COPPERWYND FINANCIAL

OCTOBER 2018

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“If this economy keeps expanding over the next year, which I think is highly likely, this will be the longest expansion in US history dating back to 1850.”

Market Commentary

It is hard to believe that fall is here and we are 75% through 2018. Where has the time gone? The one thing I do miss about not being in the Northeast this time of year is the colors of the fall foliage. When I worked on Wall Street, I would take the family up near West Point on the Hudson River and we would pick fresh apples and buy some pumpkins straight off the farm. Some great memories we made and that I cherish.

Now back to the economy and the markets. Lynda always accuses me of chasing squirrels (in case you missed the movie “Up!”, a euphemism for getting distracted). Guilty as charged!

This month I am going to give you a snapshot of my thinking on the markets and my concerns about the future. We have seen one of the best quarters for the US stock market since 2013 and profits are doing great. What isn’t to like? Profits rising, 401Ks going up, real estate going up, GDP over 4%, personal income starting to really increase in a meaningful way.

All of these things are positive and true, but that is always the case near the top of the cycle. If this economy keeps expanding over the next year, which I think is highly likely, this will be the longest expansion in US history dating back to 1850. Markets like economies that are expanding, so we are still fully invested and will remain there until our models tell us differently. Recessions are what start bear markets and high interest rates are usually what pushes the economy into a recession. This week the Fed raised short term rates to 2.25% as expected and indicated that they will raise them several more times over the next year. It wasn’t that long ago when the Fed Funds rate was effectively 0%.

What keeps me worried and you pay us to stay worried, is two-fold. First, the rising rate scenario and its impact on consumers, corporations, the stock market and the government. Second, the tariffs that have been put in place or threatened to be implemented. A trade war could upset this coordinated global expansion. I do not remember in my lifetime ever seeing fewer countries in recession.

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Rising interest rates negatively impact consumers in higher mortgage, car loan and credit card rates. This can be a cascading effect as fewer home purchases will lead to less economic activity in furniture and all the other ancillary purchases. I think we will see that impact first in the sub-prime auto loan sector which could cause a decline in the booming auto industry. Higher interest rates will also reduce corporate profits as most companies borrow money and higher interest rates will hurt profits. This could also reduce the number of companies that borrow money to fund buy backs of their own stock. Buy backs have been a major positive factor the last 9 years in a rising stock market. Higher interest rates will also make bonds and CDs more attractive relative to stocks and that will move some money into bonds and out of stocks. Lastly, higher interest rates will lead to higher deficits as the Federal government debt is $21 trillion and a 1% rise in the interest rate paid equates to $210 billion in additional deficit. Not all that debt will be subject to higher rates but you get the point, and this will trickle down to state and local government borrowing. At this stage in the economic cycle of sub 4% unemployment rates, we should be running a surplus at the Federal level and this year we are going to be close to a $1 trillion deficit.

The other troubling issue is the potential for a trade war. I agree that we have some not so great trade agreements, but we have had them for many years; so why have we stayed in them? Usually, if someone stays in a seemingly bad relationship, they are getting something out of it, however bizarre that something might be. As I look at our trading relationship with China over the last 20 years, it is easy to see why we have stayed in it. We got to import low priced goods that kept our inflation rate artificially low and they used some of the dollars we paid them to finance our deficit spending. They have lent us in excess of $1.3 trillion dollars. Our cost for that was a lot of jobs. Was it worth it? Hard to really tell at this moment. Hopefully, the tariffs will be a way to negotiate a better trade deal. If it spins out of control and becomes a global trade war everyone will lose. Nearly every item you buy around the world is sourced from multiple countries around the world. A trade war will cause prices to rise and potentially harm trade relationships for years. Ford announced that the tariffs will reduce its profits by $1 billion this year. We will see how other companies are affected.

When will these items become actionable in our strategies? We will let the models tell us but Ray Dalio (CEO of the largest hedge fund in the world and a really smart guy) estimates we will enter a recession in the next 24 months. Is he right? Who knows, but we will keep our eyes on all of this.

So let us do the worrying, if any is needed, and you go enjoy the fall colors and weather with family and friends!

- David

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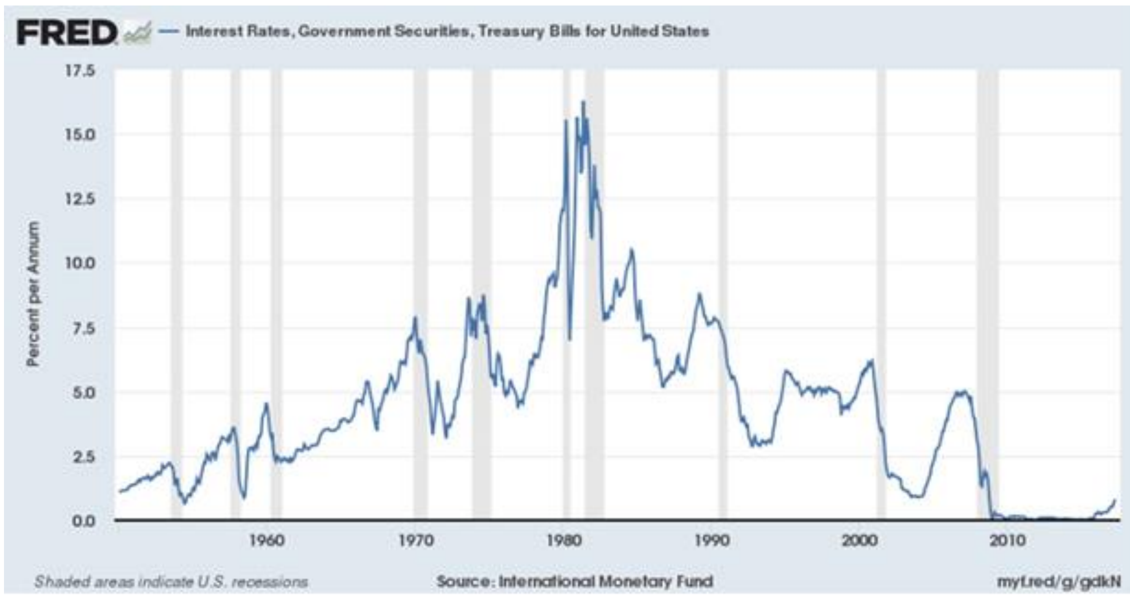
Graphic of the Month



Portfolio Spotlight

This month we are highlighting the Total Return portfolio – our bond model. As many of you know who have been with us a while, this was the model that started it all! We launched Total Return in 2010 and it has been the backbone and steady workhorse of our allocations since then. Most investors are unfamiliar with the types of bonds we utilize in these models, but include such things as emerging market bonds, high yield bonds, preferred stocks, mortgages and senior secured debt, as well as high yield municipal bonds. This year we have spent most of the year invested in floating rate investments as the Federal Reserve has raised interest rates three times (with more to come). As you can see in the graph above from the Federal Reserve, from a high in 1981, we have witnessed a 30 year trend of lower interest rates culminating in nearly a zero interest rate environment a couple of years ago. That trend has most likely ended and rates over the next few years will be increasing. Bonds generally do not like rising interest rates, but floating rate bonds have the advantage of generating higher yields as rates push higher. This has given us some stability of our bond prices while allowing us to stay invested and collect those dividends every month. We won't see the kinds of returns we have the past few years in bonds, but we have been able to stay positive when the bond index (AGG) is down nearly 2% for the year and when that stock correction finally comes, as it will some day, we will be happy to have some "boring" bonds!

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Financial Planning Tip of the Month

Attention parents and grandparents! October 1st, marks the opening of FAFSA (Free Application for Federal Student Aid) submission window! The FAFSA is the first step in the financial aid process. It is used to apply for federal financial aid, such as grants, student loans, and work-study. Don't think your family will qualify for financial aid? The FAFSA should be completed regardless, as loans and scholarship awards may also take the information on the FAFSA into account, and with tuition prices where they are these days, every dollar counts!

These steps must be taken each year, before filing the FAFSA.

1. The student should create a FSA ID at https://fsaid.ed.gov/npas/index.htm The FSA ID is an electronic signature, used to sign the FAFSA. Write down the username, password, email address and challenge questions and keep this information somewhere safe (e.g., take a picture of it with your smartphone).Also provide your cell phone number when registering for a FSA ID. This will make recovering a lost or locked FSA ID much easier. Even though the FAFSA season starts on October 1, you don't need to wait until then to get a FSA ID.
2. Determine the student's dependency status. The student's dependency status will affect whether parent information is required on the FAFSA. The student is only independent if he or she is pursuing a graduate degree, has a child, is married, or a member of the US armed services.
3. Gather important documents, such as your Social Security card and driver's license (if any). If you are not a U.S. citizen but an eligible non-citizen, get your alien registration number and permanent resident card (green card). And gather financial records relating to income, assets, and investments as all of this will be asked about while filling out the FAFSA.
4. Create a college list. You do not need to have applied for admission to a college to list it on your FAFSA. You must provide at least one college on the FAFSA for the FAFSA to be processed. It is a good idea for the college to be an in-state public college, since listing a state college first is often required for the student to be considered for state grants. You can add more colleges later.

The FAFSA is filed annually, once for each year in college.

If you are attending FAFSA workshops or presentations by your child's school, please be aware that while they are experts at the bureaucracy that is financial aid, they do not understand YOUR financial life. Consult with us before making any changes to your accounts as there are potential tax and estate considerations when you move money around.

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Your 401k Allocation

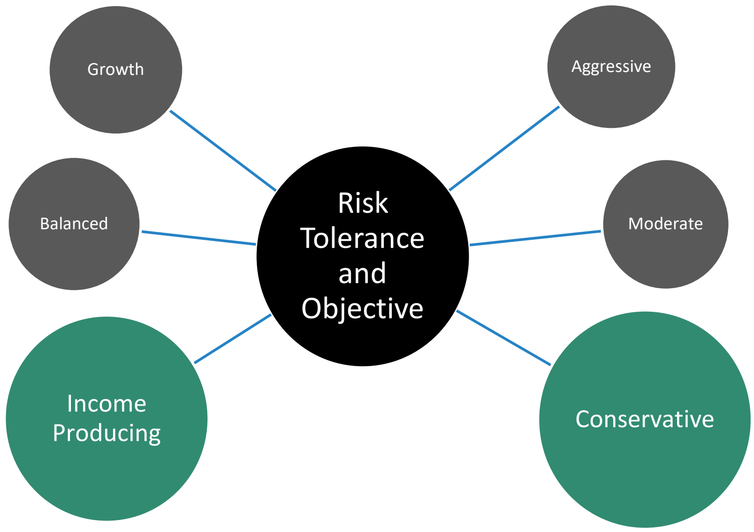
The positive news regarding Canada joining Mexico in the revised NAFTA (or the USMCA, as it will now be known) trade agreement has given the market hope that Europe and China will fall in line. The very thing that lead buoyancy to small company stocks has now been the force behind their slip the past week. And so we see ourselves lightening the allocation there and driving it back into large company stocks. Growth continues to be the story this year, so growth gets the lion's share of the changes. International is still trailing all US markets by a large margin due to the continued strength of the dollar. The dollar's strength continues because the Federal Reserve once again raised the short-term interest rate, the third increase this year, and signaled on-going increases for next year as well. Rising interest rates attract buyers to your currency, lifting the value, so we could see international stocks stunted by that force for the better part of the next year. As always, if you need assistance in getting your 401K choices in line with the above, please feel free to give us a call!

October 2018					
		Agg. Growth	Growth	Moderate	Conservative
Bonds / Cash		0%	10%	40%	65%
	Stable Asset - OR - Short Term Bond	0%	10%	40%	65%
	Total Return	0%	0%	0%	0%
	World Bond	0%	0%	0%	0%
	Inflation Protected Bond	0%	0%	0%	0%
Large Cap:		55%	51%	32%	20%
	Large Cap Growth	40%	35%	25%	15%
	Large Cap Value	15%	16%	7%	5%
Mid Cap:		30%	27%	19%	10%
	Mid Cap Growth	20%	20%	14%	5%
	Mid Cap Value	10%	7%	5%	5%
Small Cap:		15%	12%	9%	5%
	Small Cap Growth	15%	12%	9%	5%
	Small Cap Value	0%	0%	0%	0%
International:		0%	0%	0%	0%
	Developed International	0%	0%	0%	0%
	Emerging Markets	0%	0%	0%	0%

Notable and Quotable

It is not too early to begin RMD planning! Beat the rush and take care of your 2018 RMD before the hustle and bustle of the Holiday Season! Give us a call at the office to complete your distribution today!

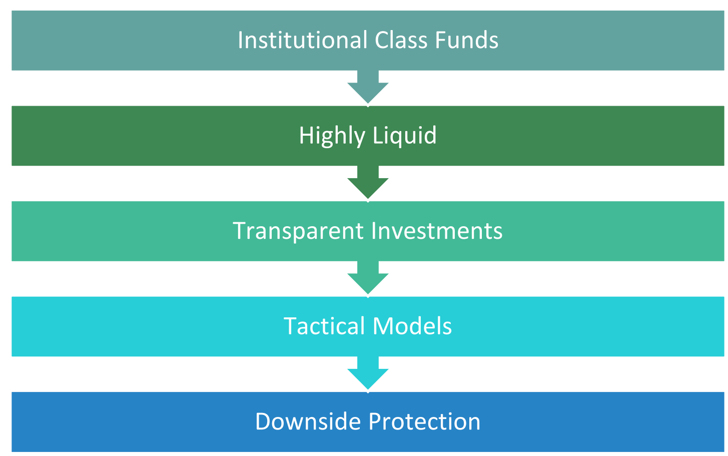
Total Return Strategy

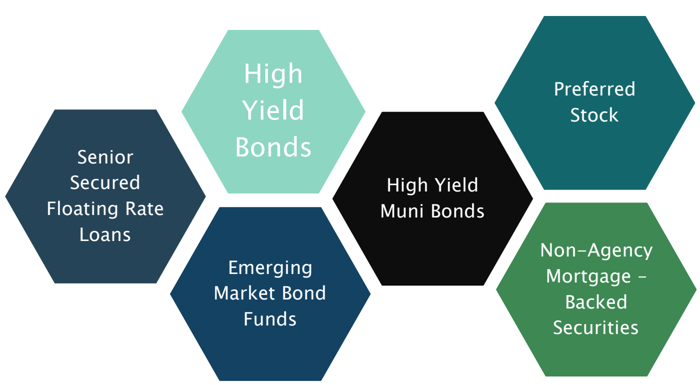


The Total Return Strategy is an income producing portfolio which incorporates a rules-based approach to investment selection. The goal is to provide reasonable returns while maintaining reasonable risk.

Key Features

The Total Return Strategy is a proprietary rules-based model that seeks to invest in a basket of income producing funds while limiting the downside risk by moving to cash if the fixed income markets are unfavorable.





Investment Universe

The Total Return strategy invests in strategies focusing on high yield, and income-producing bonds in an uptrend. An advantage to this strategy, is that it allows movement in and out of securities quickly as trends change, limiting downside and capturing as much upside as possible.

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