



# SOUND INCOME STRATEGIES

## July 2016

Index	Month / Year to Date
Dow Jones	+2.39% / +7.25%
S&P 500	+3.56% / +7.56%
NASDAQ	+6.65% / +3.80%
10yr Treasury	1.45% end of July; 1.47% beginning of July

### Markets:

Well, the British Sterling Pound has not bounced back to its pre-British exit from the European Union position, but everything else continues to appreciate. Last month, we warned of European and Asian capital flowing into the U.S. Markets – both equities and bonds – and as expected, this has been the case, pushing our equity markets and bonds markets way up. While this assists our total returns for the year, it makes it difficult to purchase fixed-income securities for new money that needs to be invested for income purposes. As we stated many times, fixed-income securities, unlike equities, have a price ceiling; otherwise, you would enter into a negative rate or yield. Given this drawback for fixed-income securities, we are forced into purchasing funds, or ETFs, as a temporary substitute for individual bonds.

An example of this scenario was our purchase of iShares High Yield Corporate bond ETF; ticker SHYG. This is an ETF that holds short-term, high-yield corporate bonds – many of which are private placement or 144(a) bonds. These corporate bonds are purchased by large investors and institutional buyers, and the only way we can get exposure to these higher yielding bonds is through a fund or ETF structure. This ETF is paying us 5.8% currently and is helping to bring in a very difficult interest rate environment. While we preach holding individual bonds over funds and ETF's, given the record low in interest rates, we need to utilize assets that are currently available for income.

While the Fed didn't increase rates at the July meetings, they did "toughen up" the language in an attempt to make markets believe that they'll increase the Fed Fund's rate before the end of 2016. If the job market and consumer spending numbers hold or increase, it's actually possible they will increase by 25 bps before the end of the year. However, we still believe the Fed is in a tough position, because if they increase rates, it could cause the yield curve to flatten and reduce bank lending. The yield curve (a graph that plots the yields from shortest to longest maturities) has flattened a bit during July. If the Fed does end up increasing short-term interest rates and the middle and longer maturities hold their levels without increasing as well, we could see a flat to possible inverse yield curve. A flat or inverse curve usually reflects an economy that is in serious trouble because growth has not only stopped, but reversed course.

*"What goes up must come down"* — Sir Isaac Newton

Though he was talking about gravity, it does apply to economics as well.

From mid-February until the beginning of June, crude oil had a nice run from roughly \$35 per barrel to \$52 per barrel. Oil has since sold off, is down -15% for July, and currently rests at \$40 per barrel. This is causing energy names to sell off in equities and bonds. Though we don't see oil/gas commodity prices increasing material higher in the near future, this could be an opportunity to pick up or swap into other energy company bonds that have an improving situation.

### Disclaimer:

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