# HARBOR VIEWS

HARBOR ADVISORY QUARTERLY NEWSLETTER

**Summary 2017**

HARBOR ADVISORY
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**A LOOK INSIDE HARBOR VIEWS**

- *Thoughts on the Economy* – The bright spot continues to be job creation which has now finished the first seven months of 2017 at an average rate of 184,000 new jobs created per month.
- *Our View of the Financial Markets* – We have not changed our expectation that foreign shares will perform better than U.S. shares, even with a lower dollar, for a number of years. The valuation disparity remains widely in favor of overseas shares.

**LATEST NEWS FROM HARBOR ADVISORY**

- You can visit us at: www.harboradvisory.com. Take a look and let us know your feedback.
- Jack De Gan continues to make news with his regular guest appearances on CNBC's top rated financial shows "Squawk Box", "The Call", "Closing Bell" and on Bloomberg TV, Fox Business News and National Public Radio.

## THOUGHTS ON THE ECONOMY

The second quarter of growth in the U.S. economy at 2.6% brought the full year rate of expansion back to the 2% level. The rate of economic growth in the U.S. economy has been at this anemic 2% rate since the recession ended in June 2009.

The bright spot continues to be job creation which has now finished the first seven months of 2017 at an average rate of 184,000 new jobs created per month. Wage gains year-over year were 2.5% before inflation. The wider U-6 rate of unemployment, which includes discouraged workers who have given up looking for a job and those working part-time who would prefer to work full-time, is currently 8.6% versus 7.9% prior to the recession.

The earnings for the companies listed in the S&P 500 are growing 12% in the second quarter after advancing 14% in the first quarter. We expect full year earnings growth to approximate 10% as a slower second half sees a slowing in the rebound of energy prices.

Capital investment by corporations continues to run at a rate well below the long-term average holding down productivity gains and, consequently, income growth. Washington could affect the rate of capital investment through tax reform with a lower rate structure and repatriation of foreign profits providing incentives to invest.

We continue to look for residential housing investment to pick up later this year or early next. New home construction is running at a rate of 600,000 units per year, 40% below the historical average, even as population continues to expand. This has led to home price increases and an unusually low inventory of homes for sale.

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**Nod to the ubiquitous disclaimer**: While we're not infrequently, and always quite accurately, accused of being of strong opinion – we want to let the reader know we've been wrong before, we will be again, but please don't hold it against us. The forward looking parts of the letter are the best efforts of fallible humans working at Harbor Advisory.

## OUR VIEW OF THE FINANCIAL MARKETS

The U.S. equity market has now achieved our 2017 return goal of 10-12% total return as of early August. The better than expected corporate earnings growth reported in the first half could add just a bit more return to stocks by year-end. Dividends paid by the companies listed in the S&P 500 have increased by 10% over the rate paid last year…a welcome support for income hungry investors.

The foreign exchange value of the U.S. dollar has again declined during the second quarter which has helped increase the earnings of U.S. companies who do business overseas. Harbor investors have benefitted from exposure to non-US equities which have outperformed U.S. stocks this year. However, if the dollar remains at its current level the competitive advantage of those foreign firms will be eroded. We have not changed our expectation that foreign shares will perform better than U.S. shares, even with a lower dollar, for a number of years. The valuation disparity remains widely in favor of overseas shares.

This year, the return on bonds for the first several months of the year has been low single digits as market interest rates have risen slightly. We expect bond returns for the year to remain low as rates slowly shift upward.

The Federal Reserve has raised the federal funds rate by .5% thus far in 2017 and will raise by another .25% later this year. We also expect the Fed to shrink the bank's balance sheet as they refrain from reinvesting maturity proceeds and interest payments in the portfolio. This process should slowly put upward pressure on interest rates which will hold returns on bonds to their coupon rates or less.

## PESKY PASSWORDS

Passwords are the bane of our modern cyber existence. With internet usage extending to all sorts of consumer access to vendors and service providers, the modern household's list of passwords can reach arm's length. Daily announcements of hacking and computer security breaches at corporate and consumer levels assuredly underestimate the extent of our susceptibility to internet fraud. The first commandment of the internet must surely be "BACKUP YOUR DATA DAILY". The second must be "PASSWORDS ARE YOUR CYBER ARMOR." It turns out that long passwords consisting of words (e.g. computersstinkkeepmesafer) are more effective and *more useable* than shorter passwords which include difficult to remember special characters.

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