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Quarterly Economic Commentary: 3rd Quarter 2016

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It's hard to imagine that we are nearing the end of another year. When we began the year, many thought the seven-year economic expansion had ended. But thanks in part to low inflation, low interest rates and a rise in real disposable incomes, the stock and bond markets have moved higher.

Bucking a five-year trend, diversification has finally worked in the first nine months; gold, real estate, foreign bonds, and commodities all performed better than stocks. This has had a material effect on multi-asset portfolios. For the quarter, domestic stocks were strong. The S&P 500 has recorded a very solid year-to-date return (YTD) of +7.8%, but the Vanguard FTSE Emerging Markets was much stronger at +17.4% YTD. Foreign stocks added value to many diversified portfolios, while acting as an invaluable hedge against a relatively weaker dollar.

In terms of bonds, we continue to see an unprecedented prolonged period of low interest rates. At the end of September, the 10 US Treasury yield stood at 1.60% as compared to 2.09% at the start of the year. Bond prices rise as yields fall and as a result, many bond holdings have appreciated. While this trend could easily reverse if the Fed decides to raise short term interest rates over time, this has not been the case so far in 2016. Furthermore, a change of 25 basis points (or .25%) to the Federal Funds Rate, as anticipated in December, should not have a meaningful effect on bond prices.

Although we reached new all-time highs in August, there are reasons to believe that this bull cycle can continue a bit longer. Many of the things we worried about three years ago – weak dollar, high oil prices, China taking over the world economy and recession – seem like distant memories today. Again, real disposable incomes are rising so consumer confidence is strong, which leads me to think that a recession is not an imminent threat any time soon. In our January Economic Commentary, I will discuss some of the possible economic implications from the election.

Sources:

Horseshoorn, Perspectives on Market Performance to Date., October 13, 2016

ValMark Advisers, 3rd Q 2016 Market Update, October 14, 2016

Past performance is not a guarantee of future results. It is also important to note that one cannot invest directly into an index. Diversification cannot assure a profit or guarantee against a loss of value.

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