Market Commentary

November, 2012

Over the seven market trading days after election day (through November 15th) the Dow Jones Industrial Average (DJIA) dropped 703 points or about 5.3%. Since then, through last Friday November 23rd, it has regained 467 of those lost points, but is still down 1.8% since election day, the result in keeping with conventional expectations: The president is reelected, which will be bad for business, therefore it is bad for the market. If the election had gone the other way, the conventional expectation was that the market would go up. Regardless of the election outcome, short-term trading is an emotional reaction, and has little to do with the longer-term outlook.

One theme of the election cycle has been the anemic growth rate of the current economic recovery. The Republicans blame it on the current administration’s policies, and the Democrats blame it on the prior administration’s policies. There is some truth to both of these positions. First, we are recovering from a very deep recession and monetary crisis that began in 2007 and ended in mid 2009. Mr. Obama cannot be blamed for that recession. The recession included a debt crisis at all levels: households, businesses, local and state government, federal government, as well as foreign governments. Research has shown that financial-crisis recessions take longer to recover, mainly because all of these participants concentrate mostly on reducing their debt rather than spending and producing. But the administration can be blamed for policies that have exacerbated the debt problem at the federal level, delayed the writing down of debt at the household level, and encouraged state and local governments to put off their own hard debt choices. Finally, both parties can be blamed for sticking so closely to their own ideologies and refusing to compromise on taxes, spending, and a needed restructuring of both the income tax system and the entitlement systems.

Here is some interesting information that gets very little coverage in the popular press, and virtually no mention by any presidential campaign: Since World War II until about four years ago, Federal spending as a portion of the economy averaged about 20%. Federal revenues averaged about 19% of the economy. (The economy is measured by Gross Domestic Product or GDP.) However, over the past four years, revenues have averaged only 16% of GDP, while spending has skyrocketed to 24% of GDP. This is a huge mismatch that must be remedied with increased revenue and reduced spending. And so we are $16 trillion in debt.

Fear of the "Fiscal Cliff" May Be Overblown

But I believe there is some good news to be had. First, federal revenues have increased 26% since fiscal year 2009 (the last year of the recession), while spending went down slightly in 2012, meaning that the current year deficit is about 28% less in 2012 than it was in 2009. This is progress, although far from what we should have to see a healthy, robust expansion.

Second, consumers are paying down debt and confidence in the future is up. Household debt has dropped by about 9% from its peak in 2008, from about $12.5 trillion to $11.4 trillion. Even better, the consumer’s ability to handle that debt is much better. Debt service payment as a proportion of household disposable income is at its lowest level since 1995. Consequently, consumer spending has been ticking up – most recently evidenced by increased consumer Black Friday spending, as compared to last year's numbers.
Third, leading economic indicators, even throughout the contentious election campaign, have remained firm; both manufacturing and service industries, while not robust, are in expansion mode. And fourth, stock market indicators that usually begin to deteriorate prior to a bear market and a recession have been holding surprisingly firm. One thing I have learned over the past three decades is that the stock market, which is a consensus opinion of millions of participants, cannot be ignored as a predictor of the future. Finally, considering the increased visibility of the problems we have, we may now be in a situation where the pain is too acute for politicians to ignore.

The Rush for “Alternatives” Continues

During the last extended bear market of the 1970s and early 1980s, as investors became impatient with the volatility and lack of return on traditional investment in stocks and bonds, so-called alternative investments gained favor. Real estate partnerships, direct oil and gas purchases, precious metals, diamonds and gemstones, and market timing strategies were promoted by advisors and product pitchmen everywhere. In 1982, just as the alternative craze was at its frothy zenith, the stock and bond markets were at multi-year lows and about to take off. In the investment world as in other areas of life, no trend lasts forever. In August of this year, headlines appeared announcing that US Treasury bonds were the single best investment category over the previous 30 years (1982 to 2012). Stock returns were only slightly behind bonds. But alternatives, at least those that survived and whose returns could be measured (gold, real estate, energy), appeared far down the investment return scale.

(On a personal note, I was not immune to the pitches I heard in the 1980's. I incorporated all of the mentioned alternatives in the portfolios I advised at the time. My long-time clients will certainly remember. Fortunately, I did not go "all-in" in those alternatives, nor did I abandon traditional stocks and bonds, as some of my colleagues from that era did. Diversified portfolios made sense at that time, as they do today.)

The same types of “alternative” investments are once again in vogue, driven by the poor returns and volatility of the stock market over the past 12 years, and boosted by the recent gains in gold, energy, and other commodities. We may have different reasons for the bear stock markets of the past few years, but to many purveyors of investments, the pitch is the same: “You can’t make money in stocks and bonds, so you need these alternatives.”

Today’s emphasis on alternatives is one more reason to believe that today’s markets and economy are not as bad as they seem. Over the next few years I believe that a traditional diversified portfolio of stocks and bonds, allocated to match each investor's goals, time horizon, and risk tolerance, will provide better results than the so-called alternatives that are popular today.

As always, we invite you to call us any time you have questions or concerns about your financial situation.

The statements above are the opinion of Kevin N. Tucker, CFP, as of November 26, 2012, and are subject to change at any time without notice. The above statements are not a recommendation of any investment product nor a solicitation to buy or sell any security. Past performance is not indicative of future results.

1 The Dow Jones Industrial Average(DJIA) is an index of 30 stocks traded in the US that represent a cross section of industries.

Dates for your Calendar:
Tucker Financial Services will close December 24th & December 25th for the Christmas holiday.

New Phone System
We recently updated the Tucker Financial Services phone system. As with all technology designed to increase office efficiency and function, it makes everything more complicated at the outset 😅. Ideally, during office hours, Gwen or Susan will answer the phone within the first few rings and help direct your call. In the event that we are busy or your call comes after hours and you receive the message system, please listen carefully to the menu choices to make your selection and leave a message. We apologize for any inconvenience.