HORTER INVESTMENT MANAGEMENT, LLC

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US Recession Odds Surging

On paper, the odds of a recession have never looked very high. It is only human instinct that makes many believe that is where we may be headed. However, that is starting to change. Since the Financial Crisis, the odds of a recession in the next 12 months held very low, around 5%. However, they have just jumped to 16% according to a popular recession calculator from BBVA. The last time the figure was higher was during the last recession. The two big factors boosting the odds are the US' flattening yield curve as well as the threat of a trade war, which is hard for anyone to gauge. According to an economist at BAML, "Our calculations suggest that a major trade war would lead to a significant reduction in growth … A decline in confidence and supply chain disruptions could amplify the trade shock, leading to an outright recession".

The Dow's Drop Was Just the Beginning

FINSUM: This is a very ugly, but realistic, prediction. We are increasingly worried about the direction of the international dispute on trade.

The Dow had a very ugly day yesterday, as did the Nasdaq and S&P 500. However, that might just be the beginning, argues Barron's. Markets plunged as Trump escalated the trade stand-off with China and other US trading partners, including limiting Chinese investment in American technology companies. And while markets have been looking at a possible trade war for months, it seems as though they have not fully priced in one of the magnitude which now looks to be emerging. According to one analyst, "Markets are starting to price in the possibility of a trade war with China, however, I would argue that a true trade war–one that drives us into a worldwide recession–would lead to a 20% or more drop in prices, so we haven't priced one in yet"

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QUOTE OF THE WEEK

"Knowledge is Power"

-Francis Bacon

Taking a comprehensive look at the overall current stock market

Taking a comprehensive look at the overall current stock market, you can see the chart below representing eight major indices and their returns through the week ending June 29, 2018. In a truly diversified portfolio, the portfolio's total return is determined by the performance of all of the individual positions in combination – not individually.

So, understanding the combined overall performance of the indices below, simply average the 6 indices to get a better overall picture of the market. The combined average of all 6 indices is 0.44% year to date.

Index	Last Week		One Month	Year-to-date
	Close	% Change	% Change	% Change
S&P 500 Index	2718.37	-35.94	-0.11%	1.67%
Dow Jones Industrial Average Index	24271.41	-309.48	-1.95%	-1.81%
Nasdaq Composite Index	7510.30	-182.52	1.03%	8.79%
60/40 Portfolio (BAGPX)	13.04	-0.14	-1.06%	-0.38%
US Aggregate Bond Index	2012.55	6.17	0.36%	-1.65%
20+ Year Treasury Bond (TLT)	121.17	0.64	1.30%	-4.01%

Data Source: Investors FastTrack, Yahoo Finance

Term of the Week:
Investment Policy Statement (IPS)

An investment policy statement (IPS) is a document drafted between a portfolio manager and a client that outlines general rules for the manager. This statement provides the general investment goals and objectives of a client and describes the strategies that the manager should employ to meet these objectives. Specific information on matters such as asset allocation, risk tolerance and liquidity requirements are included in an investment policy statement.

Dow Jones - Week Ending

WEEKLY MARKET SUMMARY

Global Equities: In a reversal from the prior week, the Nasdaq Composite Index led all three major US equity indices into the red for the week as the tech-heavy index started to feel the pain from effects of the trade war. The defensive Utilities sector, once again, outperformed all major S&P 500 sectors, with the Utilities SPDR Select Sector ETF (XLU) gaining 2.38% for the week. International equities continued their recent struggles, as the iShares MSCI Emerging Markets Index ETF (EEM), and the International Developed market iShares MSCI EAFE Index Fund ETF (EFA) were both down over 1%.

Fixed Income: Treasury yields declined slightly, with the yield on the benchmark US 10-Year Treasury Note ending the week around 2.84%. Domestic high yield bond spreads spiked from 3.39% the prior week to 3.64% in a busy week for new issuance. For the remainder of the year, high yield issuance should be light per Wells Fargo's latest forecast, which revised the projected 2018 total down from $305 billion to just $175 billion. High yield bond mutual funds and ETFs reported a pickup in outflows during the weekly period ended June 27th, losing $1.135 billion, per Lipper.

Commodities: Oil prices continued the upward swing from the prior week's clarification from the OPEC meeting on production limits. The steady climb in prices is concurrent with a tightening of the Brent Crude/West Texas Intermediate spread, despite US oil exporting a record 3 million barrels per day. Only Saudi Arabia and Iraq are exporting more oil to international markets. The American benchmark West Texas Intermediate gained over 7% for the week, to close near $74 per barrel, while Brent Crude ended the week knocking on the door of $80. Natural Gas prices declined marginally to close the week near $2.92/MMBtu.

WEEKLY ECONOMIC SUMMARY

Personal Income & Outlays: This important report released by the Bureau of Economic Analysis (BEA) indicated that the month-on-month (MoM) measure for personal income increased by .4% for May, as the component for salaries and wages increased a solid .3%. A pop in the savings rate, to 3.2%, explains weakness in consumer spending which came in below expectations for the period, at .2% MoM. Most importantly, the Federal Reserve's (Fed) preferred measure of inflation, Core Personal Consumption Expenditures (Core PCE), is directly at the Fed's 2% year-on-year (YoY) target. While the Fed wishes to protect against any additional accelerating inflation, the current rate facilitates continuing on the projected path of gradual increases.

Durable Goods Orders: Orders for durable goods, items that are meant to last for three years or more such as appliances and aircraft, dropped .6% in May in line with consensus estimates. The data from the prior month was revised higher, however, from -1.7% to -1% as business spending is still pretty strong despite the high levels in the beginning of 2018 stemming from the tax cuts. Orders for primary metals have fallen during the month, after a post-tariff announcement buying spree, and are important to watch going forward.

Consumer Confidence: The Conference Board-compiled Consumer Confidence Index may be starting to wane, as the latest release for June was below both the prior level and consensus range. The level for the expectations component dropped again and may be showing signs of consumers unease as effects from the trade war become apparent. The current conditions index is relatively unchanged for this period, signaling that consumer spending in the 2nd quarter should be robust, while the absolute value of the headline Consumer Confidence level continues to exhibit strength.

Last Week's Manager Moves—

HIM #20 —Reduced Cash from 36% to 2% and bought 14% high yield bond 10% short term high yield bond 10% high yield bond

HIM #10 —Sold 90% Short term treasuries, moved to .16% cash 99.84% equities

Current Model Allocations

Model Allocations

HIM #23 —100% Short term bond funds

HIM #24 —12.50% Cash 25% Short term treasury 62.5% ETFs

HIM #22 —100% fund

HIM #8 —100% trust

Other Managers

HIM #12 —100% treasury bond

HIM #9 —80% alternative equity mutual fund 20% dividend growth fund

HIM #1 —75% fund 15% fund 10% fund

HIM #21 —25 % Cash 75% real estate mutual fund

HIM #19 —50% real estate mutual fund 50% fund

HIM #11 — 90% Equity 10% Cash

HIM #10 —.16% Cash 99.84% Equities (48equities)

HIM #15 —100% Invested

HIM #20 —2% Cash 10% short term high yield 10% high yield 14% high yield corporate bond 15% ultra short bond 15% floating rate bond 17% high yield bond 17% high yield corporate bond

Summary

In utilizing an approach that seeks to limit volatility, it is important to keep perspective of the activity in multiple asset classes. We seek to achieve superior risk-adjusted returns over a full market cycle to a traditional 60% equities / 40% bonds asset allocation. We do this by implementing global mandates of several tactical managers within different risk buckets. For those investors who are unwilling to stomach anything more than minimal downside risk, our goal is to provide a satisfying return over a full market cycle compared to the Barclays Aggregate Bond Index. At Horter Investment Management we realize how confusing the financial markets can be. It is important to keep our clients up to date on what it all means, especially with how it relates to our private wealth managers and their models. We are now in year nine of the most recent bull market, one of the longest bull markets in U.S. history. At this late stage of the market cycle, it is extremely common for hedged managers to underperform, as they are seeking to limit risk. While none of us know when a market correction will come, even though the movement and volatility sure are starting to act like a correction, our managers have been hired based on our belief that they can accomplish a satisfying return over a full market cycle, -- while limiting risk in comparison to a traditional asset allocation approach. At Horter we continue to monitor all of the markets and how our managers are actively managing their portfolios. We remind you there are opportunities to consider with all of our managers. Hopefully this recent market commentary is helpful and thanks for your continued trust and loyalty.

Chart of the Week:
The Chart of the Week shows the US 30-Year Treasury Yield. The Federal Reserve's more aggressive stance on rates helped cause the 30-Year yield to breakout above its 200-day moving average at the beginning of 2018. However, the push toward higher rates is abating and the 30-year yield is now testing its 200-day moving average, possibly setting up a break to the downside. It has been said that interest rates are not going precipitously higher, as opposed to what some others are forecasting. Long rates receding should relieve concerns about rates moving relentlessly higher, with lower yields perhaps giving a boost to equity markets.

National Headquarters | 11726 Seven Gables Road | Symmes Township | Cincinnati | OH | 45249
P: (513) 984-9933 | F: (513) 984-5219