THE WEALTH STRATEGIES GROUP
Independent Objective Financial Advice

The Seven Signs of a Changing Economy™

"What to look for, where to find it and what to do when you see trends changing!"
As of May 2018

Summary

This month represents the end of the first year that my daughter and business partner, Brittany Jarocki, joined The Wealth Strategies Group! "Thank you" to each of our clients who have welcomed Brittany in our meetings, on our conference calls and our Skype sessions.

Brittany has accomplished a great deal in her first year at WSG. She diligently studied and passed her Series 7 exam to become licensed with the Securities Exchange Commission (SEC) and Financial Securities Regulatory Authority (FINRA) to transact securities of Corporate America and to represent investment products offered in our industry to help solve our clients' financial challenges.

In addition, Brittany passed the exams required to represent solutions that we offer via guaranteed annuities, life insurance and long-term care. She has enrolled in the College for Financial Planning rigorous two-year curriculum to become a CERTIFIED FINANCIAL PLANNER™ Professional (CFP®). Brittany has successfully passed the first of six exams and expects to complete her certification in early 2020.

Brittany has helped me gather the research I use to the keep the WSG Investment Selection Matrix™ (our investment menu) current as well as to pull the research for each issue of The Seven Signs of a Changing Economy™. Last month she wrote Sign #2, her first contribution.

As Brittany has created relationships with several of our clients' children, she has learned a great deal from Lori Green and Lisa Valdez in our office about opening new accounts, transferring in assets, creating Wealth Vision future planning reports, etc. A wonderful apprentice!

Perhaps the most important accomplishment for Brittany in her first year at WSG is she wrote and published her second book. Her current publication is titled The Seven Keys to Successful Investing™ and I must tell you, The Seven Keys book

really is great detail. It is a fast paced, easy to read key-focused book. She wrote it with bold highlights under each key so that our next gen millennial clients can read it inside their very short attention span. But I must say, no matter how experienced an investor you are, how much money you have made or lost, you owe it to yourself to read "The Seven Keys to Successful Investing", by Brittany Jarocki. Just call her at 303-933-2107 or email her at BJarocki@wealthstratgroup.com for a complimentary copy. If you would like additional copies for family members, friends in your social circle or work just let Brittany know and she will share a copy with them as well.

Congratulations on a great first year in the financial services industry, Brittany!

Lastly, with Brittany joining my business silo at the WSG I now have more capacity to work with referrals from your family, friends and social circles. Our processes, investment strategies and action systems have rarely been more well defined. We all know this nine-year up trend in the valuations of Corporate America may end in the next year or two. I think it would be wise to use this "before the next economic storm" period to encourage your friends and family to meet us for a complimentary "second opinion" on their investments and strategies!

This month, all Seven Signs of a Changing Economy remain positive! But, how about that first quarter 2018 volatility?! As I wrote in "The Weekly Update" posted 3/30/2018, we closed out the first quarter fatigued with the volatility but in reality nothing happened:

- The S&P 500 (equal-weighted) for 2018: -1.83%
- The NYSE Composite for 2018: -3.37%
- The NASDAQ for 2018: +3.81%

Really a non-event first quarter, but the CNN Money Fear and Greed Index dropped to a low of 8 out of 100! Since that reading on March 22, 2018, it has zoomed back to where it was pre-8 to the 40 range. People just don't know what to do, but we do!

Again, have a "base camp" plan:

"Rules of Clarity™":

1. Eliminate outstanding debt and have plenty of cash on hand to reduce worries during volatile economic times. This can include paying off your mortgage(s) for those inclined to think in terms of philosophy versus quantification.

2. Have a list of your monthly costs. Yes, a budget.

3. Know your sources of income, i.e. your earned income, retirement income, social security, etc.

4. You should consider allocating and diversifying your investments to reflect your constraints for time, risk and volatility. Once that is done, ALWAYS set aside a predetermined dollar amount to invest each month. At The WSG we refer to this as **"Systematic Investing"** or **"Dollar Cost Averaging*"** and it is a strategy that seeks to help grow your assets in periods of economic volatility. If you don't understand what this is, call and we'll have a class!

If you still feel queasy, then you might consider two additional adjustments:

1. Reduce the percentage of your portfolio allocated toward conservative growth. Consider moving a portion to a two-year A-rated or better bond ladder. In a bond ladder, the bonds' maturity dates are evenly spaced across several months or several years so that the bonds are maturing at regular intervals. The more liquidity an investor needs, the closer together his bond maturities should be.

2. Accept the fact that you may not have the temperament needed to be an investor, unwind your investments in a prudent way over a reasonable period of time, like one to six months, and promise yourself you will never invest for a larger future again.

In the client relationships that I personally oversee at The Wealth Strategies Group, I have created a reasonable investment portfolio customized around each client's constraints for time, risk and volatility. I believe each of these currently remains intact based on historical perspective and the economic outlook.

Read The Seven Keys of Successful Investing by Brittany Jarocki. They are designed to make you money, over time, of course!

Most of all, maintain perspective. Without it you will bounce around like the CNN Money Fear and Greed Index 40 to 8 to 40 plus, etc.! As I wrote in these notes back in November 11, 2014 (when the Dow Jones Industrial Average (DJIA) had just hit a new record of 17,500+:

"If a new record of 17,500 on the DJIA scares you, the DJIA 25,000, 30,000 and 40,000 in the not too distant years, will make you stark raving mad."

This month's Seven Signs are updated below. As always, I have added some unique insight with my comments. Just scroll down to view these now.

Your thoughts, comments and discussion are welcome. Please call me at 303-933-2107 or e-mail me at Jlunney@wealthstratgroup.com.

Respectfully,

James O. Lunney, CFP®
CERTIFIED FINANCIAL PLANNER™ Professional

The Wealth Strategies Group was founded by James O. Lunney under the guiding principle that comprehensive wealth counseling combined with independent investment advice will provide high net worth clients with complete trust in our competence, execution and integrity.

P.S. Please join me for our monthly conference call on The Seven Signs of a Changing Economy. You have the option of calling in or listening live for free from your computer. To call in, simply dial **347-826-7481**. There is no access code needed. To listen live from your computer, go to our website, www.wealthstratgroup.com, and click on the **"LISTEN LIVE"** button on the home page. You will be sent directly to our page on the Blog Talk Radio website and you can click on the link there. Instead of having a live Q & A session at the end of the call, you can now e-mail your question to me prior to the call at JLunney@wealthstratgroup.com and I will address them after my commentary on The Seven Signs of Economic Change.

The call is always on the first Thursday of each month at 1:00 p.m. MST/3:00 p.m. EST, unless otherwise noted. Please mark your calendar to join me for the next call on Thursday, June 7, 2018.

We encourage you to invite people from your family, work and social circle to join in the call. Just forward my e-mail notification to your e-mail list. It is very timely information and in the volatile investment environment a second opinion may be greatly appreciated in these uncertain times.

*Dollar cost average involves continuous investment in securities regardless of fluctuation in price levels of such securities. An investor should consider their ability to continue purchasing through fluctuating price levels. Such a plan does not assure a profit and does not protect against a loss in declining markets.

1)	**Indicator:**	*Personal Consumption Expenditure (PCE)*
	Where to find it:	*www.bea.gov*
	What to look for:	*Consumer spending increases or decreases for three consecutive months*

Entry written by Brittany Jarocki

(Positive)
This month's Sign #1 is more positive than anticipated. We left the month of February flat and in the past 30 days the Personal Income and Outlays data from the BEA shows a $50 billion increase in real Personal Consumer Expenditures (PCE) at +.40%. The $50 billion reflects increases in three important categories: wages and salaries, social security benefits and dividend income.

As Jim has been touching on in previous updates, an increase in wages and salaries is often paired with rising inflation, which the markets generally don't respond well to. This month's +.4 increase places the annualized growth rate of PCE at 1.90% year over year. Remember, the Federal Reserve uses our Sign #1 PCE as their measure of inflation. The Fed's target since the Great Recession has always been 2%, so we are right at the level the Fed desired before increasing interest rates more than the level to "normalize" back to where they should be. The Federal Reserve Board has indicated that there will be only a few slow and steady rate hikes, which I believe is the right answer and will allow all the pieces of the puzzle to fit nicely together over the next 18 months.

A Federal Reserve Board that remains steady and consistent on their plan for rising interest rates combined with confident companies of Corporate America and confident investors who received their increased dividend income, should go a long way in helping to overcome the "fender bender" market environment as we start to move onward and upward for the foreseeable future.

2)	**Indicator:**	*Institutional Money Flow*
	Where to find it:	*www.wordenbrothers.com or www.barrons.com/convictionoftraders*
	What to look for:	*Increasing or decreasing prices on high volume of large block trades*

(Positive)
If you were to go back just two months to the March 2018 issue of The Seven Signs of a Changing Economy, you would see a pretty amazing graphic. It was the CNN Money Fear and Greed Index. I had posted the graph in March, as it clearly quantified how investors had turned super positive (bullish) in January of this year with an "extreme" greed rating of 80%! Back in the January 2018 update I had written, "Give the market a few big down days in a row and you will see these newly minted bullish investors scatter like sewer rats."

That dip in valuations did happen and in less than two weeks the "Extreme Greed" level dropped to the "Extreme Fear" level of 18. Within the next week it was at 8 out of 100 bullish, as noted in this month's summary above. Indeed, the "sewer rat scatter" played out.

If you read the WSG "Weekly Update" that I write and post to the WSG website every Friday you would have seen this trend of titles for the last month:

"Just a Fender Bender" 4/6/2018
"Kicking off the Best Earnings Season Ever" 4/13/2018
"Prepare for Lift Off" 4/20/2018
"Last Call" 4/27/2018

In all, I detailed that a reading of positive investors at 8% pretty much meant anyone who wanted out of the market was out! What happens after that is they slowly came back. These are the people I call “renters” not “investors”. Renters sell when the rent is due and the rent is due when the values drop. They get scared and sell.

In the meantime, the earnings of Corporate America are trending up nearly 20% over last year, further supporting current and even higher valuations. As I write this edition on April 28, 2018, the positive level is back up to a reading of 36%.

The big institutional money continues to flow into, not out of ownership, in Corporate America. If you are going to build wealth act more like the big and smart money and less like Mr. and Mrs. 401(k). Building wealth takes patience, it takes time and it requires a plan you will honestly stick to.

This money’s money flow is strong, gaining momentum and I suspect on its way to the extreme levels once again.

Sign #2 is positive!

3)	**Indicator:**	*Leading Economic Indicators (LEI)*
	Where to find it:	*www.businesscycle.com or www.newyorkfed.org/research/global-economy/globalindicators.html*
	What to look for:	*Trends up or down for three to four months*

(Positive)
For the sixth straight month the Conference Board’s Leading Economic Index (LEI) is up. For the most recent month (March 2018) the LEI increased +.3%. In the six-month period ending March 2018, the Leading Economic Index increased +4.3%. This is an +8.80% annual rate and is gaining momentum. The prior six-month period saw an annual growth rate of +3.70%, so clearly the LEI is suggesting a growing economic backdrop six to nine months in the future, i.e. November 2018 – January 2019!

As a sidebar, the LEI has been a very accurate predictor of possible recessions. With this positive reading and the incredible momentum there is little reason to expect a reversal in the current economic growth pattern.

As noted above in Sign #2, Money Flow, the strong economic background does not prevent people from being crazy and selling into the scary news. Thus, I will remind you that I still expect three to five more corrections of 10 - 15% as we move toward the mid-term elections on November 6, 2018. Expect those, but know they are fear-based selling events and not economic based, thus short-term panic attacks.

I have also highlighted here several times the Chemical Activity Barometer (CAB). All things chemical tend to happen before many other activities in our

economy. So, this is also one of the first to show a weakening economy. Since 1919, it has shown to provide a lead time of two to fourteen months, with an average lead time of eight months, before a recession starts. This month the CAB reported in at 122. This is higher than before the "Great Recession" and is at the highest level ever recorded. The CAB remains +6% year over year.

Sign #3 remains very positive!

4)	**Indicator:**	*Employment rate and after-tax personal income*
	Where to find it:	*www.bls.gov*
	What to look for:	*A flattening, then downward trend in non-farm employment with a flattening to decreasing after-tax income would be a negative indicator. The appropriate trend would, of course, be a positive trend indication*

(Positive)
Finding skilled labor in the workforce is still proving to be difficult and companies are beginning to hire unskilled workers and use their own time, energy, and money to train them simply to keep up with the demand of their product or service. This proves to be a positive sign as the labor market and wage growth are keeping pace with corporate earnings.

Now that "all" of the skilled workers have been hired, we are beginning to see unskilled workers being sought out, which has certainly affected the unemployment rate. Today, 5/4/2018, the current unemployment rate has broken through the 4% barrier and hit an 18-year low of 3.9%. For the past six months we have seen unemployment stagnant at 4.1% despite constant hiring, and I believe that breaking the 4% threshold is due to companies running out of options and hiring unskilled workers and training them themselves.

While the 164,000 new jobs created paired with the 3.9% unemployment rate could cause reason for inflation concern, we are not there yet. The amount of hiring and wage growth is still on par with earnings growth, which has created a healthy market and therefore Sign #4 remains positive, for now.

5)	**Indicator:**	*Durable goods spending*
	Where to find it:	*www.census.gov/indicator/www/m3*
	What to look for:	*An increasing or decreasing trend, especially a trend of four to five months out of six would be a positive or negative sign*

(Positive)
These long shelf-life items like non-perishable, non-fashion items are usually the first to show signs of a slowing economy. Remember, these are items we can do without, if need be. New Orders increased +2.60%, up for of the last five months. Shipments, up ten of the last twelve months, increased +.03% for the month. Inventories increased slightly at +.10%.

What does this detail mean? Over the past year, new orders have increased +8.10%. Deeper in the detail, which I read and rarely mention, is that "core capital goods orders" are also up +8.0% versus last year. This isn't just "good" data flow it is "outstanding".

Remember, as stated above, these are items people can delay the purchase of as they are easy to do without. Think underwear, socks, another pair of shoes, etc., and they are flying out the door!

Over the first few months of 2018 the consumer put the credit card down so it could cool off, just a little, as we have seen "Personal Consumption Expenditures" (PCE) in Sign #1 above. But, they have been using that slowdown of purchases of "consumer" goods to buy these "durable" goods at a +8.10% annual clip.

Sign #5 is not as important of an input as the four signs before it, but it is one of the Seven Signs for a reason. The reason is that it tells us if consumers have excess money, if they are fearful and saving it as backup reserve, or instead if they are confident of their job, income and future. If they are confident in their future, then they tend to start buying, and or updating, "stuff" they could delay if they weren't so confident. Clearly, at +8.10% over the last year they are confident enough to continue buying durable goods, which strongly suggests the few lighter months of Sign #1 PCE is more "cooling of the credit card" than lack of money and enough confidence in the future to spend it!

Sign #5 is very strong and strongly positive!

6)	**Indicator:**	*S&P 500 Earnings per Share growth*
	Where to find it:	*www.standardandpoors.com*
	What to look for:	*Two quarters of S&P 500 earnings per-share growth, up being a positive trend and down being a negative trend*

(Positive)
Please stop here for a moment! This is important and if you take away nothing else, please let this get in your brain!

Here is a real life "example" of what the new tax cuts are "doing", not projected to do, but doing to the valuations of Corporate America!

On April 18, 2018, American Express Company said it earned $1.86 per share in the last 90 days versus $1.35 per share in the same 90 days one year ago.

Thus, American Express just earned +37.78% more than last year!

That is unbelievably good!

This is the amazing part: American Express Company's revenue was only up +11.60%!

So, how do you sell +11.60% more "stuff" and grow your profits at +37.78%, or almost four times as much?!

1. Efficiency of technology
2. Economy of scale
3. Buying back your shares. Fewer shares outstanding makes the earnings per share higher on those that remain.

There remains $2.60 trillion in Corporate America profit sitting in our overseas banks. It is starting to come home to the U.S. and as it does, companies will be buying back their shares. Cisco just brought back $67 billion of which they announced they will use $25 billion to buy back their own shares. This is so positive it is stunning. Makes those folks in Sign #2 look sort of silly!

You can expect company after company to report positive earnings that will continue to support the valuations of Corporate America. I personally expect to see the best earnings season in my thirty-six-year career. As you can see in "The Rule of 20" below, we continue to expect double digit earnings growth, which can support S&P 500 returns of double digits for 2018 as we watch the sun set on this volatile year of December 31, 2018.

The reduction in corporate tax rates combined with business' ability to fully expense their capital expenditures for the next five years are powerful tail winds for profits. So much so, that Yardini and Associates has seen earnings estimates for 2018 accelerate to $162.60/share for the S&P 500 as of 4/27/2018. I will use Yardini's $162.68 per S&P 500 share for our 2018 Fair Market Value (FMV) estimate, using "The Rule of 20".

To use "The Rule of 20" you just subtract the inflation rate from 20. I will use the same inflation rate the BEA used in calculating the Gross Domestic Product (GDP) "advanced estimate" for 1Q2018 released April 26, 2018 of 1.98%.

The result becomes your multiplier and is multiplied by the respective year's earnings per share to calculate the Fair Market Value (FMV).

- 20 – 1.98 = 18.02
- 2018 S&P 500 earnings estimate = $162.68
- $162.68 x 18.02 = 2,931.48 (S&P 500 2018 FMV estimate)

As of 4/27/2018, the S&P 500 trades at 2,669.91 (2018 FMV estimate rests at a -8.92% discount to FMV).

Not only is this market not overvalued, but how can it be overvalued when the underlying fundamentals and earnings are projected to keep getting better!

Sign #6 is positive. Very positive!

7)	**Indicator:**	*Inflation/deflation numbers*
	Where to find it:	*www.bls.gov/ppi/ or www.bls.gov/cpi/*
	What to look for:	*An interruption to the consistent but modest increase in the cost we all pay for goods and services*

(Positive)
Sign #7 is about measuring our economy's growth after adjusting for inflation, or what we call "real" growth. This means if inflation is increasing, it will pull down the real, or inflation adjusted, growth of our economy.

For the full-year of 2016 the annual growth rate, as measured by the Gross Domestic Product (GDP), which is all the goods and services we produce as a country, was +2.08%. For 2017, the GDP growth increased to +2.90%. For the first 90 days of 2018 we have decelerated to +2.32%. Keep in mind this is the "advanced" estimate and there are two more adjustments over the next two months before it is final.

If our 1Q2018 GDP settles at +2.32% that is still awesome. Keep in mind what level of activity it takes to grow a $20 trillion economy versus back in 1990 when we produced $6 trillion! Not only that but we are getting this result with little inflation, at least so far!

Inflation at the household level is measured by the Bureau of Labor Statistics (BLS) using the Consumer Price Index (CPI). For all items, the CPI is annualizing at +2.40% as of March 2018. The press has been very anxious about this as the CPI was only +2% last October. If they did just one little Google search, they would see the March 2018 CPI is exactly the same as it was in March 2017, one year ago. No inflation here yet!

Inflation as measured at the input, or manufacturing level, is where we see the first effects of inflation. The manufacturers see cost increases first and then absorb them or pass them along to consumers as a cost increase. Inflation is a little different story here. Last year in March Producer Price Index (PPI) was at +2.00%. Not bad.

However, in January 2018 it was up to +2.50% and as of this month, it is +2.90% i.e. a 50% increase over one year ago, not a great trend. Unless manufacturers are happy to watch their profits drop, those higher input costs will start making their way into our household costs via the Consumer Price Index (CPI). In my opinion, most of that increase year to date has been caused by the price of energy going up $10.00 per barrel. I don't see that continuing and as such, the canary in the coal mine is alive and well, so far!

Sign #7 remains positive!

*The Rule of 20 is in this calculation implying, and using, a price/earnings ratio, which is the valuation ratio of a company's current share price compared to its per-share earnings. Thus, 18x the expected Earnings per Share. Both EPS and the multiple of 18 could drop. The earnings could be reduced due to the consumers spending less. The multiplier of 18 could drop to, say 8 for example, if investors were to get scared and become risk adverse. All of a sudden 8 x $162.68 turns the 2,931.48 2018 FMV into 1,301.44 and even worse if earnings were to drop below the example of $162.68/share! This is the multiplier risk and earnings risk I personally worry about. It may never occur, but what an unfortunate event it would be if it did and we had not prepared for it as a possibility. Thus, I am glad we have!