AN Unobstructed View

WINTER 2018

QUARTERLY INVESTMENT INSIGHT FROM HIGHTOWER LAS VEGAS

Clarity in a Digitized World

Society has become accustomed to rapid technological change. However, we sometimes lose sight of just how dramatic that change has become. At this time 11 years ago there was no such thing as an iPhone (launched summer of 2007), Netflix was still sending you DVDs via snail mail, and no one had ever asked Alexa for anything. For many, these three products form the basis of everyday life in 2018.

As technology has advanced, more and more of our life has moved to the cloud. While that leads to enormous convenience and personal efficiency, it comes at a cost. We've found time and time again that our clients are feeling more disorganized as a result of heavier use of electronic devices. There are just too many accounts, passwords, and sites to remember. Even when everything is organized in an online portal, clients still feel a lack of organization. There is just something different about organization in the virtual world.

Enter the personal financial organizer. We've found that by organizing all your personal and financial documents in a physical binder, one you can touch and feel, you can create that sense of organization. The organizer brings together all your assets, liabilities, insurance, estate documents, and financial plan into a single location that's tangible. Sure, you'll continue to use your online accounts and portals, but you'll have something in paper form to reference when needed.

This binder becomes even more important to those you care about if something were to happen to you. Trying to decipher someone's finances is tough enough in the physical world, but is exponentially more challenging in the virtual world. Your significant other, children, or heirs will greatly appreciate the organization you've done today that saves them from additional agony during an already painful time.

We developed a dedicated process to help our clients organize their financial life. Once complete, the organizer serves as a central focus point as we work towards your goals. To learn more about the process of creating your personal financial organizer, please don't hesitate to reach out.

ALL EYES ON INFLATION

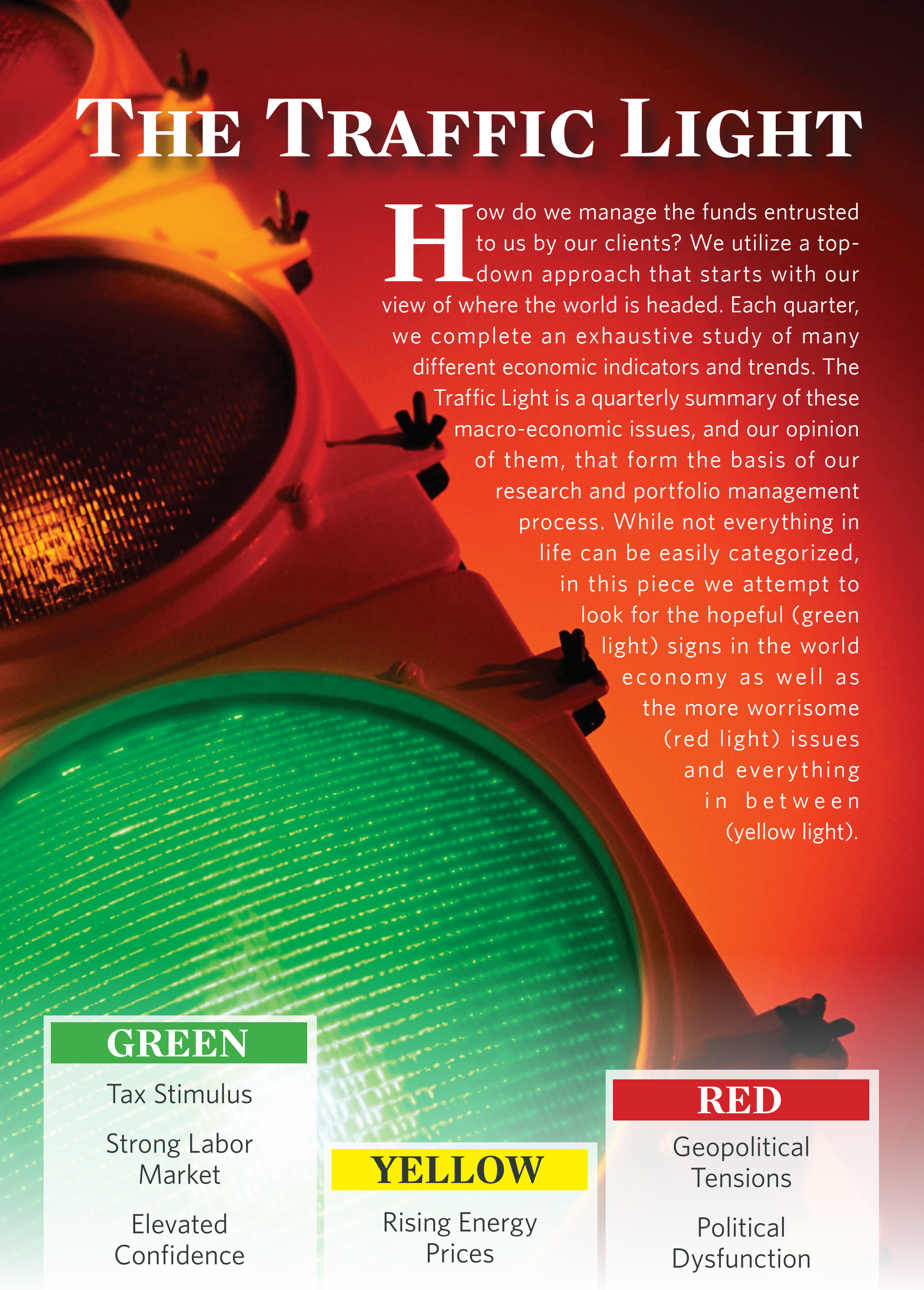
The market started off 2018 with an absolute bang on the back of increased optimism stemming from tax cuts and a robust holiday shopping season. Stocks experienced massive inflows, with billions of dollars flowing into equity exchange traded funds (ETFs). As investor optimism surged, so did valuation levels.

The market's change in any given year can be explained by the change in earnings and the change in valuation level (also known as multiples). Earnings growth has been tepid in recent years, but that hasn't stopped the market from marching higher. Multiples have continued to expand at a brisk pace, which has resulted in stretched valuations. For example, the S&P 500's price-to-sales multiple is roughly 2.3, the highest level in well over 30 years. Whether we look at earnings, book value, or cash flow, stock multiples are stretched. So why has the market allowed multiples to expand so much? The answer is low interest rates.

Other than a very short-lived move above 3% in late 2013, the yield on the ten-year treasury has been below 3% for over six years. Low rates push up what people are willing to pay for other assets because the relative advantage of investing in bonds decreases. This force helped propel stock valuations to current levels. Today, corporate earnings growth is set to surge as a result of the newly enacted tax bill. S&P 500 earnings are expected to grow by over 25% this year. If valuation levels remain unchanged and we see expected growth materialize, we would see another fantastic year in equities. However, inflationary forces may spoil the party.

In economic terms, inflation is a big deal. Inflation has a large and direct impact on interest rates, which feed through the system and impact everything from mortgage rates to bond prices. Inflation and interest rates also have an impact on stock valuations, which is where the current situation gets really interesting.

Before the tax bill was passed, economic activity had already started to pick up and inflationary forces were starting to grow. The tax bill will likely provide an extra boost to the economy and the inflation outlook, but inflationary forces don't stop there. The dollar is in a weakening trend, which raises the price of imported products. The White House trade agenda is also putting upward pressure on prices. After enacting tariffs on washing machines and dryers, LG announced they would be raising prices by $50. Additional tariffs and trade restrictions will only add fuel to the inflationary fire that has begun to burn. If inflation gets too hot and interest rates rise too fast, the market will react negatively, which is why we are keeping all eyes on inflation.



The Traffic Light

How do we manage the funds entrusted to us by our clients? We utilize a top-down approach that starts with our view of where the world is headed. Each quarter, we complete an exhaustive study of many different economic indicators and trends. The Traffic Light is a quarterly summary of these macro-economic issues, and our opinion of them, that form the basis of our research and portfolio management process. While not everything in life can be easily categorized, in this piece we attempt to look for the hopeful (green light) signs in the world economy as well as the more worrisome (red light) issues and everything in between (yellow light).

GREEN

- Tax Stimulus
- Strong Labor Market
- Elevated Confidence
- Rising Home Prices
- Earnings Growth

YELLOW

- Rising Energy Prices
- Higher Inflation & Rates
- Weakening Dollar

RED

- Geopolitical Tensions
- Political Dysfunction
- Elevated Valuation Levels
- Tariffs & Trade Restrictions

With January's strong performance, the S&P 500 has posted 15 straight months of positive total returns. That's the longest streak on record (data back to 1930), besting the previous streak of 12 straight months. Over the past few years, investors have become accustomed to amazingly consistent results void of any real volatility. While it has felt great, we all need to realize this is totally out of the norm. We believe investors need to be prepared to handle more volatility moving forward, as the forces that have kept risk in check are shifting.

While the Fed is projected to raise rates just three times this year, the fact of the matter is that rates are moving higher. Rate hike cycles have usually resulted in an eventual recession, once rates have reached levels that crimp economic activity. We are likely still a couple of years away from that point, but inflationary forces are building, which could pressure the Fed to act more aggressively. A surge in inflation is not our base case, but we have to acknowledge that risk is increasing. As a result, we have added to our gold position in an effort to hedge against an inflation-induced market pullback.

Bond prices have come under pressure as interest rates have risen. The price sensitivity of a bond has a lot to do with its length to maturity. The longer a bond's maturity, the more volatile the price when rates change. We've kept a relatively short average maturity on our bonds over the past year to minimize the interest rate risk. We anticipate we will be able to reinvest the proceeds from these bonds at better yields down the road.

International markets continue to look attractive relative to the U.S. Valuations are less stretched, especially in emerging markets. Most international central banks are still in easing mode, which creates a strong tailwind for these countries' capital markets. The dollar's weakening trend also bodes well for international exposure. We anticipate adding to our international investments as we take profits from our U.S. positions.

What are they talking about?

Relative Strength

The stock market surge to kick off 2018 has brought with it a lot of jargon. Bubbles, melt-ups, and euphoria have all seen their share of the headlines. Another term you may have seen floating around the media is relative strength. The relative strength index (RSI) is a technical trading measure that assesses the speed and change of price movements in a security or the market. The relative strength index is measured on a scale of 0 to 100, with readings over 70 considered "overbought" and readings below 30 considered "oversold."

The stock market's surge higher over the past few months pushed the S&P 500's RSI reading to over 90 in late January (measured on a weekly basis), which is one of the highest levels we've seen over the past century.

Therefore, it was no surprise to see the market begin to correct in early February. A correction was desperately needed in order to pause this melt-up, dial back some euphoria, and keep a speculative bubble from forming.

In the Media

Mike
Appeared on Channel 13
Featured at Preview Las Vegas

Adam
On MoneyLife

Check out our other publications for insight into our thoughts and process:

ruminATions:
http://www.hightoweradvisors.com/who-we-are/hightower-advisors/las-vegas/blog/

Thinking & Thriving:
http://www.hightoweradvisors.com/who-we-are/hightower-advisors/las-vegas/thinking-and-thriving/

The Stat Pack:
http://www.thestatpack.com

Follow Us

What's New?

It's been an eventful period at HighTower Las Vegas. We welcomed Shelby Sutter, our new Client Service Manager to the team in December. Shelby is high energy, fun, and a dedicated professional. She is a proud veteran of the United States Air Force where she served as an air-traffic controller and previously worked at Wells Fargo Advisors servicing clients across the nation. In her free time, she runs...a lot, working toward her goal of running an ultra-marathon.

Rayna welcomed a new member of the HighTower extended family when she gave birth to a new baby boy. Krum, was born on February 3rd, weighing in at 8 pounds and 15 ounces. We will certainly miss Rayna while she is out on maternity leave, but are thrilled for her and her family.