

“The Third Quarter Revisited”

By Tommy Williams, CFP®

Markets were relatively calm during the third quarter of 2016, yet they delivered some attractive returns overall. In the United States, all three major U.S. indices posted record highs twice during a single 7-day period in August, reported *CNBC.com*. The Standard & Poor’s 500 Index (S&P 500) experienced a 51-day streak without at least a 1 percent decline. The index returned 3.3 percent in the third quarter.



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Investors were fairly complacent until comments by Federal Reserve officials raised awareness the Fed might raise rates during 2016, possibly as early as September. The S&P 500 lost 2.5 percent and the VIX, known as the market’s fear gauge, rose 40 percent in a single day. The upheaval was short-lived and U.S. stocks rebounded quickly.

World markets were moved higher after the Fed opted to maintain its current policy. When the European Central Bank did the same – choosing not to implement further stimulus measures – markets moved lower. Markets were also less than enthused with the plans put forth by the Bank of Japan (BOJ). The central bank will attempt to control the yield curve by keeping 10-year Japanese government bonds at zero percent.

The BOJ’s goal is to push inflation to 2 percent, reported *Reuters*. However, some analysts believe the new policy may be less accommodative than the old one. Experts cited by *Financial Times* said, “On the face of it the BOJ has arguably, by setting the [Japanese Government Bond] curve at its current level, just announced a modest tightening in monetary conditions relative to where they were in the summer.”

Speculation about a September rate hike caused many emerging markets, which have been top-performers throughout the year, to give back some gains late in the quarter. When the U.S. central bank pushes rates higher, emerging market assets become relatively less attractive to investors seeking yield. In addition, a rate hike tends to

strengthen the U.S. dollar, inflating the value of dollar-denominated debt held by emerging countries and potentially slowing economic growth.

Here’s a big surprise for you! Brazil has been a top performer during 2016, despite recession and political upheaval. President Dilma Rousseff was impeached in September. Her successor, Michel Temer plans to enact fiscal reforms he hopes will bring about a mild economic recovery by 2017. Director of Latin America Strategy for Templeton Emerging Markets Group Gustavo Stenzel explained, “We believe Brazil offers a salient example of how political change can accelerate a turnaround in an economy and stock market.”

Worries about China’s economic stability receded during the quarter, *Reuters* explained:

“Recent economic data has shown signs of recovery in China’s economy. Industrial sector profits jumped 20 percent in August, the best showing in three years, while a *Reuters* poll showed manufacturing sector activity likely expanded modestly for a second straight month in September. But many investors remain skeptical about the sustainability of a

recovery that they believe has depended on government stimulus.”

At the end of the quarter, emerging markets moved higher after OPEC announced a preliminary agreement to limit production. It was the first production cut in eight years. The agreement boosted oil and energy stocks in countries around the world.

The fourth quarter of 2016 may be a bumpy one. The U.S. election has the potential to cause some upheaval, as does a rate hike by the Federal Reserve. All we can do is expect the worst but hope for the best. Perhaps we'll be pleasantly surprised. One thing is a given. Markets do not like uncertainty. Right now it is uncertain who will be our next president. That uncertainty will end in November. Perhaps the Electoral College will offer up the candidate with the least undesirable traits resulting in the post-election bounce experienced in prior Presidential contests.

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