CORRIGAN FINANCIAL, INC.

Market Update: November 2015

With investors agonizing over the prospects of a December rate hike by the Federal Reserve, stock and bond markets in November were relatively calm. November's calm was in contrast to the steep declines in August and September, and the strong October rebound. **In fact, for the past two months, domestic stock indexes have climbed by nearly 9 percent.** Global stocks remain flat for the year, with U.S. stocks up modestly. U.S. bonds are up by less than 1% year-to-date, while foreign bonds have declined sharply against the headwinds of a rising dollar.

> **We know that zero rates are no longer required for this economy.**
>
> **Joseph Carson, Alliance Bernstein – WSJ 12/5/15**

Update from the economic front:

- U.S. factory activity in November declined due to weak global demand and a strong dollar. Exports declined for a sixth straight month. (Note that a strong dollar makes U.S. exports more expensive to foreign buyers.)
- China's manufacturing activity declined to the lowest level in three years.
- Corporate defaults in emerging markets have hit their highest level since the great recession. (Emerging market corporate debt has grown five-fold over the past decade, with much of this increase coming from emerging Asia.)
- The euro lost 4% against the dollar in November.
- Gold declined 6.6% in November … the result of investors anticipating a rising interest rate environment.
- Oil prices declined amid the battle for market share (OPEC vs. the U.S.) which has inflated inventory during a time of weak aggregate demand.

Is there any good news out there?

- Manufacturing accounts for only 12% of U.S. economic output, while the services sector (which accounts for most of the jobs and consumer spending) is expanding.
- Long-term unemployment in the U.S. has fallen by two-thirds since the 2010 peak, and the unemployment rate has been cut in half.
- U.S. job growth is a good sign for wage growth, which could help to push up inflation (approximately 1.3% currently) to the Fed's 2% target.
- China's service sector is expanding and has been a bright spot for their economy. Services now account for 51.4% of China's economy … up from 49.1% in the previous year.

> **Investing in China makes sense for long-term investors. As the world's largest manufacturer, China accounts for 20% of global trade and 7% of global consumption. The total market capitalization of China's three largest stock exchanges has increased from $667 billion in December 2004 to $8 trillion in December 2014. Our interactions with the Chinese officials have been fantastic. They're trying to be planned and thoughtful about their markets' evolution.**
>
> **Joe Brennan, Head of Vanguard's Equity Index Group – 12/3/15**

Let's face it, whatever happens in China significantly impacts the global economy. While Beijing has cut interest rates and increased spending, there are legitimate concerns that growth will continue to decline in the near-term.

Emerging market debt levels have escalated … collateral damage resulting from the Fed's zero-based interest rate policy. **Emerging market corporations found plenty of available capital, as investors searched the globe for higher yields.** That flow of capital has now slowed dramatically, with bond issuance in emerging markets declining by 30% from the previous year.

Stock values have been bolstered by *synchronized* global central bank stimulus. But after a solid November jobs report (Friday, December 4), it is a near certainty that the Fed will start increasing rates in December.

Increasing rates (tightening monetary policy) is in direct contrast to the monetary stimulation being provided by Europe, China, and Japan. The concern is that this *divergence* promotes a strong dollar, which keeps inflation low (by pressuring commodity prices) and hurts U.S. exports.

So we will be going from *synchronized* to *diverging* global monetary policies. The ultimate economic impact of this policy change remains generally unknown … and we all know that the markets do not like uncertainty.

After 6+ years of recovery, the negative "unintended consequences" of zero-based interest rates now probably outweigh the benefits. **It is time to take off the training wheels and start to normalize our economy.** While future interest rate increases are expected to be slow and gradual, investors should brace for turbulence. Keep in mind, the sooner our economy is *normalized* the better we will all be in the long-run.

Have a wonderful Christmas holiday season and a happy and healthy New Year!

Daniel G. Corrigan, CPA/PFS, CFP®