what they intend to do with their $4.2 trillion balance sheet or, as the Fed calls it, their "normalization plans." The Fed said they plan to stop reinvesting the proceeds of their bonds in gradually increasing increments. It will be a long, long time before the balance sheet gets back to normal.

But the key point is that the Fed intends to raise rates at the same time they address their balance sheet. That point was not always so clear.

The Great Tech Stock "Crash" of 2017

What is happening with tech stocks? The tech sector has fallen four times in the last five sessions, and some of those drops have been pretty sharp. The stock market had been so placid for so long that a fairly minor bump in the road for large-cap tech stocks has rattled a lot of investors.

Let us add some context here: tech stocks had been leading an already powerful rally. In fact, the rally has not even affected the whole sector. A huge part of the gains have fallen on just five major stocks; Facebook, Apple, Amazon, Microsoft and Google. That's right: the latest acronym hitting Wall Street is FAAMG. *(BW: Netflix is also down, about 9%.)*

At one point, Facebook, Amazon and Apple were all up over 30% for the year. That was more than three times the rest of the market. Not anymore! In the last week, the **Tech Sector ETF** (XLK) has dropped from $57.44 to $55.57 (-3.25%).

I want to stress that the damage we are seeing in tech is hardly unprecedented. What has been unusual is the exceedingly low volatility visible until now. It is the change from very, very low volatility to normal behavior that has jarred Wall Street. Frankly, the current losses are very normal.

Next Week

There is not much in the way of economic news next week. On Wednesday, we will get the existing-home sales report for May. Then, on Friday, there will be the new-home sales report. For now, the housing sector is a bright spot in the economy, while consumer spending looks tired. We will see how long this can last.

Be sure to keep checking the blog for daily updates, and I will have more market analysis for you in the next issue of *CWS Market Review*!

- Eddy

BW: In the rest of the newsletter, Eddy reviews the earnings announcements of the companies on his Buy List. You can read about them and the entire article by clicking on the following link:

http://www.crossingwallstreet.com/archives/2017/06/cws-market-review-june-16-2017.html

Crossing Wall Street

Your Guide to Financial Success

Hosted by Eddy Elfenbein

Named by CNN/Money as the best buy-and-hold blogger, Eddy Elfenbein is the editor of Crossing Wall Street. His free Buy List has beaten the S&P 500 for the last six years in a row. This email was sent by Eddy Elfenbein through Crossing Wall Street.

BW: Information on Eddy Elfenbein and Crossing Wall Street follows on the next page.

ABOUT THE AUTHOR

Welcome to Crossing Wall Street

I started this Web site to help individual investors. I have to admit that I *love* the stock market. I think I must be an addict. In my opinion, the stock market is one of the greatest inventions in history. The stock market is simply the most consistently successful way to make money over the long term. Even after the financial crisis, stocks have still beaten every asset category over the long haul—bonds, commodities and real estate.

While the stock market may bounce around from day to day, and even month to month, the long-term trend has always been higher. Over the last 35 years, stocks have gone up 35-fold. And since the end of World War II, the stock market is up an amazing 120,000%. I wish I had been around! That was the beginning of an American financial revolution. Today, we're at the beginning of a *global* financial revolution. That is why I think the next 70 years will be even better.

The key to doing well on Wall Street is actually very simple: Buy and hold shares of outstanding companies. But too many investors never learn this valuable lesson. Or if they do learn it, they learn it the *hard* way. That is where I come in. I want to help investors avoid the mistakes that separate successful investors from those who always find themselves spinning their wheels.

There are lots of pitfalls on Wall Street. From shady companies that are more popular than they are profitable to a mutual fund industry that is more interested in its fees than serving investors. Todayis investors must be careful.

At Crossing Wall Street, I give investors my free and unbiased view of the market. I probably analyze dozens of companies every week. I am always looking over income statements and balance sheets. I've spent several years collecting my list of the best companies to own. This is my current Buy List. I've included a description of each company and its current share price. These are the ones that I make the most effort to follow on the site, but please feel free to ask me my opinion on any stock. I don't receive compensation from any of the stocks I recommend. Also, I don't "short" any of the stocks I criticize. At any time, I may own the companies on my Buy List. All of the information on this site is free and unbiased. I also have a section for Frequently Asked Questions that will help you learn more about Crossing Wall Street.

Please feel free to e-mail me. I enjoy getting feedback from investors. I am happy to give you my opinion on any stock or investing in general. I should warn you that I cannot give out personal portfolio advice, but all other topics are fair game. You can also check out some of my favorite links.

- Eddy Elfenbein

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