alpha+ capital management

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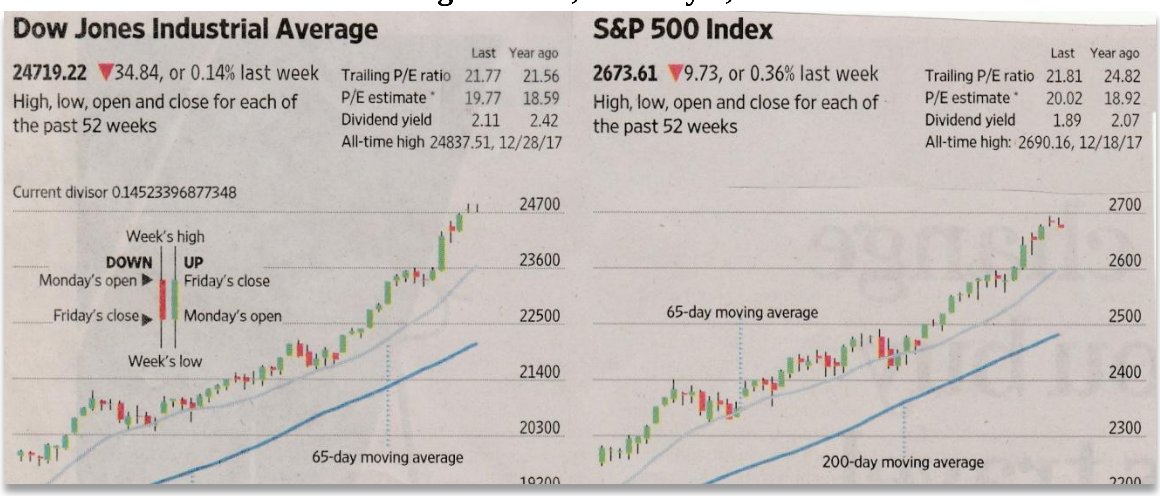
Last year, the S&P 500 Index rose 19.4% and the Dow Jones Index 25.1%, and yet, stocks are not more expensive in terms of 2017 estimated earnings than they were a year ago, and are slightly cheaper in terms of estimated 2018 earnings. The charts below depict the extent and steady advance of stock values through the year.

Wall Street Journal Markets Digest chart, January 2, 2018.



As we turn our attention to the year ahead, it is comforting to find positive elements and lack of stress in both the economy and the investment markets. For example, indicators of a maturing economic expansion and bull market would include an acceleration of wage rates and interest rates. It is logical to expect both to begin to accelerate sometime in late 2018 but our gut feel is that it will be an additional couple of years before they might become worrisome. Important other factors contributing to investment enthusiasm are the substantial decreases in tax rates for both corporations and individual taxpayers and the pending removal of some regulations which tend to suppress economic activity.

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As a second source of stimulation for the months and years to come, we expect the beginnings of a nationwide wave of infrastructure building, in which road repair and other public reconstruction projects get underway, funded largely by federal money. This sort of spending has a powerful impact on economic activity as it energizes the finance, labor, and materials sectors… pretty much the whole economy.

A third category of economic expansion could come from modernization of the US military, mentioned by President Trump on numerous occasions. Apparently, much of the fleet, weaponry and equipment used by our armed forces is old and ready for replacement. On the other hand, the recent termination of ISIS may reduce the need for military capacity.

Ideally, the long term debt of the US ought to be reduced back down from the current 116% of GDP to, say, 95% of GDP, a presumably wholesome level but one unlikely to happen unless a fortuitous sea change occurs in the form of relief from the discipline of our accumulated national debt. If continued slowly enough, the system of moderate overspending financed by borrowing can extend for a long time. The only alternative possibilities would have to be preceded by a change in social attitudes enabling more disciplined control of social welfare programs; and a world transition to more peaceful international conditions as might happen, for example, if the Russian and North Korean governments evolved to where they were no longer military threats. On the other hand, wartime psychology may be a way to focus public attention on wartime stresses instead of getting rid of their home grown dictators.

As we begin the New Year, we are enjoying a political atmosphere in which America is attempting to back away from world problem solving and focus more of its resources on domestic needs. As the threat of communism and aggressive dictatorships continues to diminish, the sanity of democratic power structures and free economies should continue to gain political support and encourage future tax reductions.

Best wishes for a prosperous time ahead.

Sincerely,

John May

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