The Chance Financial Quarterly

Well, here we are nine months through 2024. Feeling older? Can you believe 2025 will be here soon? And what's more, we will have a new president. I don't care who you prefer, this election will change things, but, we'll survive. As usual, commentators are saying this is the most important election ever. What a silly statement when you know that each new election will surpass the last one to be called "the most important election ever." But for sure, presidential elections are important and lest we forget, our Senate and House elections are almost as important. So are the state and local elections. Please vote.

Making Sense of Markets and the Economy

If you invested in the stock market, your money is doing well. Interestingly, the S&P 500 hit a snag in early August. I was on a cruise ship and tried my best to miss the news, but alas, I got on LinkedIn and people were spazzing out over a large downward move one day. You might have been worried too. But as I told my LinkedIn contacts, the smart money is staying invested for the long run. It's the dumb money that chases short-term gains and losses.

And after that horrific but brief period in August, the market recovered and overall, it went up 5.5% in the third quarter, leading to a year-to-date gain of almost 21%. Does that sound like investors are worried about the election? Frankly, I do not think whoever wins the election will trigger a big stock market move, but we'll see on November 6.

To be perfectly honest, I think the market is up a bit too much, and I wouldn't mind seeing it stay in its tracks for the rest of the year. The economic fundamentals just do not look strong enough. Remember the market moves on average about 10% a year. To have it already over 20 is unnerving. Yes, strong market performance is unnerving. To me, at least.

The big happening in the quarter was the Fed's slight release of its usual iron grip on interest rates. It cut the Fed Funds rate by ½ point to 4.75% in mid-September. This rate is the rate that banks borrow money from other banks. When it goes down, banks are able to lend more. The Fed had been keeping rates up, and they still are abnormally high, to try to cool off what it thought was an overheated economy. It wasn't overheated, but that's another story. But this rate cut will lower the rate on your money market funds and newly purchased CDs.

Inflation has been the defining economic characteristic of Bidenomics. It has cooled a bit to the 2-3% range. The Fed has always said it wants inflation around 2%. So, we still have a ways to go, but it's better than the 9% figure of a few years ago. BTW, the Fed's target of 2% is too high in the opinion of many economists. Remember that inflation is a tax that especially hits the poor. At least with actual taxes, we get government services. Inflation is simply erosion. It is universally bad, and economic policies that lead to it are the worst things government can do.

Unemployment during July, August, and September was in the 4.1-4.3 % range. This is fine in comparison to the long run, but we should never settle for numbers like this.

GDP, which I have stated is grossly overrated, came in during the second quarter at 2.8%. Economists make like this is ok, but not great. You know, not bad, but not good. As I have explained awhile back, GDP fails to pick up the enormous economic activity of an economy that focuses on services, technology, software, intelligence, and all the things that aren't easily measurable in corporate balance sheets.

And let me remind you of what really matters: national wealth. From 2Q=2022 to 2Q-2023, this country created $12 trillion in wealth, a rate of growth of over 8%. You may not feel rich yourself, but wouldn't you rather live in an economy that is creating wealth at a rapid rate?

So, please don't believe political pundits on both sides who tell you that the economy is terrible or the economy is doing well. It's kind of in the middle. Your money is doing well, but remember that the prices of stocks are based on horizons that are much longer than a president's term. Stay in the market with broadly diversified index funds, and maybe consider locking in some CD rates before the Fed brings rates down even more.

A Teaching Moment: What Exchange Rates Mean and Why They Matter

I was recently traveling in Spain and met an American who asked what I did for a living. I told him I was a finance professor. We chatted a bit, wrapped it up, and then I walked away. He then said, "Hey? Can I ask you a question?" I said "sure." He said, "Where do you get the best exchange rate?" I, of course, neither know nor care, as the differences are not that great. I suspect one will spend more time searching for a better exchange rate than is worth it. All travelers seem to do this and talk about the savings from always converting in the foreign country and in particular using your credit card or ATM.

Just remember that this advice comes from travel writers and business magazines and sites, who just repeat what they've heard. I have seen no reliable controlled studies that compare these rates simultaneously. That would be the only way to know for sure.

Unless you are exchanging a lot of money, just do the most convenient thing. It's not worth the difference. Except, …, never change money on the street or with private local vendors known as cambios. Always use a financial institution.

And be aware that you will have a buy rate and a sell rate. They will differ and quite substantially, because that is how these companies make money. It's your convenience so expect to pay.

The really important thing is that exchange rates matter greatly to our economy. And most people don't understand why.

I suspect most readers know that the exchange rate is the number of units of a currency you can get for a dollar, or, flipping it over, the number of dollars you have to fork over to get one unit of the currency. If the exchange rate for the euro is $1.05, it means that $1.05 will buy you one euro. Or the inverse, 1/1.05 = 0.9524 euros will get you a dollar. For this note, I will use the euro and quote it in terms of dollars.

So, let's say the euro is $1.05 but over a period of time it goes up to $1.30. That would be described as a weak dollar or strong euro. If it drops to say, $0.75, it would be a strong dollar and a weak euro. We hear a lot about these terms. But do we know what they mean?

Now, what causes a strong dollar or a weak dollar? A currency strengthens when the demand for its products and services by other countries increases. Also, an increase in the level of interest rates increases demand for the currency, whereby more foreigners put more money into banks to earn that higher interest in that country. Likewise, a stronger stock market makes a currency stronger. There is no single dominant factor, and it is hard to identify, what more explain, why a currency is strong or weak.

So, I ask you, do you want a strong dollar or a weak dollar? It's not about patriotism. A strong dollar is not the same as a strong country. A strong dollar means that the country's products and services are expensive. That reduces demand by foreigners. Not good.

In addition, a strong dollar means that when American companies make profits abroad and bring that money back to the U. S., those profits are reduced by the strong exchange rate. That's why you will hear U. S. multinational companies complain about a strong dollar.

I don't particularly like the term "weak dollar" or "cheap dollar." It sounds bad. But that is like saying that Walmart's "always low prices" is a bad thing. Most people view inexpensive as a positive.

Sure, when we have a weak dollar, it will be more expensive to travel overseas. That is a cost we pay for the fact that we are then selling more goods and services to foreigners. Do you want us to sell more to them than they buy from us? Frankly, I prefer the latter.

You can't have it both ways. But a weak dollar is really better. I just wish we had another term for it!

See you in January.

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