October Economic and Market Outlook

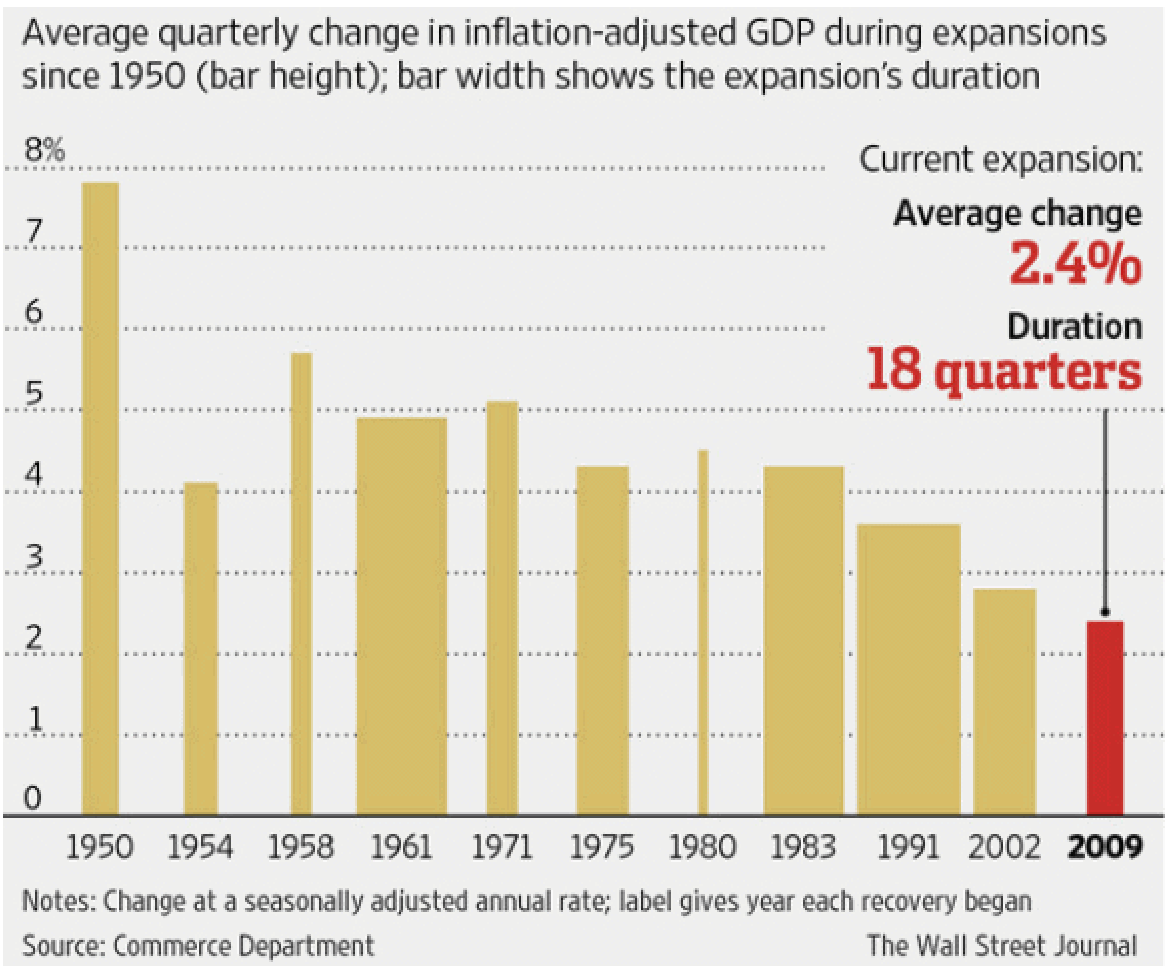
Summary

- The U.S. economy continues to recover.
- The consumer continues to spend.
- Risks are rising outside the U.S.
- Stock valuations are fair to overvalued, and price action looks tired.

October Economic Outlook

The current U.S. economic, business cycle's duration is longer than most, but also one of the slowest.

Below is a Gross Domestic Product, GDP, chart that shows the growth trends of the U.S. economy since 1950:



There are several trends that are important to notice in the above GDP chart:

- Most economic expansions last about 5 years.

- On average, we have a recession about twice a decade. We have not had a recession since 2009.

- The economic expansion of the 1980s was longer than most because baby boomers entered the work force, and started families, and bought their first homes. Many consumer businesses had enormous expansion in the 1980s including: Walmart, Home Depot, Hasbro, CarMax, Limited…

- The 1990s expansion was fueled by the digital, internet revolution. Many technology company's growth exploded during the 1990s: Microsoft, Intel, Dell Computer, Cisco, AOL…

- Notice since the 1970s how each cycle has grown less than the previous. There are many reasons for this. Briefly they include: the law of large numbers (it's hard to grow a $17 trillion economy, the approximate size of the U.S. economy, 3% on a sustained basis) too much debt, a more competitive global economy; baby boomers and millennials (major consumer groups) have changed their consumption habits; changing labor force (outsourcing, technology disruptions, many employees are on variable compensation).

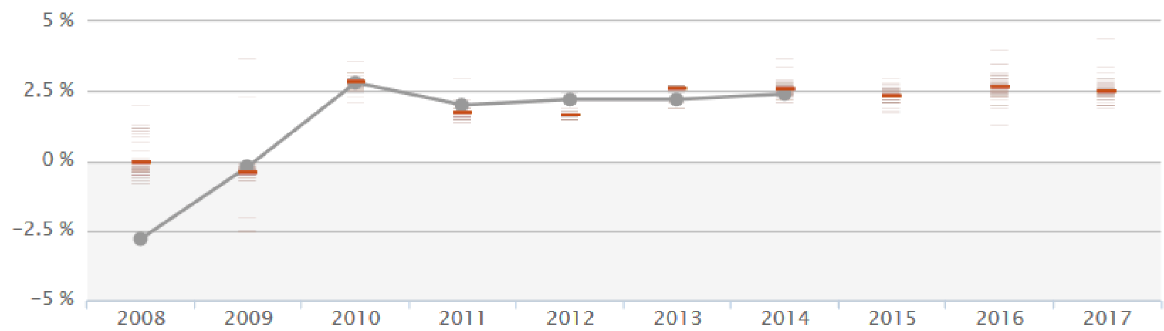
- The expansion that started in 2009 is now about 7 years old, longer than most economic cycles. The current expansion does not have an economic trend that accelerated growth similar to the 1980s, 1990s. The economic trends of the early 2000s were leverage and real estate that ended in the worst economic crisis since the Great Depression.

  The other major trend of the 2000s has been China's emergence as an economic power and the commodities boom. Many economic and investment trends related to China are starting to reverse, and are raising risks to the global economy and markets.

Below is a chart of GDP for this expansion that started in 2009:

GDP (annual)

Actual Estimates 10 yr. 5 yr.



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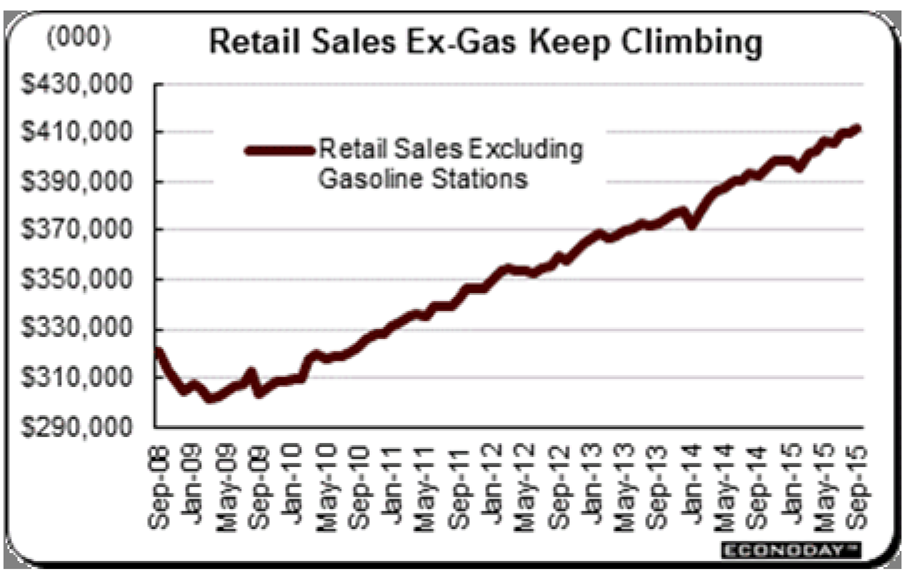
GDP (annual)

Actual (Jan. 2014)	Projected: Jan. 2015	Projected: Jan. 2016	Projected: Jan. 2017
2.4%	2.3% ▼	2.6%	2.5%

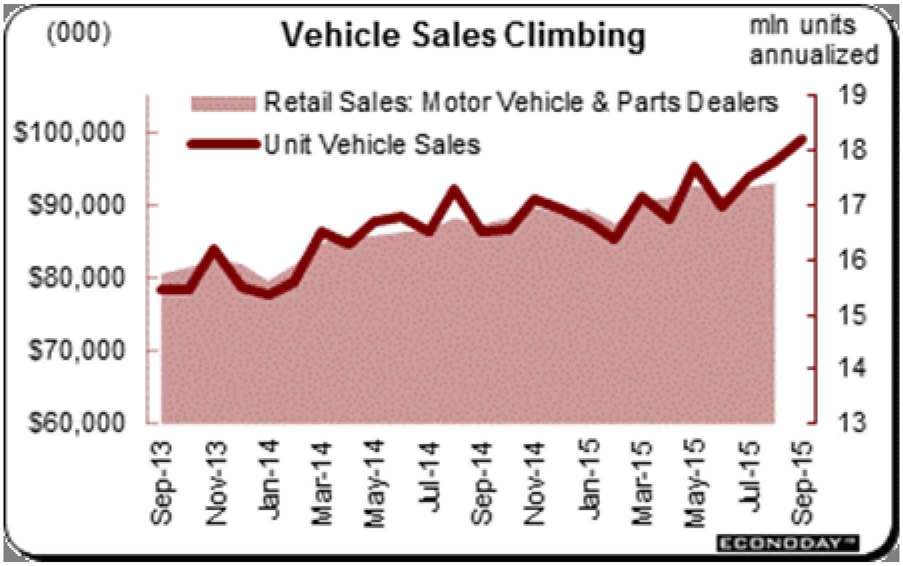
The U.S. economy started its recovery in this economic cycle in 2009. Most economists see the economy continuing to grow for at least two more years.

About 70% of the U.S. economy is consumer and the consumer continues to spend and buy homes and autos.

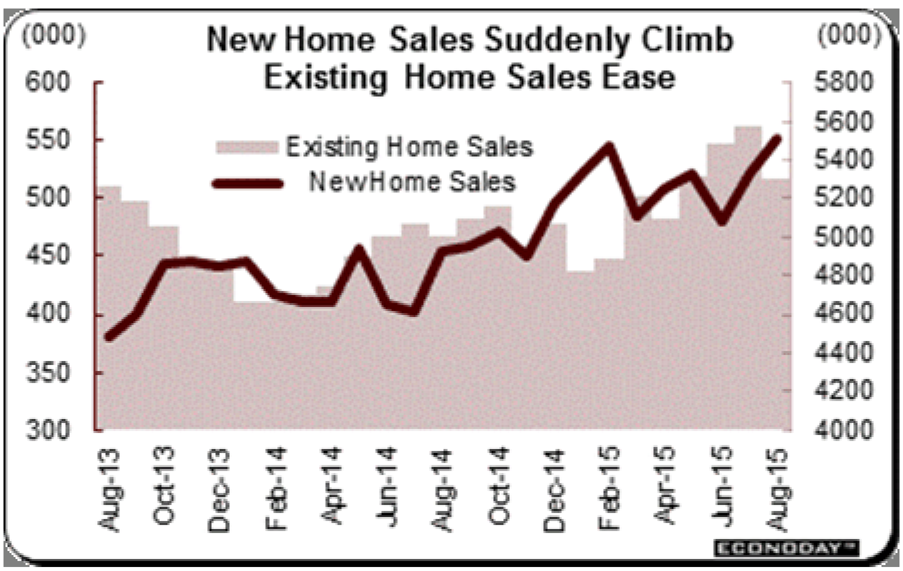
Below are trends for retail sales, autos and housing:



The U.S. economy can normally expect the consumer to contribute to the economy.



The latest auto sales report was 18.2 million, the strongest report since July 2005.



Home sales have picked up. Analysts attribute the improvement in home sales to a potential in a rise in interest rates, and improving labor markets and economy.

October Market Outlook

Below is my monthly forecast for the markets:

2015 FORECAST					
	EARNINGS ESTIMATES	**RISK,GRWTH ADJ P/E**	**FORECAST**	**CURRENT PX**	**PTNTL %**
DJIA	1078	15.5	**16,709.00**	17,217.00	-3.04%
SPX	125	16.5	**2,062.50**	2,030.00	1.58%
2016 FORECAST					
	EARNINGS ESTIMATES	**RISK,GRWTH ADJ P/E**	**FORECAST**	**CURRENT PX**	**PTNTL %**
DJIA	1168.22	15.5	**18,107.41**	17,217.00	4.92%
SPX	132.53	16.5	**2,186.75**	2,030.00	7.17%

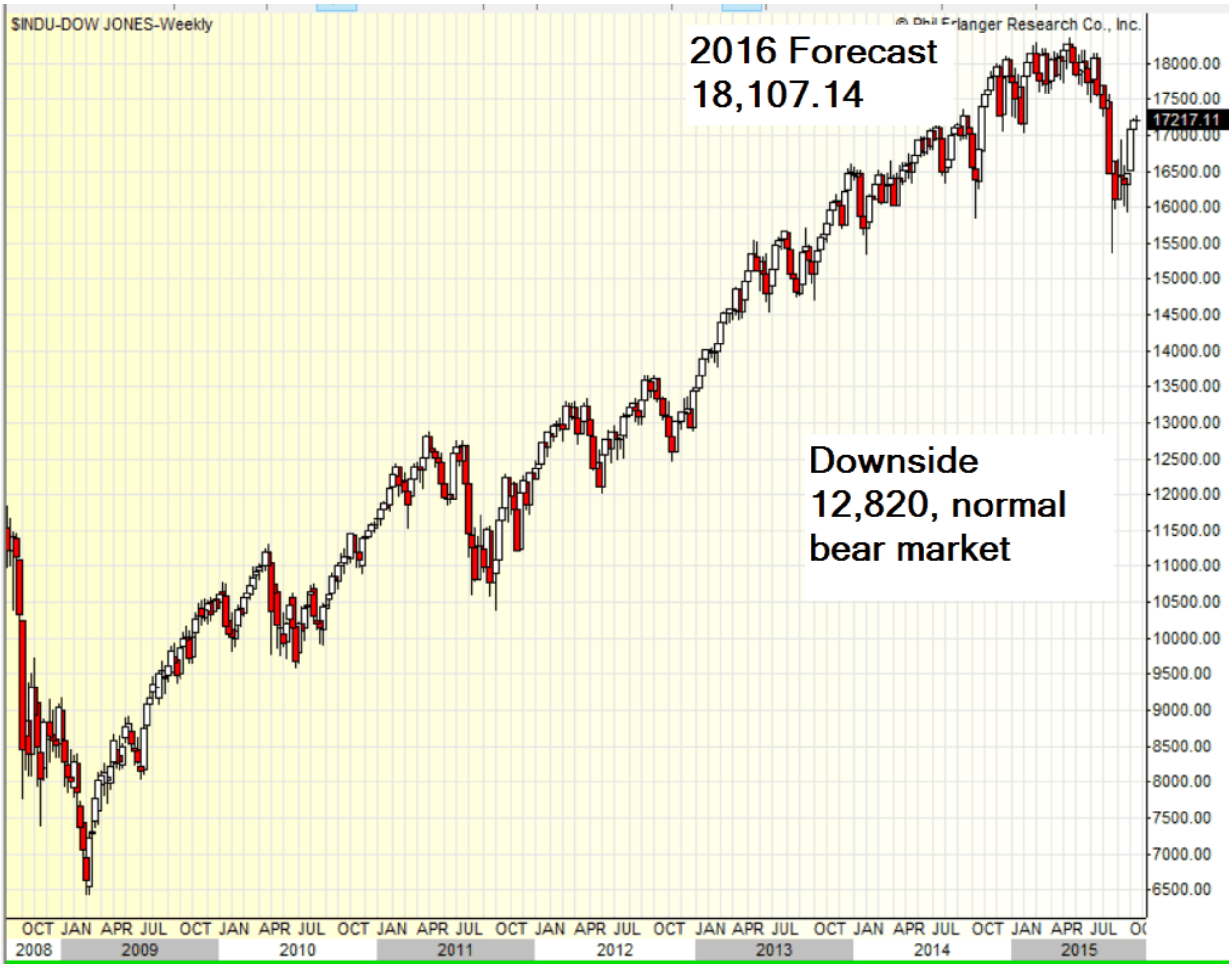
Consensus earnings estimates from Barron’s, Thomson Reuters, Factset

Let’s review my forecast for this month:

- The consensus Dow Jones Industrial Average (DJIA) earnings forecasts keeps falling. In April, the consensus earnings forecast for 2016 was 1,221.61 and the current consensus earnings estimate is 1,168.22, a decline of about 4.3%.
- The S & P earnings estimates also keeps falling.
- I lowered the P/E for this year and next because of the aging market and rising risks.
- Currently the markets are fair to overvalued.
- Next year the S & P has a total potential of about 9% total return (7.17% growth and about a 2% dividend).

It must be said that economists, analysts are not good at forecasting turning points in the economy and markets. Investors do need to use more caution this late in the cycle.

Below is a graphic look at the bull and bear case for the DJIA:



The market bottomed in March of 2009, and has been in rally mode since. Again, this bull market is longer than most, and has more than doubled.

The DJIA is slightly down this year and looks like it's starting to look like it's rolling over, a bearish sign.

If earnings are met, and the P/E stabilizes at about 15.5, the DJIA could move back to this year's high.

Most bear markets average a decline of about 30% from the peak of the bull market. If risks continue to rise, and we go into a bear market, the market could fall to the 12,800 level.

If you would like to meet with our staff to discuss your investments, please call us to make an appointment.