Triweekly Series

Ideas and Nuggets of News You Can Use!

LINDNER INSIGHTS

What will 2018 have in Store?

LINDNER CAPITAL ADVISORS, INC.

A Registered Investment Advisor

600 Village Trace, Building 23 | Marietta, GA | 30067

"Big enough to deliver, small enough to care"

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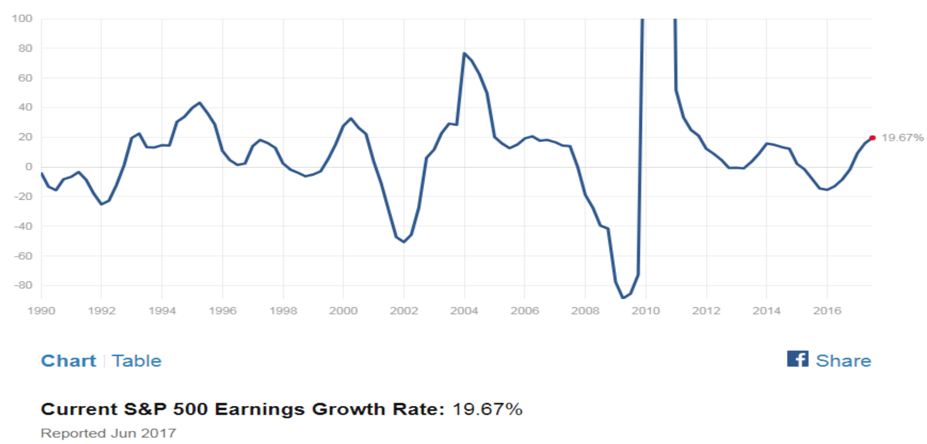
by Chris Briggs, CFP® and Leo Rose, AIF®

What will 2018 have in Store?

Unless things change between now and the end of the year, 2017 will be a good year for investors worldwide, with U.S., Developed International and Emerging Markets all experiencing solid gains. Over the course of the next few weeks you will hear all sorts of predictions for 2018. They will range from overly optimistic to downright pessimistic. Surges and crashes will be discussed in the press. Many of your clients will be asking, “what do we do different in 2018?” If you have correctly determined their risk tolerance (with LCA’s help), the simple answer is their assets are invested the way they should be. That said, there are pluses and minuses which we are likely to hear about on a repeated basis in 2018.

Pluses -

1) Tax Reform – By the end of 2017 or the beginning of 2018 congress agrees on and passes tax reform legislation, lowering tax rates for individuals and businesses alike. Individuals are likely to spend the new-found income on consumer goods and services, benefiting the economy. Businesses will use their additional earnings to invest in equipment, hire people and buy back shares of stock.
2) Continued regulatory reform – Businesses must comply with constantly changing and complex rules governing everything from who and how they hire to what they can sell, to whom and how they can advertise.[1] The administration has been and will continue to cut through expensive and time-consuming regulation. This improves new business creation and efficiency at existing ones.
3) Worldwide recovery – The world suffered an economic crisis roughly 10 years ago. As a result, central bankers across the world responded by lowering interest rates and providing additional liquidity in the form of bond buying. The coordinated efforts by the world’s central bankers has led to economic growth in almost every corner of the world. Equity prices have followed. Internationally, this accommodation should continue for the foreseeable future.
4) Strong corporate earnings – Growth of corporate earnings (profits) is the reason people buy stocks. The rate at which future earnings will increase over current levels influences how expensive stocks can get. As seen in the chart below, earnings growth is strong. [2]



[1] http://smallbusiness.chron.com/five-areas-government-regulation-business-701.html
[2] http://www.multpl.com/s-p-500-earnings-growth

Minuses -

1) Higher rates – U.S. interest rates are likely to rise in the near term and eventually rates will rise overseas as well. With unemployment here in the U.S. at near record lows and the economy and stock market growing, the Federal Reserve has stated it wishes to move U.S. interest rates to a more normalized level. Moving from a rate of effectively 0% just a couple years ago, the federal funds rate is currently at 1.25%, will likely finish the year at 1.5%, and consensus has the rate at 2-2.25% by the end of next year.[3] Used as a benchmark to set other borrowing costs, the federal funds rate rising over time, increases business and consumer loan rates. This reduces the amount of money people and business can afford to spend and slows the economy. Other central banks around the world will eventually follow the Fed's lead.
2) Aging economic expansion – Much of the earnings growth that drives stock prices is itself driven by economic expansions. Earnings and therefore stock prices can also be driven by the fear of or realization of an economic contraction (recession). The economy is constantly expanding and contracting. Expansions typically last longer than contractions, but either one of these phases can last for long or short periods of time. The current expansion, which started in June of 2009 is about 101+ months old, which is the second longest in U.S. history, behind the 120 month expansion which occurred from March of 1991 – March of 2001.[4] No one is saying a recession is looming, just that this is a historically long expansion.
3) Valuations – What you pay for an investment plays a large part in your potential for future returns. As we referenced in our October 26th, 2017 Triweekly, "Valuations Matter, Don't Overpay", the current valuation of the S&P 500 as a multiple of its earnings is 22.04x. This puts the markets earnings multiple well above its long-term mean of 15.68x and median of 14.67x.[5] Multiples can get higher, as they have in the past. Understanding and paying attention to the multiples paid for in an investment in a portfolio can greatly improve the probability of success. Look at the valuation comparison we published in the same Triweekly.

Lindner Capital 95/5 Portfolio (Equities) vs. S&P 500 (September 30, 2017)

	LCA 95/5 (Equities)	S&P 500	Premium Paid for S&P 500
Price to Earnings	17.51	22.04	26%
Price to Book	1.7	3.07	81%
Price to Sales	1.08	2.15	99%
Price to Cash Flow	8.72	13.68	57%

[6]

[3] https://www.thebalance.com/current-federal-reserve-interest-rates-3305694
[4] https://en.wikipedia.org/wiki/List_of_economic_expansions_in_the_United_States
[5] http://www.multpl.com/
[6] Morningstar Direct

The “Who knows?” -

1) 2018 elections, here and abroad – Domestically, it will be difficult to top the results of the 2016 Presidential election but with a third of the Senate and the entire House up for reelection, it will make for an interesting year. It seems unlikely, yet possible, that Republicans lose enough seats for the Democrats to regain control. At stake would be potential disappointment for the market relative to desired programs and reform. The greatest confusion will come from Europe as the United Kingdom continues to negotiate terms of leaving the EU and who and how soon the British Prime Minister, Theresa May, will be replaced. Italy could surprise the world and the market in its elections held early next year. If a populist is elected there, creating additional ground swell against the EU, the market could get nervous.[7]

Add it up, and 2018 offers many potential market turns. Proper portfolio construction should be based around proven and reoccurring investment themes. Portfolios need to be properly diversified among investment style (value and growth), market cap (large and small) and geographical location (domestic, developed international and emerging markets). There should be a discipline of regular and consistent rebalancing of the investments back to their target allocations, which allows profits to continue to be harvested from investments rising in value and be invested in ones that have underperformed (sell high, buy low). Additional portfolio diversification and risk reduction can be sought by adding non-correlating assets to a client’s holdings.

This is yet another opportunity to review a client’s risk tolerance, objectives, and reinforce why you choose to partner with Lindner Capital Advisors. Have a happy and healthy 2018.

[7] http://fortune.com/2017/11/20/predictions-2018-future-business/

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About LCA...

Lindner Capital Advisor, Inc. is a federally Registered Investment Advisor based in suburban Atlanta, Georgia, with representation throughout the United States. Our investment platform provides access to institutional fund strategies and exclusive money managers that are not readily available to the retail market. Our portfolios are designed to be consistent with a client's unique investment objectives, individual time horizon, and tolerance for risk. LCA has been CEFEX certified since 2006 and is committed to our fiduciary responsibility.

Ask your Relationship Manager for a copy of "The Educated Investor" written by Robert Lindner.

For more information, call (770) 977-7779 or email portfolios@LindnerCapital.com.

Visit LCA's website at www.LindnerCapital.com

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