The Financial Navigator – June 2015 Newsletter

With the presidential election a little over a year away, the political season has been heating up and there has been a lot of talk about income inequality and 'one percenters'. The first article below, *The Upper Uppers*, summarizes what it take to belong to this exclusive club. What is interesting is how low the bar of entry is in certain states; you don't have to be Warren Buffet or a Wall Street banker to qualify.

What's Next for Oil Prices? discusses the historical drop in oil prices we have experienced over the past year and whether the era of cheap oil is over. The final article, *The Harm in Financial Journalism*, offers some thought provoking ideas on why the news and data supplied by consumer journalists is almost always harmful to your financial health.

Enjoy the first month of summer, and as always feel free to forward this email to anyone that may share your interest, and let me know if you have questions about a specific situation.

Sincerely,

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The Upper Uppers

What does it take to be a "one percenter?" How much do you have to earn before you fall into this rarified zone?

A new study written by socioeconomists Estelle Sommeiller and Mark Price, looked at state-level tax data from the Internal Revenue Service over the past 35 years. Their research reveals that if you live in Connecticut, you're a "one percenter" if you earn more than ($678,000) a year, higher than New York's threshold of ($506,000), the ($539,000) threshold in New Jersey, ($555,000) in Washington, D.C. or ($532,000) in Massachusetts. California ($438,000) and Texas ($423,000), which are considered wealthy states, actually came in behind North Dakota ($502,000).

States with the lowest threshold include West Virginia ($243,000), Kentucky and Alabama ($263,000) and Maine ($274,000). New Hampshire comes in at ($365,000) and Vermont at ($299,000). If somebody earning a good income in Connecticut or New

York wanted to break into the one-percent category, he/she could move to a less competitive state.

Nationwide, the total share of income going to the upper 1% rose by about 12 percentage points since 1979. The one-percenters in Connecticut make a little over 33% of all income in that state, and in New York, the percentage is 32.6%. Elsewhere, the range is generally in the 14% to 22% range, up from the 7-11% range back in 1979.

So it isn't just hedge fund managers and Wall Street bankers that fall into the "one percent" zone and where you live really dictates whether one qualifies.

What's Next for Oil Prices?

Last year, the big news in the U.S. economy was the dramatic fall in Brent crude oil prices, from just under $110 a barrel last July to something less than $45 a barrel in mid-March. Since then, oil prices have jumped back up to more than $60 a barrel. Does that mean the era of cheap oil is over?

Probably not, say the experts. Bill O'Grady, at Confluence Investment Management, points out that U.S. energy production, when you add 9.2 million barrels per day of oil production to 1.0 million barrels per day (equivalent) of natural gas, is the highest it has ever been, even higher than the production levels during the OPEC oil embargo in the 1970s. Meanwhile, Saudi Arabia appears to be pursuing a multi-pronged political agenda by keeping its pumps working overtime: when the world's largest oil exporter drives down the global price of oil, it harms the economies of Russia and Iran (which need higher oil prices to prop up their domestic economies) and also discourages even higher oil production in the U.S. At the same time, the Saudi effort to suppress oil prices also suppresses the economic drivers of alternative energy, by making solar and nuclear power seem expensive compared with oil-generated electricity.

Meanwhile, more oil is on the way. Iran's oil minister recently announced that if/when sanctions on the country are lifted, it will raise its oil production from 2.7 million barrels a day to four million over the subsequent eight months.

The recent Confluence report also offers a couple of very interesting statistics. First, the average citizen of planet Earth consumes about 4.7 barrels of oil a year in energy use. That in itself may not be surprising; what is striking is that this number has barely fluctuated since 1983, and is down from 5.3 barrels in the late 1970s. There are huge differences among countries. U.S. citizens, on average, consume 21.8 barrels a year, while the average Chinese resident consumes 2.9 barrels.

The other interesting statistic is the declining amount of energy required to produce an inflation-adjusted dollar of economic production in the world. In 2013, the most recent year this data has been collected, the figure was the lowest it has ever been, and is more than 50% lower than in 1980. The world economy, in other words, is at least 50% more efficient in its energy use than it was 30 years ago, and that efficiency has been increasing steadily over that three-decade period. Last year, European oil use hit its lowest level since the mid-1990s, and U.S. oil demand peaked in 2007, and is expected to fall by between 1.8 million and 2.7 million barrels a day by 2035. In an op-ed piece in the Wall Street Journal, economist Steve Yetiv says that as economic growth becomes increasingly disconnected from oil in the next 20 years, attention will shift to scarcities in food, water and minerals.

None of this guarantees that oil prices will fall back to their mid-March lows, but it does suggest to energy experts that the recent rise in prices won't take us back to last year's $100+ prices either. Yetiv speculates prices in the range of $52 to $68 a barrel for the foreseeable future. Translated, that means the days of (relatively) cheap oil could be with us for a while.

The Harm in Financial Journalism

In most areas of our lives, the more information you get, and the more up-to-the-minute it is, the better we can do business and make astute decisions. It is interesting that investing is one area where the opposite is true.

We're not talking here about the second-by-second blips on a Bloomberg terminal that traders and computer algorithms use to make quick-twitch buys and sells. We're talking about the normal news reports, cable TV investment reports and investing articles that you're bombarded with on a daily basis. In general, the news and data supplied by consumer journalists is almost always harmful to your financial health.

How? Consider profiles of mutual funds and mutual fund managers. The quarterly profiles in Barron's and the articles in Money, Kiplinger's and the Wall Street Journal tend to focus a bright spotlight of attention on the hot funds—that is, funds that outperformed their peers (and the market) in the previous quarter. Three months worth of track record is statistical nonsense, but the hot fund manager is interviewed with breathless deference normally given to a certified genius. It is interesting that seldom if ever is the next quarter's genius the same as the last one. Anyone who invests with the fund of the hour is in grave danger of suffering a regression to the mean—which means losses when compared with the indices.

Even one-year and five-year rankings have no predictive value, particularly when the focus is on outliers who were well ahead of their peers. Meanwhile, when we aren't reading about hot managers, we're hearing about what the stock market did (or is doing) today. Today's price movements are, to a statistician, meaningless white noise, indicative of nothing remotely significant about the future. The markets go up today, down tomorrow, up for a week, down for a week, and during each of these time periods, analysts try to tell us the causes of these random bounces. They would be more productively employed trying to explain the "causes" behind each of the waves in the ocean, yet we can't help listening to their plausible explanations as to why this earnings report, that jobs report, or some other speculation on what the Federal Reserve Board will or will not do has affected our investment outlook.

And, of course, at market tops, when new money is chasing returns at the most dangerous possible time, the news reports are telling us how the markets have been going up, up, up. When markets are depressed, and it is the best possible time to put new money to work, the news reports are telling us all the bad news about months of market losses. Swimming against that tide is nearly impossible, even for professionals.

There may be meaningful information among this chatter, but it's unlikely that most of us will see it amid the noisy background. Back in the late 1990s, one analyst who couldn't believe how much people were paying for tech stocks finally broke through the background noise by pointing out that Amazon's share price had reached approximately the same level as the entire yearly economic output of the nation of Iceland, plus a few 747 cargo jets to carry it all back to the U.S. Of course, few listened, and the bursting tech bubble cost a lot of investors a fortune.

Today, we're being told that the current market rally is long in the tooth, that the Fed is going to raise rates soon, that market valuations are kind of high, and of course that certain fund managers did really well last quarter and yesterday's market was up or down. The problem is that we were hearing exactly the same things last year and the year before (remember?), and still the market churned ahead, cranking out new record highs.

Unlike just about any other activity you might pursue, the best, most astute way to invest is to turn off the noise and let the markets carry you where they must. The short-term drops tend to become buying opportunities in the long run, and over time, the U.S. and global economies reflect the underlying growth in value generated by millions of workers who go to work each day and build that value. Investor sentiment will swing around with the unhelpful prodding of journalists and pundits, but people who stay the course have always seen new market highs eventually, while people who react to every positive or negative report tend to fare much less well. When it comes to the markets, wisdom trumps up-to-the-minute knowledge every time.

Maybe somebody should tell that to the journalists.