Podcast Episode: August 2016 Market Update | August 22, 2016

Elean: Welcome to the Paragon Financial Partners podcast, where we discuss the markets, our strategies, and how to live better today while planning for tomorrow.

Hello, and welcome to the Paragon podcast. I'm here with Evan Shorten, the firm's founder and principal.

Evan: Hello, this is Evan Shorten and I want to thank everyone for tuning into this episode. If you would like to listen to our previous episodes, you can do so at paragonfinancialpartners.com/media. To subscribe to our podcast, you can find us on iTunes or Stitcher Radio.

Elean: So, today we want to talk about the market and provide an update of what has been going on lately. We saw both the S&P 500 and Dow Jones hit all-time highs in the second half of July and maintain their gains despite increasing uncertainty in both the U.S. and abroad; we're seeing the price of oil constantly fluctuate depending on daily news; low gross domestic production in both the U.S. and Europe; and as of now, none of these seems to affect the markets. Evan, what's the consensus behind the rise in equity markets?

Evan: So, there are a number of reasons why we're experiencing this market rally. With the 10-year U.S. Treasury yield down to 1.52% as of Thursday, August 18th, we continue to see investors seeking income from dividend paying stocks. Investors are trying to find yields and the bond market is not providing enough of it. We can actually see this playing out by the fact that Vanguard has closed its dividend growth fund to new investors. The fund saw an increase in cash inflows of over $3 billion in the last six months and that's just crazy. Additionally, we had an earning season with a lot of major companies reporting good results. Companies like Amazon, Google, Alcoa, Mastercard, Wells Fargo, Facebook and many others have posted solid earnings when they reported two weeks ago.

While we're not advocating or recommending these stocks, we just want to make the point that large companies that make up the main equity indices did well and that provides a certain level of investor confidence. Additionally, trading volume is down due to summer months, with the end of August typically being the period of the year with the least amount of trading volume. The last thing I want to mention with regards to the most recent market rally is that uncertainty in China and Europe are pushing investors into U.S. equities. There's been a lot of economic data coming out of China depicting a broad slowdown along with increasing debts as the Chinese government tries to stimulate the economy.

Additionally, Europe continues to experience economic problems with Greece and Spain, slowdowns in France and Italy, combined with Italy's weak banking sector. Simply put investors, both domestic and foreign feel sense of safety in U.S. equities compared to the international markets.

Elean: Okay, since you mention foreign investors, do you think foreign investors are having a large impact on the U.S. markets overall?

Evan: Yes, it's not just foreign investors seeking safety in the U.S. equity markets but also U.S. bond markets. One of the reasons we have seen the 10-year Treasury continue to come down is because of an influx of foreign investors seeking both safety and higher yields.

Elean: Higher yields? I think a lot of our listeners might think that sounds funny, foreign investors putting their money in the U.S. due to higher yields.

Evan: Well, yeah, it sounds somewhat weird to say it out loud but ironically as we deal with historically low yields in the U.S., many developed nations actually have much lower yields. A few countries like Denmark, Germany, Japan, Sweden and Switzerland actually have negative yields at the moment. Essentially, the U.S. is giving foreign investors a balance between safety and yield that is becoming increasingly difficult to find in the developed world.

Elean: Okay, then. As we mentioned in the beginning, oil has been fluctuating whenever any news comes out. As of today, Friday, August 19th, oil is around $49, $50, which is an increase over the recent $40 per barrel mark. How does this affect U.S. equity markets?

Evan: While no one can predict what's going to happen in the market tomorrow, I'm not sure oil will have too strong of an impact on the markets. Obviously, oil prices held steady, it would help calm investors, but again, there's a lot of hunger for yield. We've been in rally mode since February, and the markets have leveled off a little bit in June and then rallied again in July and maintained. All this occurred during oil price declines. When the price of oil went down to the price of $40 a barrel, equities are behaving somewhat independently of oil, and again, the hunger for yield and relative safety seems to be the driving factor.

Unless the Federal Reserve raises interest rates by a meaningful amount which I believe is highly doubtful, the current condition pushing investors into equity markets are likely going to continue. The major thing we took away from this past Wednesday is Federal Reserve meeting, is that the Feds is divided with respects to interest rates, and as long as the Fed is divided, rates are likely going to continue to stay at current levels.

I also want to emphasize that investors should invest in a broadly diversified manner and not focus too much on short-term movements. With the upcoming election, we are bound to see more volatility in the markets. Just because oil is down or there are sentiments about the equity markets being too hot, a potential bond bubble, etc., being broadly diversified over several asset classes with a long-term view is going to be a prudent strategy. Don't make any hasty decisions based on the news of one day. I'm confident the news and the media will report about something completely different two or three days later.

Elean: Okay, great. Thanks for the insight Evan. We hope you enjoyed this episode of the Paragon podcast. If you want to listen to more of our episodes, please visit our media page at paragonfinancialpartners.com/media. Also, please subscribe to this podcast on iTunes or Stitcher Radio, and again, thank you for tuning in.

Evan: Yes, thank you very much.

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