This Publication Brought To You Courtesy Of:

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CARTER FINANCIAL

CLIENT BULLETIN

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➢ *Website Update*

The Carter Financial website recently received a facelift. In addition to an updated look and feel, there are a few upgrades including access to all accounts held through us using the “Current Client Login” button in the upper right corner as well as access to the past five years of monthly Client Bulletin editions under the “Archived Editions” section of Client Bulletins (this makes fact-checking a snap!) Please take a look at www.stevecarterfinancial.com.

➢ *Continuing Education*

I recently attended a continuing education conference at the Kellogg School of Management at Northwestern University in Evanston Illinois. Topics included how technology is transforming the way we age (consider a mirror in your bathroom with a web camera that monitors your temperature and vital signs); financial planning in the shadow of dementia; potential effects of global debt hitting 235% of gross domestic product; and a healthy dose of investment portfolio construction breakout sessions.

➢ *Brexit Follow Up*

While investment markets interpreted the Brexit vote as a bimodal event, it wasn’t. The referendum was just the beginning of at least a two-year process of negotiations. There are numerous potential paths from here: 1) after seeing the results of the first vote, new leadership could call for a new referendum (this is politically unlikely); 2) negotiations could lead to Britain leaving the EU without the enactment of tariffs and penalties (also unlikely because it would encourage additional anti-globalization movements in other countries.); 3) the most likely scenario, then, is contentious trade negotiations between the United Kingdom and the European Union. Brexit has, figuratively speaking, tossed the economic chips into the air and the tenor of the trade negotiations over the next two years will determine where those chips fall.

➢ *Negative Interest Rates*

As of 6/30/16, there was approximately $11 trillion (in US dollars) of sovereign debt that carries with it a negative yield. Countries issuing negative yield debt include Japan, Germany, Sweden, Denmark and Switzerland. What this means is that investors are willing to loan money to these governments with the guarantee that they will receive back less than the amount they loaned. A personal finance analogy is having a variable rate mortgage on your home and seeing the interest rate go so low that the bank starts PAYING you interest every month! (Source: Fitch).

➢ *Who Would Do This?*

So why would an investor loan money (by buying a bond) and ***pay*** for the privilege of lending it rather than ***receive*** interest as normally is the case. A few reasons some investors may consider buying them:

- **Flight to safety**. High-grade government bonds are classic safe-haven assets. If you believe that every other investment option in the world carries with it the probability of a greater loss than the negative interest rates then you would buy these bonds.
- **No other choice**: Some investors, such as banks and insurance companies, are required to buy certain types of government bonds in order to comply with regulations.
- **Price appreciation**: Just because the yield is negative doesn't mean that it can't go even ***more*** negative. Since a bond's price moves inversely to its yield, even lower negative rates would result in price appreciation of the bond.

If all of this confuses you then you are in good company.

➢ *Why Are There Negative Interest Rates?*

On the other side of the transaction, why are central banks issuing debt with a negative interest rate? Having run out of conventional options, they are attempting to stimulate their country's economic growth by essentially forcing individuals and institutions to put their money to work elsewhere in the economy. So far, this attempt appears to be misguided and ineffective. Negative interest rates reduce the profitability of banks, which makes them ***less*** inclined to make loans, and businesses are less willing to make large investments due to the uncertainty created by monetary policy being in uncharted territory. Negative interest rates also distort the natural flow of capital throughout the financial system which can lead to bubbles and higher inflation.

➢ *Fed up with the Fed*

The foregoing discussion is evidence that the effectiveness of **monetary policy** (which consists of the actions of a central bank that determine the size and rate of growth of the money supply) has reached its limit. Central banks played a role in stabilizing economic growth after the global financial crisis, but they have no arrows left in their quiver to affect economic growth. The next time you hear that Fed chair Janet Yellen is speaking or see an article analyzing every utterance the Fed makes, ***tune it out.*** The Fed grows more and more irrelevant to our nation's economy with each passing day. **Fiscal policy** (government spending and tax policies) that creates a tax and regulatory environment that encourages economic growth is what is needed now but that may be a lot to ask for in an election year.

➢ *Doubled debt*

Our nation's total outstanding debt has doubled over the last eight years. The national debt was just $9.492 trillion as of 6/30/08. As of 6/30/16, the national debt was $19.382 trillion, an increase of $9.9 trillion. This trajectory does not seem to concern the rest of the world. The yield on the 10–year treasury note, which is the interest rate at which investors are willing to loan money to the U. S. Government, closed at 1.36% on 7/8/16, the lowest closing yield ever for the USA's 10-year paper which has been traded since 1790. I guess next to the negative yield on a German or Japanese government bond, 1.36% doesn't look so bad. (Source: Treasury Department).