

APRIL 2017

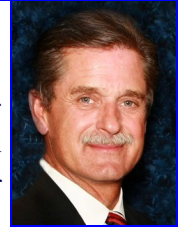
Scott's Thoughts —

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The Long Long Trailer and a Bit about the Market

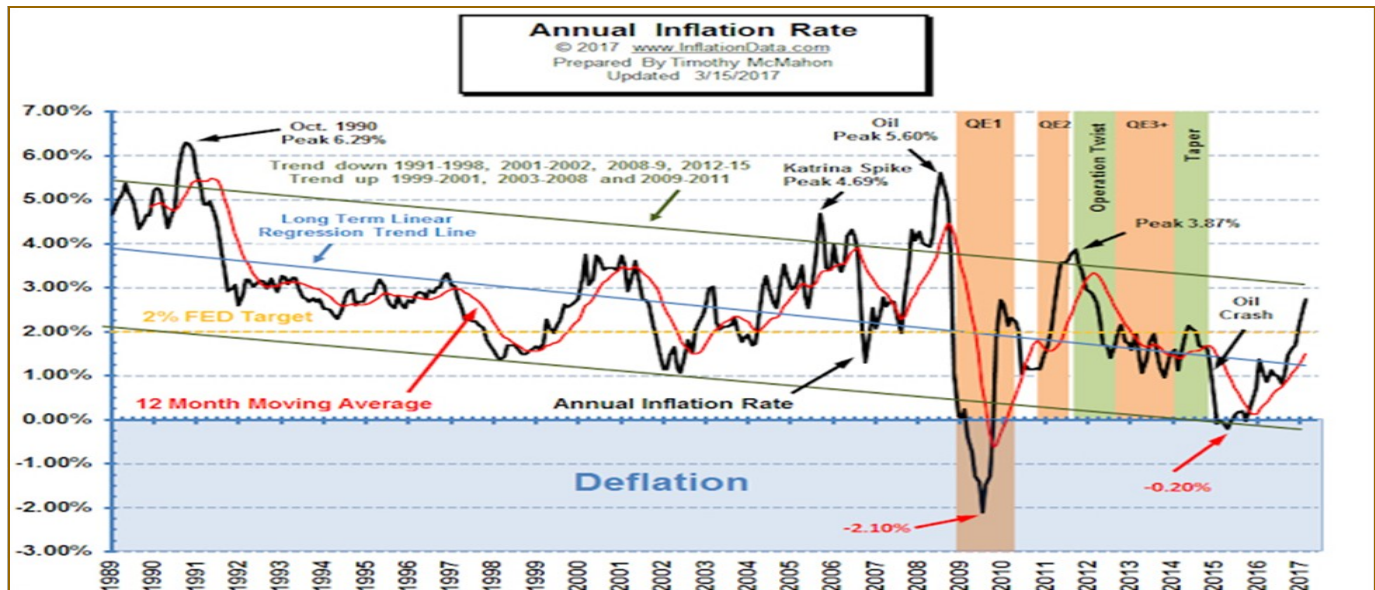


Scott Husband

The first quarter of 2017, brought higher prices in the equity indexes, slightly higher prices in the bond markets and metals, with the surprise being the financials and oils. The Energy Sector (XLF) declined almost 10%, while the financial sector (XLF) rose, but less than the S&P 500. I expect both of these sectors to out-perform the broader indexes as this bull market matures.

Overall, the equity market is not inexpensive. The current rally began after election-day and I believe reflects positive investor sentiment generated by the perception that the economy will improve because taxes will decline and regulations will become less onerous. These things need to happen to justify this rally.

The last week of the quarter was quite a week. The transportation index rose 2.5% in the week. The Russell 2000 (IWM) rose the same 2.5%, the S&P 1%, and Amazon increased \$20 Billion in value (in the same week!). Consumer confidence is at a 16 year high, 93% of manufacturers are optimistic, and the NASDAQ enjoyed 21 record closes in the quarter. Its' been a good run. The CPI (inflation) came in at 2.9%, which reflects the improved optimism (confidence begets demand, both consumption and investment).



With the consumer price index (CPI) rising and the Fed no longer “printing” huge amounts of new dollars, it seems reasonable to assume that the velocity of money is increasing. I have written about this in the past. The velocity of money is simply how many times a year a dollar is earned and spent. During the Great Recession the Fed printed trillions of new dollars BUT deflation was the outcome. Though there was an abundance of money, the Great Recession scared consumers and corporations resulting in the velocity of money declining dramatically. Today’s increased confidence should increase money velocity, with the expected result being what we are seeing in the current inflation numbers. Interest rates declined slightly in the first quarter even as the CPI rose, which can happen but not in the longer term. Historically the “real” borrowing rate (inflation adjusted) is 3%. Today the 10 year Treasury bond pays less than 2.5%; inflation is 2.9%. At this rate, the buyer of a 10 year bond will lose over 5% purchasing power and perhaps as much as 7-8% purchasing power after paying income taxes.

Scott's Thoughts (continued)

The lawmakers in Alaska are talking about new taxes. One of the options is an income tax based upon the Federal Tax return. I find it difficult to believe Alaskans require three times more per capita government expenditures than Californians do. (In 2015 Alaska spent \$18,196 per capita compared to California's \$6,420. Kaiser Institute). The chart below shows the Federal income tax levels. I understand that over 40% of tax returns pay no income taxes at all, while the top 3% pay more than half.

After everything is said and done, "we find that every man, woman, and child owe over \$70,000. Worse yet, the total debt per taxpayer is over \$190,000 and rising fast. If you include unfunded liabilities, the total debt per taxpayer rises to around \$1.2 million, give or take." (debt clock). Placing all else aside, government debt is beyond our capacity to repay without diminishing the value of the dollar. This is the reason I continue to own hard assets. I am optimistic on the economy and therefore stocks, but not if the administration's agenda is beyond political reach. Bonds enjoyed a 3 decade long bull market, ending with NEGATIVE interest rates. Obviously that market has seen its' best days.

Who pays income taxes? The rich, mostly

Individual income tax statistics, by income group

| ADJUSTED GROSS INCOME | % OF RETURNS FILED | % OF INCOME TAX PAID |
|------------------------|--------------------|----------------------|
| Less than \$15,000 | 24.3 | 0.1 |
| \$15,000 to \$29,999 | 20.4 | 1.4 |
| \$30,000 to \$49,999 | 17.6 | 4.1 |
| \$50,000 to \$99,999 | 21.7 | 14.9 |
| \$100,000 to \$199,999 | 11.8 | 21.9 |
| \$200,000 to \$249,999 | 1.5 | 5.9 |
| \$250,000 and above | 2.7 | 51.6 |

Note: Preliminary data are based on a sample of individual income tax returns filed between January and late September 2014, which are then weighted to represent a full year of taxpayer reporting.

Source: Internal Revenue Service

PEW RESEARCH CENTER

On a personal note, our adventure in the "long long trailer" was not at all what we planned. A year ago we began planning an RV trip with my siblings, leaving Spokane and heading down the coast eventually arriving in Phoenix. Heading towards Spokane, on old snow covered mountain roads, was the first indication that things might not go as planned. As a hint, know that a GPS setting of "fastest route" does not necessarily mean that. Next came a 15,000 pound trailer pushing the truck down a steep and snowy mountain road ending with a nights' stay (not rest) in a Wal-Mart parking lot. Frankly, I did not see that coming. Of course being unable to exit the parking lot without stopping traffic in both directions added to the adventure. Arriving on the coast of Oregon, after snow, sleet, and even hail, was where I learned that by the third time my wife says "POLE!", it is too late to avoid said "pole". The damage was fairly small. Did you know they had record rain fall on the coast this year? Did you know that Crescent City, California had 50 foot waves (which washed away that night's destination). Not every river we camped by had flooded. Not every canal had broken. But it did rain 20 of the 21 days we traveled. And with enough wind, rain can go sideways. I did not know it was a \$300 fine for walking a dog without a leash on the beaches of California. Same amount as the fine for leaving a dog unattended in a car as one rushes into a store. Palm Desert was pleasant except for a friend's unplanned need to visit a hospital (everything turned out fine). It does rain in Phoenix by the way. The really good news, a ticket from Phoenix to Fairbanks cost only \$350. And even better, the 3,600 miles I drove back to Fairbanks was without our dog needing to stop even once (she was \$100 to get on the plane) and I could listen to four books on tape. By the way, in Montana there are very few liquor stores, but one can buy a full bottle from any bar apparently. I visited Safeway's wine aisle, and the "long long trailer" sold last week.



Olive Sez...a fish out of water?!?!