TRIVETT WEALTH MANAGEMENT

> *"Bull markets do not die of old age. They die of excess — overspending, overleverage, overconfidence"*
> -Ryan Detrick, Senior Market Strategist LPL

The overarching theme of my 2017 year-end client newsletter was that at some point the "endless gifts of dramatic stock market gains" will become, let's say, not-so-endless. Well, it looks like we have arrived at that point. While we haven't seen a major downturn this year, other than a temporary pullback of 10% - a technical correction of sorts – **the drunken-sailor-style runup is clearly over**. Also central to the newsletter was the likely emerging volatility in 2018. This too has officially happened as evidenced by the VIX, which peaked near 37 during early February, and has brought with it angst for the *check-my-account-three-times-a-day* investor, and great opportunity for the *dollar-cost-averager.*

BY THE NUMBERS

So here is where we find ourselves at the 2018 midway point. The flagship S&P 500 is up 2.6% while Foreign Stocks pulled back 2.4%. US Bonds were down 1.6%, and the 10-year Treasury declined 2.7%. The best performing sectors were Consumer Discretionary 11.5% and Technology 10.9%. The worst sectors were Consumer Staples 8.5% and Telecommunications 8.4%. GDP was at 2% through March 30 and unemployment was at an encouraging 3.8%. We did see a 10% correction that lasted thru early March, but we only stayed there a few days before things swung back. Hence, Nick Murray cleverly dubbing it ***"the little correction that couldn't"***

CONCERNS

Bond Market

By all measures, fixed income has been the primary laggard of most client accounts. This is simply the result of rising interest rates. It is fairly safe to assume that rates will continue their climb, as all but plainly stated by the Federal Reserve.

Despite this likelihood, I still advise owning bonds as part of a healthy diversified portfolio (although one should keep an eye on duration). Aside from the fact that I am a militant non-market timer, there remains tangible value in owning fixed income. First, **bonds continue to offer a non-correlating style of diversification from stocks**. Did you notice that bonds did relatively well during the S&P's short-lived correction in February? I did. Historically, bonds tend to go up when stocks go down, and vice versa.

There's value in that. If equities were to suddenly fall out of bed, bonds may very well keep a portfolio afloat during the drop. The other reason we still need fixed income (or any other temporarily declining asset class for that matter) within our diversified portfolio, **is that it can create rebalancing opportunities.** Any time a holding within a portfolio goes up or down, it creates an opportunity to sell off, or buy more. For example, if XYZ stock was $10 per share yesterday but is $7 today, you better believe that under normal circumstances I'm going to buy more while it's on sale. On the other hand, if it goes up to $14 per share next week, I may consider selling some. Do you see? For the long term disciplined investor, it's typically a good thing when a holding declines in value, and even better for the dollar cost averager!

Tariffs

There's no question that the Administration's posture regarding import tariffs has not been warmly received by the markets. I honestly don't know what to think about this. On one hand I understand the fairness doctrine that Administration espouses, but at the same time, having a trade imbalance is not implicitly bad, nor is it a reliable metric for assessing a nation's fiscal health. Many countries, such as Russia and Brazil, have trade surpluses yet their economy is nowhere near as stable as the USA. Think about it on a micro level. I have a trade imbalance with my grocery store. I "import" their goods weekly in exchange for cash. I am therefore, in a perpetual trade deficit with Kroger and Aldi (incidentally, my all time favorite grocery store). But is this bad, and do I care? Of course not. Our relationship remains mutually beneficial, despite our ongoing "trade imbalance." I get my groceries, they get my cash. We both part ways smiling.

Ultimately, we probably won't wind up being entangled in an all-out trade war. It's my opinion that what we are experiencing is political rhetoric that will soon die down. But I could be wrong. And if we do end up battling with other world economies it will not be good for the markets in the near term.

Interest Rates

Interest rates are stable . . . for now. But if we see inflation - which by the way was 2.8% in May - begin to increase, the Fed may ratchet up the Federal Funds rate (as well they should). Thus far, I've been complimentary of the Fed's actions. It seems to me that the velocity of rate hikes has been appropriate. Nevertheless, it's something to keep an eye on.

Student Loans

I opted to comment on this only because so many of you are physicians with sizeable student loans. When I began working with doctors, somewhere around 2006, the average student loan debt of ETSU Quillen College of Medicine's graduates was around $180,000 (at least this is what I remember from a conversation I had with someone in the financial aid department). Now <u>I routinely see medical school loans between $300,000-$500,000</u>. And pharmacy school debt isn't much better. Plus, this is all in the face of Stafford and Grad Plus rates floating between 6%-8.5%. Making matters worse, all Federal student loans are now unsubsidized (meaning interest accrues from the moment of origination).

For medical school graduates this can sting. But at least they will have the financial horsepower to pay back the loan. My fear is for those graduates with less lucrative professions, such as social work and education. They too, can have upwards of $200,000 of debt with little ability to pay it back. There is a growing crop of people facing this conundrum and it concerns me.

I would also not be surprised if Congress ends the *Public Service Loan Forgiveness* program for **new borrowers**. In fact, there have already been proposals placed in the Administration's current budget for such cuts. My opinion is that the PSLF's days are numbered. I imagine this would manifest itself with an all-out termination of the program, or some sort of means testing, or perhaps an occupational exclusion.

POINTS OF OPTIMISIM

Cash in Company's Coffers

I spent a disproportionate amount of time discussing the new tax bill in my previous newsletter. And for good reason! I continue to believe the tax bill -which took effect Jan 2018 – will continue to stoke the economy and capital markets. Although, I must say the former has created more national debt, which must be dealt with at some point. However, regarding the latter, it seems like corporations are reacting as we thought. For instance, **S&P 500 companies spent $167 billion on capital expenditures in the first quarter of 2018**, the fastest pace in 7 years (Google topped the list at $7.3 billion). We are also seeing a lot of money being brought back to the US from overseas. It seems reasonable to expect continuing repatriation of foreign earnings -currently trapped overseas by confiscatory taxation. **For the 12 months through March, there's been just over a trillion dollars make its way back to US Soil.** The new law charges multinational companies a one-time tax on those profits. This will hopefully lead to further share repurchases over the coming months, which would be good for the markets**.**

Earnings

After-tax earnings for the S&P 500 companies are 25.3% higher in Q1 compared to the same period in 2017, according to Thompson Reuters. Forward P/E multiple (my favored valuation metric) remains healthy at 17.18%. Nothing much more to say here. Earnings are good, which in many corporation's case, justify the higher valuations.

Unemployment

Have you been on an airplane this year? How about a trip to Disney or Dollywood? Everything is packed with passengers and tourist. Talk to any business owner. Business is booming. Plumbers, dentists, designers and service professionals are booked up months in advance. I recently played tennis at a private club, and the member who invited me said that for the first time in the club's history, they were considering adopting a membership waiting list due to the abundancy of incoming membership applications. Turns out when people have jobs they spend money. How novel!

As of May the unrounded unemployment figure was 3.755%, the lowest since 1967. Let me repeat that. **In May, unemployment was the lowest since 1967**! But it gets better. Jobless rates for workers without a high school diploma fell from 6.4% a year ago to 5.4%. And African American joblessness is down from 7.6% to 5.9%. Even as the unemployment rate has trended sharply lower, wages have risen by 2.7% over the last 12 months. According to the Department of Labor's statistics, there are for the first time since the government began keeping records, more unfilled jobs than there are unemployed Americans. **How is this not being plastered on every financial journal throughout the land**?! Which brings me to the next section . . .

FAKE NEWS!

I continue to be disgusted, and even amused at the barrage of clickbait catastrophism within the financial media.

"if it bleeds, it leads" continues to be the media's mantra. These organizations irritate me to no end. Their blatant misleading of their readers and sometimes flat out untrue statements regarding our economy and equity markets are responsible for confusing honest investors who are trying their best to make prudent high-stakes decisions. They all to eagerly highlight negative stats, misrepresent neutral data, and single mindedly ignore anything positive.

You want a recent (but by no means, the best) example? Gladly! First, go back to the previous page and read the *Unemployment* section. Did you read it thoroughly? How can any rational person hear those Department of Labor figures and have a pessimistic interpretation? Well, apparently Yahoo Finance is up to the challenge. As the cascading data was being released, they published several articles. The big headline read "*The jobs report had some downsides too*." Another was titled "*Unemployment is at an 18-year low, but will new tariffs spoil the party*?" Are you kidding me?!

I rest my case, and simultaneously digress. Although I must admit I find the foregoing rant wonderfully therapeutic.

Looking back from March 30, 2009 – the birth of the current bull market – through today, I have compiled a sampling of the various "Armageddons" that we have experienced. Each Armageddon carried with it countless articles warning you to **get out now before it's too late**!

- 2011 – European debt crisis
- 2012 - US faces "Fiscal Cliff"
- 2013 - Year 5 of Quantitative Easing"
- 2014 – US drawn into Syrian conflict
- 2015 – Greek debt crisis; China's growth slows
- 2016 – Wave of populism effects worldwide elections, culminating with Brexit vote
- 2017 – Hurricanes pummel US and Caribbean
- 2018 – Fear of trade wars

Yet, a hypothetical investment in the S&P 500 index in June 2009 would have compounded annually at approximately 15% through June 2018 (assuming reinvested dividends, and excluding expenses, fees, and trading cost), **despite the headlines** - keep in mind that past performance is no guarantee of future results and indexes can't be directly invested in. This means a $100,000 lump sum investment would have grown to approximately $351,000 today if left untouched; smack dab in the face of every previously listed so-called crisis.

And if we go back a little further, we could also talk about the real estate crisis (2007), the Great Financial Crisis (2008), unemployment topping 10% (2009), and on and on it goes. Yet in the face of it all, companies still make products and consumers buy them. Period. I mean, what do you think the stock market really is? **In the end**, **the stock market is merely a reflection of companies' ability to generate profits**.

Woe to the poor little market timer who toed the starting line in 2009 as an overconfident fellow, convinced that he wouldn't get blindsided again with the next 2008-style bear market. Oh no! He's gonna get out before it's too late. *Sheep get slaughtered* as Gordan Gecco says, and he ain't no sheep! So off he goes with his market-timer starter kit, consisting of charts, graphs, and all the technical analysis needed to navigate the market's treacherous waters. Over the years, he will eagerly brag at cocktail parties about all the winners he chose, while conveniently omitting the losers. Fast forward to June 2018 as he limps across the finish line with ½ the returns of his inattentive, and composed counterpart, all the while, carrying a sack full of trading cost, and short-term capital gains to boot; oh, and sore shoulders from carrying all the stress that comes with a decade of day trading and unsuccessful market timing.

This brings me once again, to underscore the value of any advisor as primarily the **modification of your behavior**. Sometimes a change is needed, and a good advisor will lead you to make such a change. But sometimes the right move, is to make no move. As unsophisticated as that sounds, it sometimes can be the precisely correct advice for many long-term investors. I also might add, the "do nothing" advice requires courage for your advisor to make in the face of the aforementioned media, who daily toss out reasons to "*do something before it's too late!"*

I submit to you, once again, as I have in prior writings, that your behavior is the number one factor of your retirement security. According to a recent article in the Washington Post titled '*Dying at Your Desk is not a Retirement Plan*,' baby boomers — those born between 1946 and 1964 — have a median nest egg of $164,000. **No amount of market timing or stock selection can overcome this problem. Only your daily choices matter. The truth is that most financial problems are a result of ill-advised actions. In other words, no one ever declared bankruptcy because their IRA generated 6% instead of 8%.**

Getting a young client to save another 5% in their IRA or convincing a retiree to hold steady when the market drops precipitously (as it did in 2008), has far more real-world impact on your financial health than eeking out another 1% return – which is never guaranteed and nearly impossible to consistently execute anyway.

By the way, my office will send out notices to all clients if/when the S&P drops 10% - and another at 20%. I hope you will deploy whatever excess cash you have the next time the market offers you such discounts. I can't call everyone, so be watching for the email.

WHERE WE GO FROM HERE

As it stands, we are missing 3 key ingredients that typically accompany a major pullback: *over confidence, excessive borrowing, and excessive valuations in relation to share price*. Obviously, anything can happen, at any time. But it doesn't seem as though we're on the edge of something dangerous. Experts agree, however, that we're not likely to see a repeat of the 2017 runup, as if that argument even needs to be made. Although volatility somewhat subsided in the last quarter, I wouldn't be surprised to see it return to February's level. Finally, given the increase in valuations, quality stock selection continues to become increasingly important, since the number of bargains aren't nearly as abundant as they were in 2011.

Of course, all the prior conjecture really shouldn't matter to the long-term investor. My hope is that you see all this economic commentary as something interesting to read (which sounds like wishful thinking on my part) but having no bearing on your long-term financial life. **The one thing we know for sure is that the dollar's value is worth more today than it will be in 20 years**. And I continue to believe that

the best way to protect oneself from inevitable inflation is to invest in the great companies that create it. Simple enough?

CHANGES TO ADVISORY ACCOUNTS

I review all advisory portfolios on a semi-annual basis. **During the latest review, it seemed prudent to reduce some portfolio's fixed income duration by introducing a new security into most qualified advisory portfolios** (those affected were sent an email). This was accomplished by incorporating a mutual fund that primarily holds lower maturity bonds - trade confirmations were sent out accordingly.

The idea here is that the Federal Reserve continues to indicate they will be increasing the Federal Funds Rate. If/when this happens, we will see bond prices decrease, which is customary due to the inverse relationship between bond prices and interest rates. Longer term bonds are much more susceptible to a decline if/when rates rise. Hence, this change will reduce the overall duration for the fixed income piece. As an investment advisor, this is as tactical as I get and is a rare departure from the strategic philosophy I generally hold.

I plan to conduct the year-end model portfolio reviews in mid-December. The primary purpose is to identify tax loss harvesting opportunities for non-retirement accounts. I will also perform a general review of all portfolio holdings by examining fund expenses, management changes, etc. I don't anticipate making changes but will go where the data leads.

FIRM CONTINUITY

One of the benefits of undergoing my transition from Northwestern Mutual to private practice (which is now approaching 16 months!) is it has caused me to reexamine the health of my business. Most changes I've made have had little effect on you, the client. Yet, I did identify an area where I have been hypocritical. For years I have preached about the importance of making sure your affairs are in order, in the event you don't make it home one day. Will your family be ok? Who will step up to be there for those that depend on you? Well, turns out <u>I haven't been practicing what I preach as it relates to my Firm's continuity</u>. It's time I turned the tables on myself. I owe it to you to ensure that if I can't continue as your advisor, due to death or disability, that someone can. The person to whom I've entrusted this awesome responsibility is **Amy Edwards CFP®**. Amy is the founder and CEO of Aspire Financial Services in Kingsport TN. She is a Certified Financial Planner™ and has been in the industry for 19 years. She is among the brightest financial minds that I know. **Effective May 30, 2018, Amy and I entered into a formal buy/sell agreement, facilitated by our mutual broker-dealer, Securities Service Network LLC. If something were to happen to me, Amy will have immediate access to your accounts, case notes, etc**. I chose Amy because I know that she is first and foremost a lady of integrity who possesses a great moral compass. She is also someone who puts clients' first, not just in words, but in action. Amy has the knowledge base and competency to step in and quickly get up to speed on a client's personal situation. Between Amy and Leah (my most cherished and valuable business asset, as anyone would know that has interacted with her), I have no doubt you will be in the best hands possible. Hopefully I will be around for decades to come. But if not, take comfort in knowing we have taken measures to ensure you continue to receive diligent and trustworthy guidance.

FUTURE PUBLICATIONS

My original intent was to publish quarterly newsletters. Yet, after going through a full year of writing, *I've come to believe my time, during non-client facing hours, is better spent working on whitepapers and articles that are more relevant to real world situations. Besides, I frankly find market commentary sterile and even sometimes boring to write*. You can find any number of talking heads to give you market commentary. It's a commodity. But well thought out and honest commentary regarding every day financial situations is rare. I feel I provide much more value in this category. So, **moving ahead, you will be receiving semi-annual newsletters, in lieu of quarterly, with an increasing number of whitepapers/articles, covering a large array of financial topics.**

I hope everyone's summer is off to a great start! As always, I welcome any feedback and/or questions.

Sincerely,

Matthew J Trivett CFP® CLU® ChFC®