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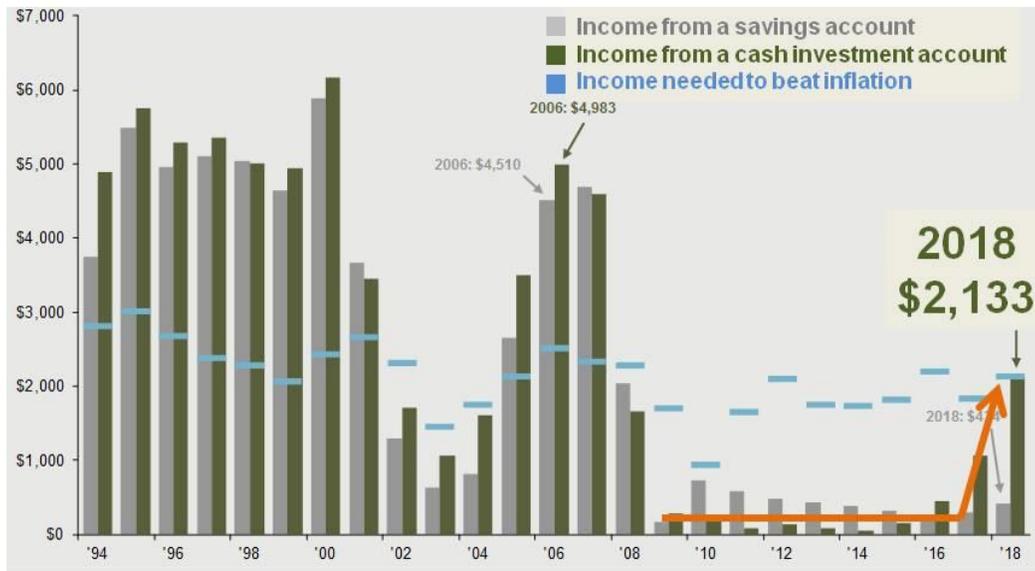
October 11, 2019

**Why So Much Cash? Because It Makes Cents**

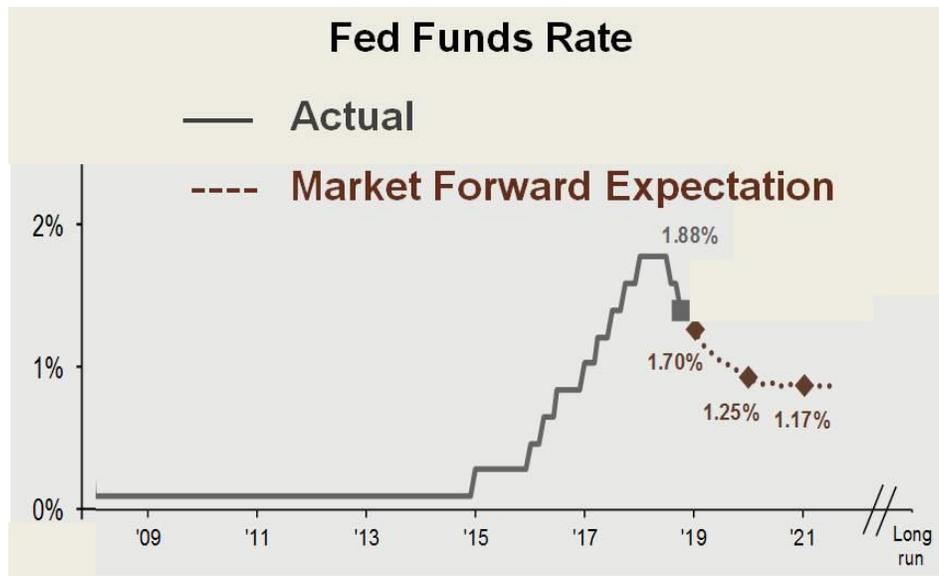
The U.S. Federal Reserve recently reported that there is roughly \$20 trillion in cash and equivalents in overnight money market funds, checking and savings accounts and certificates of deposit. This amount of cash is worth nearly half the value of all U.S. traded stocks.

Short-term cash, properly invested, is making anywhere from 1.7% to roughly 2.3% (income on cash in savings accounts remains near lows). Long-term, 10-year U.S. treasury bonds offer less at about 1.6%. After years of nearly a zero-rate return on cash, a 2%ish return is a significant improvement and is keeping pace with inflation.

**Income on \$100K, Cash Accounts**



The current Fed Funds rate is roughly 1.85%. Market expectations are for this rate to decline to roughly 1.2% in the next 18 months. As the Fed Funds rate declines, we expect interest earned on savings accounts will also decline.



What if the rates on short-term cash were to drop to 1.5% or even 1%?

Last week, *Delta Insights; Pinball Between Low Rates and Slowing Growth* talked about how the stock market is caught between a low interest rate and a Chinese tariff place. This week, we explore the interest rate side of this box which is currently offering support for stock prices.

Stock prices are fundamentally determined by discounting future earnings back to a value today. The discount rate includes both a risk-free rate and a risk premium. The logic is a stock investor should receive no less than the risk-free rate plus a risk-premium for investing in a risky asset.

## Present Value Formula

$$\text{Stock Prices Today} = \frac{\text{Future Earnings}}{\text{Risk-Free Rate} + \text{Risk Premium (anxiety, uncertainty)}}$$

The consensus analyst estimate for S&P 500 earnings in 2020 is roughly \$182. The average risk-premium for the past twenty years has been 3.7%. If we plug a 1.5% risk-free rate into this equation, we arrive at an S&P 500 valuation of 3,500. The math

suggests the S&P 500 could rise by about 20% over the next year if earnings expectations hold up, the risk-premium remains near its average level and the risk-free rate declines to 1.5%. At a 1% risk-free rate, the same math shows a potential 34% gain in the S&P 500 over the next year.

What could go wrong? What could go wrong is a continuation and/or escalation of the trade war that further slows global growth and causes future earnings to decline. Analysts have been revising down the 2020 earnings estimate ever since the trade war began. This trend is unlikely to change until the trade war negotiation moves in a more positive direction. Hence, the market finds support on low interest rates and resistance on negative trade war news.

During this period of uncertainty and volatile, range-bound trading, the Delta Market Sentiment Indicator (MSI – an intermediate-term trend indicator) remains bearish.

### **Give Us a Call Today**

We have unique and sophisticated investment methods that seek to capture the stock market's gains while minimizing drawdowns in bear markets. If you would like to learn more about how we manage money, we invite you to give us a call at **(415) 249-6337**, visit [www.deltaim.com](http://www.deltaim.com) or email us at [info@deltaim.com](mailto:info@deltaim.com).



*“As soon as the overseas markets stabilize, then yes, you can get a puppy.”*

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# Delta Stock Market Dashboard

MARKET SENTIMENT IS

**BEARISH**

THIS WEEK'S NUMBER IS

**37.5**

Our technical indicator decreased  
this week from 46.0 to 37.5

## INDICATOR STATISTICS

Consecutive Bearish Weeks:	2
Cycle Inception Date:	10/4/2019
Range:	37.5 - 46.0
Mean:	41.8
Bullish Weeks YTD:	26
Bearish Weeks YTD:	15
*S&P 500	-0.5%
*DJIA	-0.3%
*NASDAQ	-0.5%

\* Percentage change during current cycle



(Delta MSI is published every week in *Barron's*)

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