KEEN ON
RETIREMENT

Market Update Webinar
With Matt Wilson

Welcome to Keen on Retirement

Bill Keen: Hey, everyone, Bill Keen here. I wanted to take a moment and introduce our podcast today. We have a special treat for you and that we're releasing a recent market update webinar, produced by Matt Wilson, as a podcast today. So if you'd like to listen to this, right where you're at, you can follow along on the audio portion of that webinar, but I would contend that the better way to consume this information, so that you can follow along to some of the slides that Matt put together, he puts a lot of work into these presentations.

And the webinar version of this is much better, in my opinion, to take in and understand the information that Matt is talking about. Another added benefit to watching the webinar is that there's a video of Matt as he talks. So it makes you feel a little more personal because you get to see him as he presents. With that in mind, we hope that you enjoy this presentation, however, you decide to consume the information. Thanks, and we'll talk to you soon.

Hello, everyone, and welcome to our market update webinar. My name is Bill Keen and I'm the founder and CEO of Keen Wealth Advisors. Welcome. It's nice to see the sunshine poking its head through here in Kansas City today. As many of you know, we are a fiduciary retirement and wealth advisory firm, helping folks to navigate up to and over into retirement, with the real understanding that, for most folks, their investible assets, to a large part, are what they're going to be relying upon to fund the remainder of their lives.

That's an interesting process for folks who have saved and been prudent over the course of a lifetime to consider, "The paycheck is going to stop at some point, and I'm going to have to rely on my investments as the engine to a financial plan going forward and that's going to have to last the rest of my life."

So I commend you all for being on this webinar today, to take some time out of your day, but I've seen success with some folks that stay engaged to a certain point and then really, in my opinion, and I am biased when I taught this

information, is that when partnering with a fiduciary advisory team that you know is paying attention to the things, exactly like we're going to be talking about today, that has created and produced success for folks over time.

Now, today, we're going to talk about the stock market. We're going to talk about the economic environment that we're in. We're also going to talk about federal reserve policy. Then we're going to go into what happened in Q4, and Q4 of last year did get some folks' attention, but then what happened in Q1. And then I would contend more importantly where we are headed now. We're not attempting to make you an economist or portfolio managers, but for those that do have an interest, we want to provide you with the look at the items that we watch closely in our firm each day.

These items do provide the framework that shapes our investment allocations and recommendations. So my speaker for today is Matt Wilson. Matt and I worked together for over 17 years. He is a managing director of Keen Wealth Advisors and the firm's chief investment officer. And for those of you that listen in to the Keen On Retirement podcast, you know that Matt's a regular guest on that podcast and I really try to pick his brain on that show about the issues he'll be talking about today.

For those of you that have attended our presentations, holiday breakfast each December, Matt does a fantastic job. You know that he takes complex issues and presents them in a way that's understanding and interesting. He uses charts and graphs to demonstrate what he's thinking and this webinar format is again as a wonderful format using technology to be able to allow you to follow along on your screen while he's presenting and hell even go through as he's speaking and presenting and highlights certain things on the slides to point out what's he's trying to demonstrate.

So this is a great format for this type of a presentation. I did want to let you all know there will be a replay available of this, shortly after the presentation is concluded. So if you wanted to see a replay, you can or you want to forward that onto someone you think may be interested in that. Then also one last thing, we do have our open house. Many of you have attended our open house in the past, that's coming up on June 5th, here at our offices. We have the same thing, the Jack Stack BBQ, the band, the tents. I guess, more importantly, the Sheridan's ice cream, but that's part of it and a lot of fellowship and good camaraderie.

So mark your calendars for that if you haven't seen that notice already come through. We have a lot of clients of the firm on the webinar today and I just wanted to say welcome and it's an honor and a privilege to be your advisor and to be on the journey with you. It's something next to family and health. We know that the money part of things is very important topic and we take it very seriously. So with that, Matt, I'll turn it over to you, sir. Thank you.

Matt Wilson: All right. Thank you. We've got a lot of info to cover today and I do enjoy this format because I'm able to share with you a lot of charts and graphs and explain the concept that ... It can be a little complex at times. There's a section for questions, and we'll just compile those throughout today's presentation and then, at the end, time permitting, we will answer those questions. So there's a spot for you to enter those in.

Now, we're going to cover these different topics today. We're going to go over the stock market, talk about the economic environment here in the United States and then what the Fed policy is and then where we're headed. So just to kick it off, what has been happening here in the stock market? Essentially, we're back to risk on and what means is that stock values have gone up. They've performed well since the beginning of the year. A lot of different things have happened that cause that, but I think that we're back to fair valuations when it comes to the stock market.

These are some headlines that we've actually had since the beginning of the year and one of the ones that I think is interesting is this cover of Barron's Magazine and this just came out just a month ago and it just says, "This bull market has no expiration date." It's always interesting when we have media talking about how great things are. Some might say that is contrarian indicator and we do pay attention to that once things maybe get a little bit irrational or a little bit too much exuberance, so to speak.

Here is a graph of stock market with some different headlines going back to 2015, and you can see I pointed out some pullbacks on here. But what I want to show here is, one is volatility it's not something to be afraid of. It's actually a feature of the markets, not something that is a bug. Volatility is here to stay and even when we have advancing markets, we're going to continue to have volatility. But just recently, so here you can see this is where I've got my cursor highlighting the peak in September 2018. Shortly after we entered Q4, the chairman of the Federal Reserve, Jerome Powell, he said, "We are a long way from neutral."

And basically what he means when he says that is that we're going to continue raising rates and what the market looked at that said, they, the Fed doesn't get it, and the Fed is going to push this economy into a recession. I have some charts to show you what I mean by that but essentially, what the market was looking at is they're going to invert the yield curve. They're going to push short-term rates too high it's going to go higher than long-term rates, and that's going to tighten credit here, in the US, which is going to slow down the economy and that's really what the market was reacting to.

Now, in addition to that, there was deceleration of earnings. So earnings' growth in 2018 was very strong but then in 2019, expectations are to slow down. Now, it's to slow down not to go negative, but just to slow down. Now, after Powell had his talk in October, markets reacted negatively, all the way

down to then another Fed meeting in December, which, again, they raised rates again, said they're targeting 3% and markets, definitely, didn't like that.

Bottomed here in December, actually Christmas Eve, 12/24/2018, and then since then, we've had a nice recovery and actually since this chart's been created, we are back at old-time highs. A lot of that driven by, again, by the Fed, where Powell said, in January that essentially he admitted to getting it wrong, "We got it wrong. We're backing off our call for 3% rates. We're paying attention to the yield curve and we're not purposely going to invert it." So market is definitely like that. So a little bit of here's what's happened over the last six months or so.

The other aspect that happened, we watch the trends of the market very closely and what I've got here, this is actually going back to 2009, last 10 years, we have the S&P 500 and then I have two lines on here. The blue line is the 50-day moving average and the red line is the 200-day moving average. These are just indicators of the direction of stock prices and what we look for are these concepts called golden crosses and death crosses. And yeah, they're widely followed, so they get a lot attention in the media but a golden cross is represented by gold arrows and that is when the 50-day moves up above the 200-day moving average.

So you can see when that happens and typically when that happens, and this is, you can go back many decades and look at these points when this has happened, has led to a sustained advancing markets. Now, on the flip side, we have death crosses, which are represented by the black arrows and that is when the 50-day moving average moves below the 200-day moving average. We do watch those. Now, those don't necessarily indicate that we are headed into a recession or indicate that we're headed for significant volatility.

It does mean there might be some short-term volatility, but when we are experiencing a strong economy and an advancing economy, these death crosses tend to be very short lived and rebounces to the upside, which, again, over the last decade, you can see how, yes they did cause some short-term market downturns but all alleviated themselves to the upside. They are, again, widely followed, but it is an indication that risk is back on, that stocks are in favor again, trends are in our favor.

Now, what drives stock prices over time? We get this question a lot. Now, here's what I've got. This is a log scale of the stock market and this goes back to 1991. So this red line is the S$P 500 with dividends reinvested. The black line is just the S&P 500 total ... I'm sorry, just price return index. So that's not with the dividends reinvested. What I've drawn here is just a trend line. This gray line, this is just from point to point. Now, this is again on the S&P 500 total return index, so with dividends reinvested.

Just even going back to 1991, you can see we're back on path of a 10% growth rate and going back to 1926, data has supported that stock prices on average, on about 10% a year, and there's even data going back to early 1800s which supports that as well. That long-term stock market grows at about 10% a year. And what this trend line, the reason I show this is because I believe we are back to fair valuations. So what would get us concerned is when stock prices are high above this trend line. When I put this in a format like this, you can clearly see that stock prices in the late '90s were well above the long-term trend. You can see they decoupled.

It got very extended from 1995 all the way up into 2000, meaning that stock prices were advancing much faster than history would suggest that they've done in the past. And then you can also see then there's periods where stock prices get significantly below that long-term trend, like we saw in 2008, 2009. And then the recovery since then has just brought us back to that long-term trend. I think, occasionally, when people maybe take a step back and they look at the market and they hear about ...

The stock market in the US is advanced 400% since March of '09 and some people might actually show a chart or they might see a chart online. And one, the reason I put this in a log scale is because this is actually how you should be looking at stock charts, but many charts are shown in an arithmetic scale, which just shows almost a parabolic move higher, which scares people. They believe, "This can't last. This has to end and it's going to end a very dramatic fashion that we're not going to like."

But when you actually put this in the correct scale and you look at where we are on our long-term trend path, we aren't significantly higher or lower than where we should be from a long-term trends basis. So stock prices are right on track. Now, that doesn't mean, and I'm going to probably say this throughout the presentation, there won't be volatility because there's always volatility, but you don't see a significant risk because of overheated markets or overvaluation.

Now, this next line, this is on just the price return. So without dividends reinvested, the markets earned about seven and a half percent a year on a price return basis. The reason I point this out is because of my next slide, what I'm going to show here is what drives earnings growth. So, we know that stock prices grow at about 10% a year, well, what drives that? Earnings drive stock price appreciation. So it's just the profitability of corporations here in the United States.

This is a graph of the S&P 500 earnings and I've got up in the right-hand side here, 2019 estimates and then 2020 estimates. This earnings graph mirrors the seven and a half percent growth rate on the price return index, which is, you take a step back and you think about it, it's like, "Okay, if earnings are growing at seven and a half percent a year, price appreciation should be seven and a half percent a year," which it is. We are on that same trajectory. Now, of course,

things don't come in a straight line. We're going to have some volatility around these growth curves, but you can see we're right on that growth curve.

And again, earnings will get higher or lower than those long-term trends in certain periods, but we are still back just on track for that long-term trend. When you look at 2019 and 2020, still in that same trajectory. Now, this is a 2018 earnings. Earnings in 2018 were up 23%. So as I mentioned earlier, part of the volatility in Q4 of 2018 was around the expectation that earnings growth isn't going to continue at that rate, earnings have decelerated and the expectation for 2019 is about a 3% growth. And then going into 2020, we're looking at about 12% a projection for earnings growth.

Again, here's S&P 500 earnings with the projected numbers in 2019 and 2020, and then what I've plotted is now the S&P 500 on top of that in the black line. So now you can see just how clear that correlation is between stock prices and earnings. We say that a lot, in a lot of our one-on-one meetings and also in our presentations that the number one driver of stock prices, future values in the stock market, is corporate earnings and this graph does, I think, a very good job of showing that correlation.

What we have here now is within what drives that growth rate. So if we look at, "Okay, we can see that the stock market is driven by corporate earnings." Well, what drives corporate earnings? Here I've got a measure of the economy. This is nominal GDP and nominal GDP is before inflation is taken out. Nominal GDP has been growing at five and a half percent a year and then real GDP on this graph has been growing at 3% a year. Here is now corporate sales. So these are sales per share of the S&P 500 in the red line and again, you can see sales. So that's top line revenue follows nominal GDP.

And so as we measure, "Okay, well, then what drives stock prices?" Earnings drives stock prices. "What drives earnings?" We can see GDP drives earnings and these have been on a growth path here since the recession ended in 2009. So just to recap that section on the stock market. So stock prices are driven by earnings and earnings are driven by GDP. So we've got this framework that we're going to continue to work through, throughout the presentation, to really help you understand the economic machine that really drives the stock market here in the United States.

So, now let's go into the economic environment because what I want to now show you is then how do we expect earnings to grow based on what we expect GDP to grow at? So here is just a graph of real gross domestic product in the US, so that's all the goods and services that were produced. Net of inflation, we're at about $19 trillion and on this graph, all the gray bars ... And anytime you see a gray bar in any of the graphs, that's represented by a recession under these gray areas here. What you'll see is, in a GDP, GDP slows down during these recessions.

Some of them are more clear than others, but you can see definitely either some stagnation or some reduction in GDP when we go through those periods. Now, this is where we're at today. No slow down on the GDP chart. Now, here is a lot of data on this slide, but this is on the left-hand side, we've got the economy and in essentially, the economy is operating at full employment and at full potential.

All the bullet points, what I've got, those are all the things that we look at and I think the ones that, if anyone wants to look at, those are the important items to pay attention to when trying to measure the economy because there is a ton of data. You can actually go to one of the Federal Reserve's websites, the St. Louis Federal Reserve, and I think they have over 500,000 data points out there that you can actually monitor and track. So you can overwhelm yourself with information, but there really is only a handful of things that are extremely important.

And also this is a press release on the right-hand side from the Federal Reserve and just a summary of this press release was just recent slowing and very benign inflation. So basically what they're saying is we do see a slowdown in the economy and slowdown in corporate America, but inflation also has been pretty stagnant. That's one of the actually key things here with the Fed and what they're trying to do because their mandate is to keep inflation within a certain range and they say it's about two to two and a half percent.

In addition to that, they have another mandate of full employment as well here in the United States. When inflation is not very high, that gives them some some flexibility to stimulate the economy and whatnot, but they look at reducing or making the monetary policy a little bit more contracture, contract monetary policy when they feel that inflation is getting out of hand and the data doesn't suggest, at least the data that the Fed looks at, that inflation is getting out of hand and is part of the reason why they said they're comfortable pausing rates at this time.

This is a graph from the conference board and this an index of 10 leading economic indicators. This goes back to the 1960s and what you ... I watch this very closely because what we see here is that it peaks significantly before a downturn in the economy. On average, it's 13 months before this index of economic indicators peaks and then we actually enter into a recession. Just lately, the newest data came out and it eclipse the previous high that was hit back in September of 2018. So there was some fear that we might have peaked in the economy back in September because we hadn't hit a new high up until the March reading came out and we have eclipsed that.

So the economy, again, is continuing to grow and expand, not showing signs of peaking. And again, even when it does peak, that doesn't just mean that the market's going to roll over or that everything's going to roll over. It just tells us that we could be entering in a recession and there's definitely some lag time

before we enter into that recession. Here I've got, on this slide here, is actually all of those economic indicators. So here we've got the 10 on the top here and then we've got the level of them.

And the level I'm not as concerned about, what I tend to look at is the trend, are we improving? Are we stable or are we worsening in these trends? Because that will indicate if we're headed into a peak scenario and then headed into a recession. Down below, we have the coincident indicators. Now, these actually move in tandem with the economy and so we would expect these to actually rollover at the same time that we're entering in a recession. So the coincidence indicators, none of them are indicating that we are headed into a recession, which would be in a very short-term basis.

This interest rates spread, this is the yield curve that I mentioned that the Fed ... That's them pushing short-term rates above long-term rates and I'll show you some graphs on that and what we're looking at. Here's building permits. Housing has been slowing some. It's actually gone sideways for a couple of years now. Trend, most recent reading has been negative but it's not falling off a cliff by any means and again, average work-week starting to slow down a little bit too, but that is a data that does fluctuate a lot.

Now, what makes up GDP? We have a GDP equation and that is made up of four components. Consumption is the first component and that is a consumer spending. Then we have investment by private companies. So those are business investment. We have government spending as the next component and then the last piece is net exports. So it's how much do we export versus how much do we import? Those four components combined provide us with what our GDP is here in the US. So where are we? What are those four components? As I mentioned, we're at about $19 trillion. Of that, personal consumption is nearly 70% of our GDP. So that is the largest driver of our economy, is just consumer spending.

Next biggest area is private investment. So that's business spending, then we have government spending at 17% and we actually, because of our trade deficit, we are subtracting from GDP with our imports versus our exports. So when we look at then what direction GDP could be headed, we want to focus on the consumer because that is by and large going to determine what direction our economy is going to go. So where is the consumer headed? Again, just to recap, stock prices are driven by earnings. Earnings are driven by GDP and GDP is now driven by consumers.

So you can see this framework that we're building out onto our view on where stock prices are headed. So how are consumers doing? So let's look at that through the lens of the job market first. So we are at full employment here in the United States. The unemployment rate is at 3.8%. Initial jobless claims continue to tick lower, meaning that people aren't filing for unemployment, which is one of the very first indicators that we are headed for a slowdown. And

then also the labor market here in the US is tight. It's actually a pretty interesting to see this.

So this red line, this is job openings and then we've got total unemployed in the black line, and that's everyone looking for a job. So right now, we're in a situation, which has never happened before where we have more job openings than people looking for job. That's never happened before. So the labor market, we call this a tight labor market. When labor markets back in '09, you can see here that big gap, that's considered a very loose labor market. There's a lot of slack in the labor market. That slack has gone away and you can see, yes, the consumers are in control now of the labor markets and very interesting to see that happen.

Now, how are consumers wages going? How is spending going for consumers here in the US? So what I've got here, this is real disposable personal income per capita and basically what that means is that's all of the income after taxes. So the disposable piece's post-tax. So that's available for consumption and then we divided among all of the people in the US, so that includes babies all the way up to the elderly folks. And so we can see it had definitely had periods of stagnation in the great financial crisis here in '07, '08, '09 and then we've started to tick higher.

One thing that I think is interesting is we look at the year-over-year growth rate since the last recession. So since '09, real disposable income. So, again, after inflation has grown at 2.4% since '09, the previous expansion, so from '02 to 2007, real disposable income was only growing at 1.8%. So we're actually growing disposable income net of inflation faster than we have in the previous expansion here in the US. And that's a good sign because that does drive consumer spending disposable income.

Financial obligations ratio. So this looks at all of the fixed obligations around mortgage payments, consumer debt, automobile payments, rental payments, everything that is a fixed expense, and what we measure is the percentage of the disposable income that is now set towards those payments. We're at very low levels, historically speaking, and still so very sustainable, that tells us there's still a lot of discretionary spending that's available. So when we take the disposable income, we subtract out these financial obligations, we're left with discretionary spending and that I money that will flow through the economy via the personal consumption. And so very good data here to see when it comes to our future expectations for GDP growth.

Now, household debt, this is on the spending and income side. So how is household debt? Household debt has been fully repaired and again, the financial obligations record lows and indicating that people have money to spend. Now, here are the household assets. So these are consumer balance sheets. So at the very bottom, we have the nonfinancial assets, which is primarily real estate. Then we have the financial assets, which looks at your

investments and stocks and banking counts and what have you on top of that, and the growth rate, going back to 1990, has been on about a 5.6% compounded growth rate.

You can see we definitely had periods where household assets were growing faster than our long-term growth rates, but we are back on track to that. Now it started to get a little bit of ahead of itself, but just with the market pullback in Q4, we are just back to trend line on the financial asset growth rate. Now, here is the debt level. Now, in the next slide, we look at what do a households have on the debt side? Biggest chunk is on mortgages, then the next piece is consumer credit and then now we have some other expenses like student loans and what have you.

You can see we definitely had a peak there in 2007, 2008. Credit consumers delivered, essentially credit came down, if we look at all of the categories. Credit and debt has expanded since then and we are at all-time highs when it comes to household debt, but again, we have to put that in context of household assets. So when someone just talks about debt in a vacuum and they don't compare it to everything else, that doesn't give you the bigger picture, and so this is net worth. So this is the value that we have over and above the debt.

And so again, this is the net worth here in the United States, long-term trend, you can see represented by that black line there. We are just back to long-term trend levels. So we're not significantly higher or lower than long-term trend on our growth rates. You can see the real estate bubble that we had and the impact that had on household net worths and also the stock market bubble. Again, those aren't showing signs that households are even getting overextended on the asset side that could lead to an overexpansion and then a recession because of it. So households are in very good shape in 2019.

Now, on the liability side, this is actually what makes up a little bit deeper dive in into the liability. So we've got mortgages in the gold area, you can see as a percentage of that total debt where mortgages are at, a little bit of revolving debt to model loans, credit card debt, student loans and that's the one I wanted to point out. Student loans, you can see how those have grown over the last decade, but again, not a significant piece, and then we've got just some other debt levels.

Student loans are about 10%, almost 11%, of all household debt and student loans are getting a lot of attention because of some of the default rates in the level of student loans. But as a percentage of the total debt, not a significant portion across the US. These are delinquency levels and you can see the different components here and are any of them ... what trends are headed into, so 90 days plus delinquent. Credit cards aren't showing any increase in delinquencies. We can see now student loans have trended higher, had a definite spike here in 2012 but then had been pretty stable in terms of their delinquency rates.

Mortgages aren't showing any signs of increased delinquencies whatsoever. Auto loans are starting to trend a little bit higher in terms of delinquencies and then also on the revolving debt side, those are following a mortgages, no signs of increased delinquencies. So when we look at it on an aggregate, yes, auto loans currently are trending a little bit higher, but on an aggregate basis, what we're concerned about is, what direction are all of them headed? You can see here in '06, '07, they all started to trend a little bit higher headed into the financial crisis that started in 2008 and none of them are indicating that payments are getting delinquent and people are getting behind on their payments in any significant fashion.

Now, we do get a lot of questions about the government debt and what's going to happen with that. So want to go over just some different components to the government and the government debt. This graphic is the federal debt clock. You actually go to usdebtclock.org, and you can see a lot of different components to it, but this just points out the level of the national debt. It basically just shows a spinning number that looks like it will never stop and can be quite scary. But they also have gross domestic product and some other inflows in there, but it's interesting to see.

But it is designed to scare everybody when this is published. So let's put this in context a little bit. So who owns our debt in the United States? So what this is, this is all the different components to the federal debt and 60% of it is owned by domestic individuals or institutions. Federal Reserve actually own some, financial institutions, pension funds, mutual funds. Those are 60% of our holders of our debt and then foreign holders make up the other 40% of the holders of the federal debt.

When we look at federal debt as a percent of GDP, and this is how you want to look at the debt. You don't want to just hear the number and think of the number and compare that number to a historical basis. One, because it hasn't been inflated and so it's very hard to compare. So you want to compare it to GDP, which is, again, all the things that we produce in all of our output here in the US. So this is our federal debt that's public as a percent of the GDP. So this doesn't include debt to the government owns to itself. It just strips out all of that debt.

And basically, what you're seeing on this line is when the line is going down, that tells us ... It doesn't tell us that the debt's going down, it just tells us that we're not increasing the debt as opposed to increasing GDP. So GDP is rising faster than the debt is, in the US, and then when we have the spikes, that is when the debt is rising faster than GDP. And you can see around some of the wars, great depression, debt was a rising faster and GDP to fund those specific situations. And then post World War II, that's actually when we were the highest.

We have not been back to those levels in terms of debt to GDP, but GDP has grown significantly faster than the debt all the way up until great financial crisis and now we're starting to see a spike in that growth rate. Now, again, this doesn't mean the debt was going down, it just means GDP was growing faster than the debt. Now, this dotted line, this represents where we're at today and then from there is the projection from Congress onto what level they expect the debt to go ad compared to when they plug in all their different inputs.

So let me talk about what some of their inputs are and what some of their projections are, and then actually what some of the solutions could be. So these are the expenses. This is what the government spends money on. So social security, we've got healthcare programs, like Medicare and Medicaid. Other expenses, defense spending, non-defense spending, and then net interest. So when we talk about the overall debt, really what we're concerned about is this net interest because the ability to service the debt is what the government is focused on.

It's not focused on paying it down and it will never pay it down. The government is not centered to pay down the debt. All they are is they're incented to just make sure that they continue to make payments on that debt and that they're able to refinance it when the debt does mature, that they're able to refinance it to whether it's other domestic institutions and individuals or into the foreign markets. This gray line, this represents, again, where we're at today and then where the projected expenses are headed based on the congressional budget office projections.

So net interest is projected to increase and that is made up by two things. One, the level of debt, they are expecting it to go up. So interest payments would be higher just because there's more debt, but then also that interest rates are higher as well, which would increase the total dollar amounts that they are going to spend on it. But you can see it's not an exorbitant amount compared to some of the other components of the outlays from the federal government.

This is interesting. This is all of the revenues. So going back to the 1960, these are government revenues and then I've got, again, projected versus actual. So the gray, the dotted line here represents where we're at today and then what the projection is going forward. This dashed line now is showing what the projection was before the tax cuts and jobs act of 2017. So that was passed in December of 2017, went into effect in 2018 and so this is what the projection was before that got passed and then now you can see, compare that to the projection now.

So, definitely, a gap was created in the revenue line primarily because tax rates went down on personal and business side, but that gap definitely was starting to close in 2025. After that tax cuts and jobs act's set to expire. Now, next, we've got now federal outlays. So all the expenses that I just showed as a percent of GDP and one thing that's important to see is when the black line's above the red

line, that is when we had more revenue than we had outlay. So we had a surplus and you'll see that is rare. It is rare for the government to have a surplus and it probably will never have a surplus again. And if it does, it's probably not going to last very long.

You can see going back to the late '60s, the only surplus that we've really had since then was in the late '90s and it lasted for four years before we went back into a deficit. So we're always going to have deficits here in the US, it's just at what level of deficit do we focus on and does the government need to start making changes? Again, on the outlay side, you can compare what the current projection is and then the projection was before the tax cut was enacted in late 2017.

What I've got here on this next graph is just the federal deficits. So again, anytime you're looking at this and you can compare it to historical basis, it's important to do so. This red bar is the zero line and essentially anytime this red line is above the red bar, it's telling us we have a surplus. As I pointed out before, it is rare for us to have a surplus and we've had significant deficits going back 50 years and that's just the name of the game here in the US. 2018, 3.8% was the deficit as a percent of GDP projected to minus 4.4% in 2029.

So what can we do about it? Because as I showed in that graph up front, this is the projected federal public debt and you can see where we're at today as a percent of GDP. So this is where we're at today and then the projection is for it just to continue to grow and expand. The reason it's growing and expanding, it's because the projections are, we're going to grow the debt faster than we're going to grow the GDP. And so at what level would it take to hold the debt constant?

So what that means is that we'd still have a deficit. It's just GDP growth is projected to outpace the level of the deficit and that's at 2.9%. So using projected budget deficits, if they could keep that at a 2.9% level versus 3.8 where it's at today and then the projected of 4.4, then the government would be able to hold the debt to GDP ratio constant. So, again, they would never pay it off, but this would keep debt as a percent of GDP from expanding. So they don't even have to balance the budget, they just have to get to a point where budget deficits are just aren't as significant where they're at today.

And then if they're able to even get the budget deficit a little bit smaller than where it's at today, then this percent of debt to GDP would actually start to fall a little bit. So it's not a problem that I don't think the government can't fix. The 1%, we're talking 1% of GDP to be essentially cut from the budget, which is not an easy solution. It's simple in concept, in terms of actually functionality. What programs they would cut and how they would get to that point is a little bit more complex, but it's definitely not something that I think that they couldn't accomplish if they really focused on it.

Now, let's turn our attention now towards the Fed because I mentioned the stock market has been hanging a lot of its performance on what the Fed has been saying. Here is what's been happening. The Fed was promoting a 3% rate on other federal funds rate and we're sticking to that, and then markets really did not like that. So they did change their stance on that and what they're trying to engineer is what's called a soft landing. And I'll show you what that is when we talk about the yield curve because essentially what the Fed has done is they create where sessions here in the US.

They're designed to help either stimulate the economy or to make the economy contract a little bit when they play with interest rates, and essentially, that's kind of what they're doing. When we go into a recession, it's because economy got overheated and they took rates significantly higher than where they should have, and that really put a slowdown in the economy, much stronger than what they anticipated. This is a statement from John Williams. He is the president and CEO of the Federal Reserve. So Jerome Powell is in charge of the Federal Reserve. This is the number two guy, John Williams.

And essentially, what he's saying, in this statement, is that we are in an economic situation. This is march of 2019, by the way, is as good as it gets and that Fed funds rate is now normal. What they measure that buys, they have a concept that they call R-star and it's where they look at the federal funds rate and then they subtract the rate of inflation. Inflation right now is at about 2% as federal funds is at 2.4. So when you net those out, R-star is 0.4 and their target is at 0.5. So they're saying rates are neutral.

And if R-star was higher than 0.5, then we would say rates are ... They're going to cause a contraction in the market, meaning they're trying to slow down the economy or when R-star is lower than where it's at, they would say we're trying to be accommodated if we're trying to stimulate the economy. So they're saying interest rates are not ... They're not stimulating the economy and they're not contracting the economy. We're at the neutral rate right now and based on where they see, what I highlighted here was strong labor market, moderate growth and no sign of significant inflationary pressures, baseline outlook is quite favorable.

So that is where the Fed is right now. They think things are essentially in a very sweet spot when it comes to the US economy. The kind of the soft landing, as I mentioned, this is the S&P 500 going back to 1950s. Again, the gray bars are recessions and then what I've pointed out is at the bottom of this graph is the length of the expansions. So we've got 106 months in that recovery '58, '92 you see the different ... We're at 118 months in our expansion. Record, 120 months, was in the '90s. So not quite a record here yet, but getting close to eclipsing that.

But recessions, that's what we are scared of here in the US. You'll see here, this is the great financial crisis. US stock market down 60%. Peach before the

recession, bottomed at the bottom of the recession. This is the tech bubble bursting here in 2000. Again, a significant drop off around that recession. You see these other events here that have led to a recession in the past. This is a funny quote, I think it's funny. This is from Chairman Powell and he said, "There's no reason to think this cycle can't continue for quite some time, effectively indefinitely."

So what he's saying is, "We, the Federal Reserve, control the market." Essentially is what he's saying is because if they believe that rates are neutral and they believe ... They're saying, "We don't believe that there's going to be a recession in the future if we do this right. If we do this right, we do our job right, we'll never have a recession again." I don't ever think that's possible that we will never have a recession again. So, I'm not going to say that I believe him when he says this, but I just think it's interesting that that's what he's kind of saying.

But he is admitting that the Federal Reserve basically either prevents a recession or causes a recession. It goes both ways with this comment. So this is yield curve and so this is what the Federal Reserve basically controls, and this is why we talk about it so much. Essentially, what this is, this red line is the difference between the very short-term rates, which is the Fed funds rate, compared to the 10-year government treasury. And so anytime this number, this red line is above zero, that just tells us that short-term rates are lower than long-term rates, which is generally what people think about.

If you think about, "Okay, if I have money in a money market account, I would expect to make less interest on that than if I bought a 10 year CD." If I bought a 10 year CD, I expect to get paid a higher rate of interest than if I had money in my money market account and the reason being is because I'm taking on some risk with a CD. I'm not at risk of losing my money, but I'm at risk of inflation, so my purchasing power risk, and then also have higher rates because if I lock up my money for 10 years, there's a risk rates might be higher in a couple of years and I could have had a higher rate. So I have some opportunity costs potential.

And so that is how most people think about the yield curve and that's how it works most of the time. But in these periods where the red line is below zero, what that is, is indicating that short-term rates are higher than long-term rates. And a lot of people, when I talk about this concept, they remember this section here. This got so bad that it doesn't even fit on my graph. You can see it's cut off here at the bottom, but this was in the early '80s. President of the Federal Reserve back then was Paul Volcker and he raised short-term rates so high that you could get darn near 20% in a money market account.

But if you locked up a 30-year mortgage, it was 13% which again was very high, but you're going to take out a 30-year loan and only pay 13% but you could kept your money in cash and made 20. So that spread was significant. There's a big difference in that spread during that period. And then lately, this is going back last 30 years, you can see the recession before the early '90s. This is the

recession headed up in the tech bubble bursting and then this is the recession of the great financial crisis. So what's happened proceeding all of these recessions, post World War II, is the Federal Reserve has pushed short-term rates higher than long-term rates causing a recession.

You could see very clearly that the recession has followed after every time we've got to a point where the yield curve has inverted, where short-term rates were pushed higher than long-term rates. It's not just barely pushed over, we're seeing a significant almost 1% in many of these scenarios before the economy starts to really slow down. And the reason it causes a slowdown in the economy is that is when credit gets tight, what this is signaling is how easy is it to get credit and what's the cost of credit? Because banks make loans to individuals and when banks borrow money, they borrow money from, call it essentially the Federal Reserve, and then they borrow at the very short rate and then they lend it out along the longer term rates.

So you take out a 30-year mortgage, they're lending you money for 30 years. You take out a car loan, they're lending you money for five, six years, whatever length of your car loan is. If they have to take out a loan at a higher rate than the rate they're lending it to you at, they're losing money and so that causes credit conditions here in the US to become very tight and it slows down the economy. All this does is indicating how quickly do we think the economy's going to slow down based on this spread? So what I've got here is actually here is where we're at today. We are not below zero.

When we look at the Fed funds rate compared to the 10-year treasury, we're at about 0.1, that's the slope of the yield curve graph here. So let me show you now, here, then compared to some different key levels. So this is blown up from early '80s now. You can see a little bit clearer this yield curve and then the recessions that have followed once the yield curve inverted. Now you can see here, this is where I've highlighted the different pieces where how significant this yield curve has to get before we expect it to lead to our sessions.

So we're looking for something that doesn't just barely eclipse the zero line, we're looking for something that continues to go down. Half a percent or 1% below zero on the yield curve inversion to the lead to a recession. So now let me show you how this compares to the stock market and so how does the stock market perform when we have these different yield curve inversion? So this black line is the stock markets, the S&P 500. Now I've got the yield curve on top of this. So this is going to get a little messy. So, follow along here.

I've got a lot of different things I'm going to point out on this graph, but this is showing what the stock market's done, what the yield curve imposed on top of it. Here are the previous times when the Fed has pushed short-term rates significantly higher than long-term rates causing a recession, you kind of see where those data points are. Next, what I pointed out is exactly where we're at today and then compared it to history. So this is where we're at today, point

one. We have not inverted yet and this is where ... This is in '06, yield curve didn't invert and this is in '95, similar situation.

And so this is the soft landing that we're talking about. Basically, the Fed saying, "We are paying very close attention to this and we're not going to invert the yield curve. So we're going to either back off some of our stance on pushing rates higher or we're actually going to cut rates," which there's some people in the current administration, Larry Kudlow is one of them, that is calling for a cut in interest rates. And this is why he's calling for a cut, he's saying, "You should not invert the yield curve." That's basically why the administration is calling for a cut rates.

The economy's moving and expanding even where rates are at. So it doesn't necessarily mean that we need to cut rates, but they're just pointing out to the yield curve as a reason for that. Now, when we've had periods like this, and if the Fed can do this right, which, again, there's a lot of attention being paid to this, we've seen previous periods where we've got to this point in the yield curve where stock markets have performed significantly well during these periods where we've got to this point. So this is in the late '90s. Got very close to yield curve inversion and then this is the stock market performance post that.

Yield curve invert eventually, but again, it did take some time. This is '98, then it started to significantly invert back in 2000 to lead to a recession. And then this one here is back in '04, '05, '06. We had a soft landing here in '06 and we saw a stock market continue to grow and expand and perform on a positive notion where we're at today. So that is where we're at today and I think considering all the economic fundamentals ... So this is all part of the framework when we add on top of health of the consumer, what does job market looking like? What are wages looking like? And then what does that lead for future stock prices?

I think that supports our thesis that we expect to see future stock prices continue to increase here in the US, and that leads us to where are we headed? This is our framework when we look at the economy here in the US and what our outlook is for higher stock prices. So, right now, we do have a tight labor market. Our wage's rising. These are all questions that we ask ourself and they lead are consumers spending more because wages are going up? GDP continues to grow and expand. Corporate earnings then rise, which then leads to higher stock prices.

So that's the economic machine here. That's what drives higher stock prices and so all of these are actually in a very good shape right now. We do have a very tight labor market as seen by the number of job openings compared to the number of people looking for jobs. Wages are going up. Real disposable income is continuing to increase. Consumers are spending ... We are seeing that credit is expanding. They are taking on a little bit more depth but not significant amounts of debt and they're not defaulting on it either.

So that leads us to expect that GDP will continue to grow in the US. It's definitely not going to continue to grow at the rates that we saw in the '90s. We are much more mature economy now and our growth rates are going to be not as high as they have been in the past, but still, positive growth is really what we're concerned about. Corporate earnings are projected to continue to rise and I expect them to because of the other inputs that we look at. So that leads us to higher stock prices and so when we put all that together, that doesn't mean ...

Again, we're not going to have volatility. They'll have pockets of volatility here in the stock market, but that volatility should be short-lived and will alleviate itself to the upside in quite a fast fashion, like we did see in Q1. We had a pullback in Q4. We had a recovery in Q1, now we're back to all-time highs and we talked about that at our breakfast in December about the health of the economy and why, even despite the volatility, why we expect stock prices though to recover from that.

Now, on a short-term basis, this is actually published by CNN every day. It's a Fear & Greed Index and so this helps us ... I look at this as more of just a very short-term sentiment indicator and it's showing a little bit signs of greed. The snapshot was taken last week and we are seeing that in market last couple of days have come down a little bit, and that's to be expected. We've had a quite a run here since January and we're going to have some small pullbacks even in a strong bull market. And when we see this number start to creep up, that will definitely lead to a little bit of short-term volatility.

One year ago, markets were in a fear mode. You can see that by the indicator there at 33 and there definitely was a rebound post this fear reading back then in 2018. Now, where do we go from here? This is data that we look at. I really do like looking at how markets have performed on a historical basis and compare it to situations that have been similar. So what we've done is we've taken the S&P 500 and we said, "Okay, let's look at all the times that it corrected at least 10% from all-time highs."

So what that means is market hit an all-time high and then went down at least 10% or more after it hit an all-time high, and that is represented here in this section of the graphs. A lot of numbers on here, but then once it hit a new high, we wanted to look at how many days did it take to hit a new high. See, kind of a wide range there but right now, we hit a new high, April 23rd, 2019. So it took 95 days from the market to peak to hit a bottom, which was represented there on Christmas Eve, 12/24/2018, down 19.8% and it took 120 days to recover.

So then what we wanted to look at is then in previous scenarios where we've had a situation like this where the market peak went down 10% and then went back up to an all-time high, what happened after we hit that second all-time high? And what we can see, I pointed out here in the green box is one year later, we've seen stock prices advanced on average 9.1% but the median return, so

medians takes out the outliers is actually higher, 11.2% with positive returns 84% of the time. So we have significant tailwind when we look at this and say, "From historical basis, when markets hit all-time highs, they tend to move higher."

So over the next 12 months, we expect stock prices to move higher, a very strong dataset here to support that and then when we couple that with our framework when we look at, "How healthy is the economy? How healthy is the consumer? Does that lead to better corporate earnings, which would lead to higher stock prices?" And I'd say the answer's yes, which then I believe that we're going to see this play out. This is not a point to point basis. So, again, not to say that it's going to go in a straight line, we will expect some volatility, but we look up a year from now, we definitely do see higher stock prices.

And so with that, I know we've gone just a little bit over the hour mark here, but that's just to summarize our overall framework. That's our outlook and those are the components and so our goal is actually to have these webinars on a quarterly basis and cover this data, and a lot of the data will be similar. So that, one, we're going to point out the trends from period to period so that I can show you, "Here's what we were looking at in previous sessions and here's where that data is today."

And so you can understand what our view is on the market and that does have implications on our weightings and that's our ... One, from a high level, how much do we have in stocks versus bonds? But then all of the different asset classes that we own inside the investments as well. So with all that being said, all that, that we appointed out on this presentation, we are maintaining our equity holdings. We believe that markets will continue to move higher, so not looking at underweighting stocks at this point, considering all of that and then also of course keeping things rebalanced and whatnot. So you'll see those situations happen as we go through.

Now I'll take a second here, compile some questions just to see if anyone has any questions, feel free to submit them. I see a few of them coming in here today and as Bill mentioned as well, we are going to have a replay available for this in very short order too. So I know we cover a lot of stuff, so sometimes people like to come back and review those things as well. So I'll just take a second here and get these questions compiled.

Okay, got a few questions here. One of the questions that I've gotten is on the unemployment. I talk a lot about unemployment in the jobs market and the question is on the unemployment rate. So I didn't show a graph of that. I typically do, but the unemployment rate, yes, it's about 3.8% here in the United States. The question is, does that represent ... Is that a good metric to follow? I hear a lot about unemployed people or underemployed or people not getting counted and so should we be watching the unemployment rates?

So what the unemployment rate does measure, at least the one that is widely followed, is just individuals that are actively looking for work that aren't employed. So if you dropped down in the workforce, you're not included into the unemployment rate. So there's a few different measures of that. The government does measure how many people have taken a job that they're overqualified for or have dropped out of the workforce and that number peaked in 2010, and that was close to 17% and now it's around 7.5%, and the long-term trend is actually closer to 10.

So that number of individuals that are both unemployed and underemployed and dropped out of the workforce has trended significantly lower since the great recession in '09. So, even though we see the headline number at 3.8%, that doesn't necessarily include everybody, but the broader measure is on that same path. It's still on that same curve. The other kind of component with the unemployment rate is around wages too. People ask about wages a lot and is that a good metric? Because they hear wages aren't rising.

I showed that real disposable income per capita. Now, when we look at that measure, that can get skewed by high-income earners because when we just take the number and divided into the population, if there's a high number, that's going to skew it a little bit. But we can also just look at growth of wages for production and non-supervisory individuals as well, and that number has been continuing to trend higher just as the real disposable income as well. So when we break it up and we look at it in different components, where we look at what are the executives and management making compared to what the production and non-supervisory individuals are making, they're both headed in the same direction and still growing. So, again, on the wage front, things are looking good for everybody.

A question here I have too is on the projection of the debt to GDP, that ratio and when the projection was run out to 2049, is that a concern? In a vacuum, we would prefer less debt than more debt, but at the same time when rates are low, debt is a way to pre-fund certain things that we couldn't do if we didn't have the cash available. And so when we are taking on long-term debt at very low rates, whether it's an individual or institution or government, they're able to fund a lot of different projects and what have you, that they may not have been otherwise able to do so.

Now, what we're concerned about is just their ability to service debt, not ever pay off the debt. Just to be able to make the payments on it and the way they're able to make the payments on it is future tax revenues. If the economy can continue to grow at a ... And when they're projecting out their growth rates, by the way, on the economy, they're only using about 2%. Q1 GDP in 2019 just came in at 3.2, very strong number, but when they are projecting it out, they're using 2%. So if the economy can continue to grow and expand, that actually will grow future tax revenue, which will help continue to make those debt service payments.

The last question I've got here and then I'll let you all hop is, "One year after the tax cut, what is the economic indication of the effect?" We still haven't seen much in terms of flows except for this Q1 number. I think this Q1 GDP number, 3.2%, was a strong number and that was definitely something that I think had some impact from the tax cut in 2018, kind of led to that, but it still takes time. There's a lag time from when a policy is enacted to when we actually see the effects and those lag times can be up to 18 months in some cases.

So seeing that, that tax cut happened last year, we're pushing about a year, a year and a half now. So I think we'll start to see more and more data that will indicate what's the impact. Now, first and foremost, on the corporate earnings front, that was where we saw the aspect of corporate tax cuts, just earnings increases in just the underlying data right there. So things are shown they're on a real-time basis when it comes to those tax cuts.

I want to thank everyone for attending. As I mentioned, we will have a replay available. We'll send you out the link to that replay once it is live and I look forward to having another one of these webinars at the end of Q2 where we'll recap Q1, Q2 and then go over our outlook for the rest of the year because this economic data, I mean, very strong now, but we do pay close attention to this and our outlook will adjust as the data adjust. So thank you, all, and we will chat soon.