



# TILDEN

Capital  
Management

An Investment Advising and Financial Planning Firm

Firm Inception 08/03/10

**04/16/14**

## **Quarter in Review**

### **The Markets**

The first quarter of 2014 started with equities selling off 3.5% and long-term bonds rallying 4% in January. Equities rallied back, but long bonds didn't sell off (up 6.55% for the quarter) despite the continued taper from the Fed. The big winners for the quarter were REITs and Long Bonds, with Mid-cap stocks up over 5%. All sectors were positive this quarter except emerging markets, which was down 6.5% in January and just couldn't seem to get back positive with Russia invading Crimea.

Yellen's Fed continued to taper in the quarter, now buying \$55 billion a month down from \$85 billion. However they moved away from Bernanke's quantitative goals for raising interest rates in their minutes of the March meeting. The market reacted strongly to those comments and they have caused a very choppy beginning to April. With more *qualitative* rate guidance, the Fed in my opinion has reduced its clarity, and created more uncertainty. Chairman Yellen went out of her way to make sure the markets knew this did not mean they would tighten monetary policy sooner than stated, offering more in explanation than was probably needed. 2013 Q4 GDP was revised down to 2.6% while Q1 GDP is estimated at 2.0% and Q2 is at 3%. The Russian invasion of Crimea proved once again that a diversified portfolio helps to mitigate unexpected risks. Bonds, US Real Estate and Commodities did very well during the latter half of February during the invasion while stocks sold off significantly. US Politics have for the most part not played a major roll this quarter with the debt ceiling getting expanded to \$17.2 trillion dollars, the fifth increase since 2011, and will keep this topic on hold until March of 2015, and away from election topics.

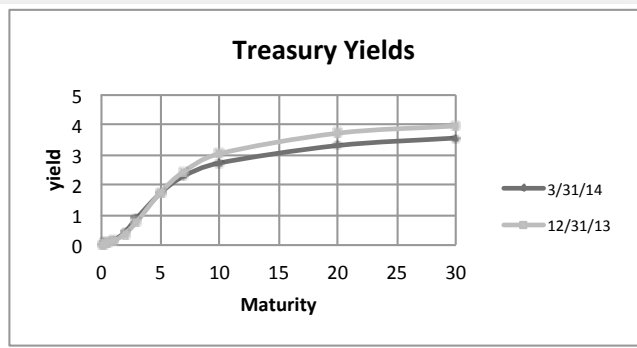
### **Interest Rates**

With the three Federal Reserve Board member nominations still in committee the board is currently only made up of 4 of the 7 governors. Regardless, the Fed has continued to taper its bond-buying program, but interest rates in the back end have remained subdued. In fact from the 5 to the 30-year treasury, **interest rate have all declined** over the first quarter. The Fed has purchased close to 50% of the treasury issuance in the back end of the curve along with over 100% of the issuance (and has since September of 2013) in conventional 30yr mortgages issued by FNMA an FHLMC. It is also buying 15-year conventional mortgages and GNMA issuance to hold the mortgage rates down.



With the addition of the unrest in the Ukraine interest, interest rates have tightened an average of 37 bps in the 10 through 20-year treasury rates. The 30-year fixe rate mortgage rate is around 4.4% while the 15-year is 3.4%. Refinancing levels have dropped off substantially as the MBA (Mortgage Bankers Association) Refinance index continues to fall.

Years	3/31/14	12/31/13	Difference
0.08	0.03	0.01	0.02
0.24	0.05	0.07	-0.02
0.5	0.07	0.1	-0.03
1	0.13	0.13	0
2	0.44	0.38	0.06
3	0.9	0.78	0.12
5	1.73	1.75	-0.02
7	2.3	2.45	-0.15
10	2.73	3.04	-0.31
20	3.31	3.72	-0.41
30	3.56	3.96	-0.4



## Leading Economic Indicators

The Conference Board's leading economic index increased in both the first two month's of 2014, up 2.7% for the past six months. My concern is the diffusion index is at 50 and has been for the past two months. This means that even though the index continues to show leading indications of growth it is only coming from half of the ten components. Hopefully we will see a reversal of this trend and more of the components will contribute positively this month.

## Jobs

At the time of this write-up **nonfarm payroll** posted and increase of 192,000 jobs, not too far from consensus. There were also positive revisions to January and February. We have gained 2.0mm jobs over the past 12 months, and the unemployment rate now stands at 6.7% (unchanged since December). The household survey, the survey used to calculate the unemployment rate, added 476,000 jobs in March. The only way the rate could have stayed the same was if the denominator increased as well, and people rejoined the potential workforce.

The **4-week moving average of unemployment claims** is **316,250** as of the time of this write up. Claims continue to fall toward pre-recession levels. The ISM employment survey however has been dropping and currently resides at 51.1 just above the inflection point. We are less than 500,000 jobs away from pre-recession job numbers, but the Fed is trying to back off quantitative data points for increasing the Federal Funds rate target. If the employment



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situation is recovering, the stock markets are at all time highs, and the real estate market is recovering, then why are they still so concerned? Are they always going to be the last one to leave the party?

## **Production**

Industrial production had a stronger Q1 than Q4 2013 after the downward revisions to Q4. Up 1.7% this quarter compared to 0.8% for Q4. Manufacturing employment growth though continues to slow year over year adding only about 80,000 jobs to the sector over the past twelve months. But we are still over 1.6 million jobs away from pre recession levels. Looking at the total jobs from both the Nonfarm and Household surveys we are only 500,000 jobs away from pre-recession levels. Which means that not only are we net negative for manufacturing jobs but it would take the next 21 years to recover those jobs at the current annual rate! At this point it just looks like average weekly hours of the existing workers are increasing along with capacity utilization. Productivity and increases in the labor pool aren't the cause of industrial production growth.

## **Housing**

Downward revisions of census bureau's annual new home sales reduced sales by 10% for November and December combined. The five-month average and the February reported number is 440,000 new homes sold. Even though interest rates declined over the past quarter it looks like new home purchases are leveling out. Existing home sales have fallen off as well, down 5.5% since December ending February, and 12.5% since September. The S&P/Case-Shiller Home Price index was down slightly for the 4<sup>th</sup> Quarter of 2013 but up a total of 11.3% for 2013. The Fed is doing its best to keep mortgage rates accommodative (as it is the entire mortgage market anyway), but the market is definitely slowing, in both price appreciation and building. From 1990 until the recession in 2008 the percentage of single-family housing starts to the total housing starts was around 81%. Since the end of the recession the average has been 73% with the most recent number at 64%. Looks like we are building multi-family.

## **The Consumer**

After the US government reopened its doors last year the consumer confidence numbers increased. But they have stayed at December levels or only slightly better in the first quarter of 2014. Despite a very harsh winter consumers viewed their personal finances better than they had in the beginning of the year. But durable good purchases and home purchases declined as consumers started to look much deeper at the affects of potential interest rate increases. Real personal consumption expenditures on durable goods were only up 2.7% year over year ending February. This is the lowest level since August of 2010.

All of the personal income and outlay data was pretty good for the start of the year. Even Real Personal Income less transfers was up year over year ending February. The savings rate is holding pretty steady in the low 4% area



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while the borrowing growth rate seems to be slowing slightly on a year over year basis. While the revolving/credit card portion of consumer credit is still well below pre-recession levels, the total and non-revolving/student loan/car loan portion is well above it. It still amazes me that we as a nation continue to borrow to purchase education products that don't lead to jobs that can justify the education's cost (and debt) in the first place. We are failing over and over again to recognize the return on this investment does matter and that all college educations are not created equal.

## Inflation

As of March CPI was up 1.54% annually while PCE was only up 0.87% as of February. Over the past twelve months the average annual rate was just 1.4% for CPI.

## In Closing

We are now **57 months** into an economic expansion with the **average expansion being 42 months** for the past 33 cycles. The Fed's taper continues but their purchases still make up over half of the Treasury supply and over 100% of the mortgage supply in most issues. Leading indicators are holding, but only half of them are supporting the growth. The employment picture looks the same albeit with a stationary unemployment rate, but the Challenger Intended Dismissals index was at the lowest Q1 level in 20 years. Personal income and expenditures are up year over year and consumer confidence is up. Looking at the current reported economic statistics I believe there is still less than a 17% change of contraction. Therefore I may make some tweaks to the allocation but no large shifts out of risk assets.