ECONOMIC AND FINANCIAL MARKET OUTLOOK - 2018

Our *Preliminary* Expectations For The Coming Year

Prelude:

Before sharing our expectations for 2018, a few brief comments on 2017 are warranted.

2017 has been a very strong year for domestic financial markets (particularly equity) and investors in general. It has also been a year far from what most economist/strategists had anticipated as the year began. Rather than rising interest rates, an increase in the value of the U.S. dollar relative to most global currencies, and the resulting increase in equity market volatility; the opposite has been true. Interest rates (10-year U.S. treasury bond yield) have actually declined, the dollar has fallen, and the S&P 500 has experienced one of the lowest levels of volatility in decades while providing strong returns. So much for consensus.

Looking Ahead:

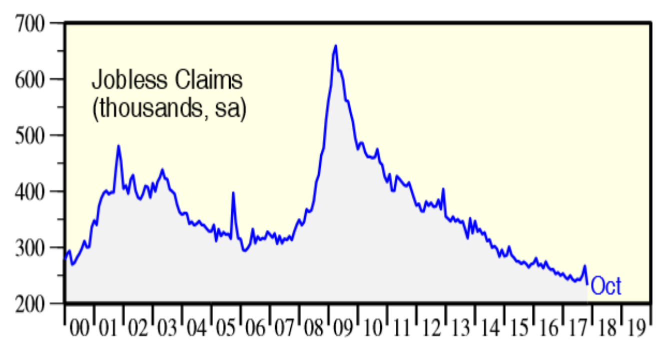
As we approach the end of 2017 we are completing another year of gains for the S&P 500. Spurred by the expectation of tax reform (or at least tax cuts), historically low interest rates, rising corporate profits, renewed global growth and a domestic pro-growth agenda, the S&P 500 has provided a total return of +20.7% through December 8, 2017.

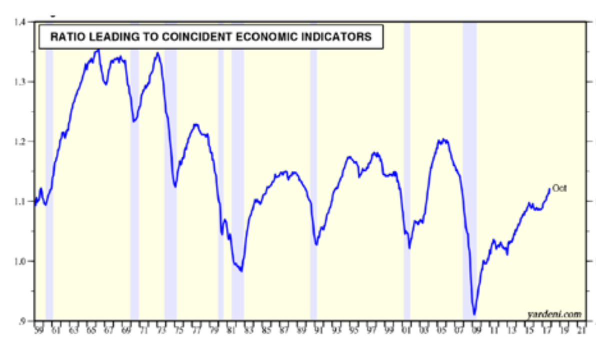
While we are not “blindly” bullish on forward returns for the stock market in the near-term, we remain optimistic. As markets reached new highs this year, we have “trimmed” back equity positions and will continue to do so in order to stay within portfolio guidelines. However, as long as U.S. and global economic data remain positive and don’t indicate the likelihood of a recession, we find no reason to ***significantly*** alter equity positions.

Some investors may be inclined to think that after a meaningful rally the stock market is likely to fall (remember last year was a +12.6% for the S&P 500), however, there is little correlation between one year’s equity market return and the next. As we have previously described, “bull markets don’t die of old age”, they fade as economic trends soften. At this time, remain invested.

The Economy:

Economic data is currently not forecasting a recession in the foreseeable future. In fact, the opposite appears true. Two easily and broadly watched economic indicators e.g., Weekly Jobless Claims and the Ratio of Leading/Coincident Economic Indicators are two such forecasting tools. Currently, the Weekly Jobless Claims report shows jobless claims at the lowest point in decades, and the Leading/Coincident Economic Indicator is in an upward trend. See below.





Source: Yardeni Research, Inc.

Shaded areas denote recessions

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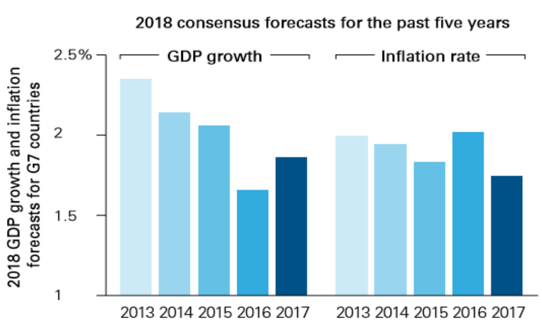
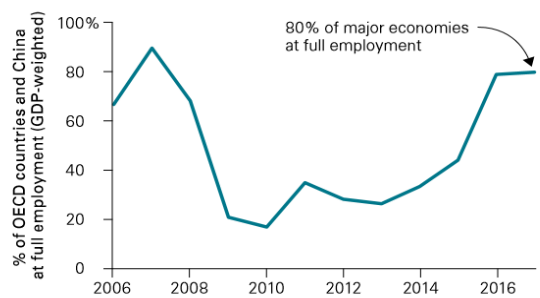
The trends displayed on the previous page, along with others, have pushed consumer and business confidence to levels not seen since the years prior to the financial crisis. The increasingly tight labor market, combined with increased housing values, stronger balance sheets and positive financial market returns have set the stage for continued optimism and a pick-up in consumer spending (70% of U.S. GDP) which is extremely important to the domestic economy.

Improving economic fundamentals are not only being seen in the U.S., but appear to be occurring around the globe, particularly in Europe and Japan. With increasing consumer demand, low inflation (in part the result of technological advances and global competition), and historically low interest rates, the stage seems set for another positive year of economic and corporate earnings reports ***("it's all about the earnings")***. S&P 500 earnings per share are anticipated to rise an additional 10% in 2018.

Global Growth & Economic Fundamental Indicators



Note: The Group of Seven (G7) countries are the industrialized democracies Canada, France, Germany, Italy, Japan, the United Kingdom, and the United States.
Source: Vanguard, based on data from the International Monetary Fund.



Source: Vanguard, using data from the Organization for Economic Cooperation and Development and the International Monetary Fund.

The Bottom Line:

Geopolitical events, terrorist activities, and the proverbial "Black Swan" are all factors we consider and discuss regularly, but are very difficult to anticipate. Economic data e.g., employment, capital spending, personal income, debt levels, inflation, interest rates, etc. are always open to interpretation, but are reasonably easy to obtain and to evaluate (hopefully correctly).

Based upon the fundamentals discussed above and in previous ***Outlooks,*** we continue to see a positive environment for financial assets. We anticipate a continued moderate, synchronized global economic expansion, along with a gradual "tightening" by central banks leading to somewhat higher interest rates and a modest pick-up in inflation.

We remain aware that the U.S. equity and, probably, the fixed-income markets are valued at premiums to historic valuations. However, we also believe that economic fundamentals, in addition to synchronized global growth, potential changes in fiscal and regulatory policies, and higher corporate earnings support those valuations.

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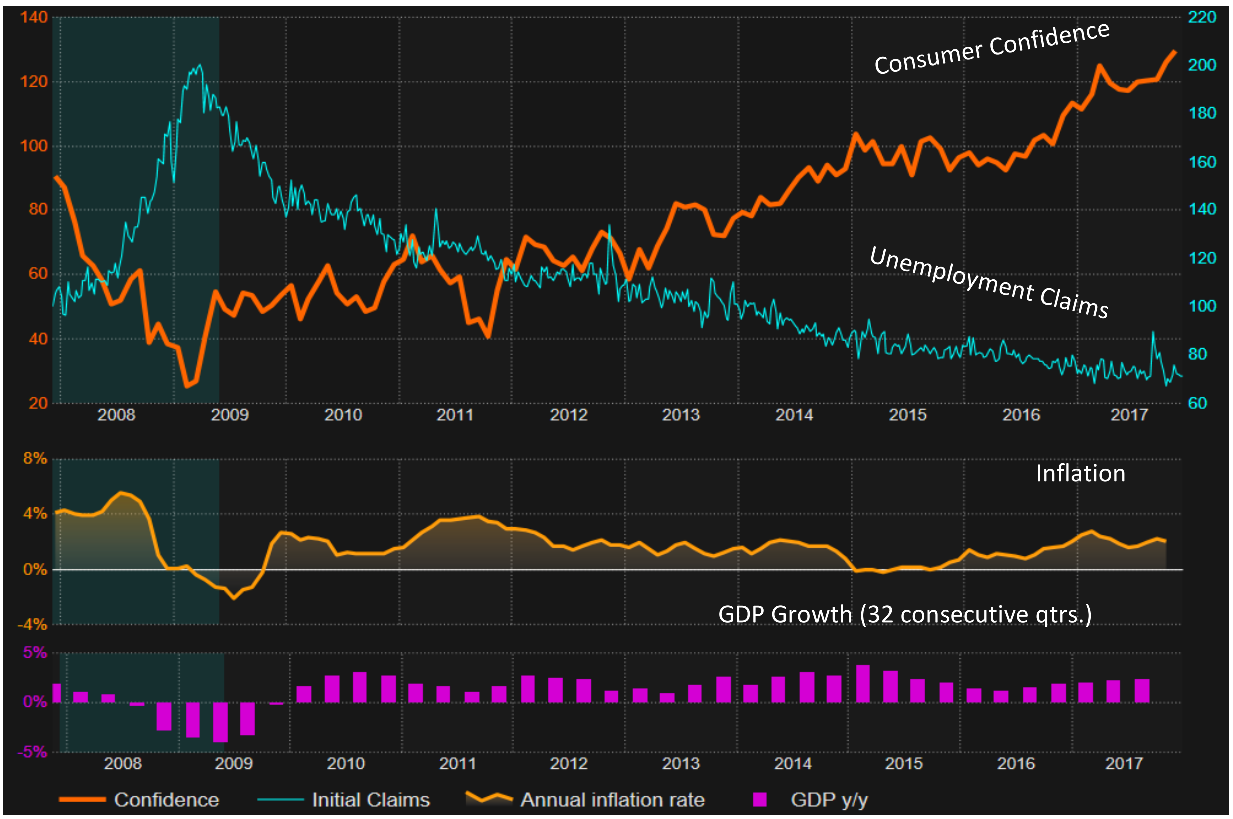
We regularly ask ourselves, "What would cause a change in our current positive outlook and portfolio "positioning"? The answer (as in previous Outlooks): a change in direction (decline) of corporate profits and/or consumer sentiment; a cessation of growth in China or the Eurozone; a spike in the price of energy; and/or an inversion of the yield curve (rates on short-maturity investments exceed those on longer-maturity investments). We do not anticipate a change in any of the above in the near future.

The chart below, which we have shared with readers regularly, provides strong evidence that positive economic trends remain firmly in place.



Source: Thomson Reuters Datastream

With respect to portfolio strategy, we believe that while the environment appears positive and healthy, after almost a decade of rising values, it is important for investors to remain disciplined, "balanced", diversified, both globally and by asset class, not react to short-term "chatter" and to be realistic with respect to anticipated returns.

At this time, we continue to emphasize investment in the shares of high quality (always) companies that are operationally leveraged to an improving economy such as technology, industrial and financial companies, but also those exposed to long-term transformations such as that which is occurring in the health care industry. With respect to fixed-income (bonds), we recommend maintaining a short-to-intermediate average maturity to reduce volatility and potential loss of capital in a rising interest rate environment.

We welcome your questions, comments and/or critique'.

We wish all, a memorable, peaceful Holiday Season and a healthy & Prosperous New Year

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The opinions voiced in this material are for general information only and are not intended to provide specific advice or recommendations for any individual. All performance referenced is historical and is no guarantee of future results. The economic forecasts set forth in the presentation may not develop as predicted and there can be no guarantee that strategies promoted will be successful. All indices are unmanaged and may not be invested into directly.

There is no guarantee that a diversified portfolio will enhance overall returns or outperform a non-diversified portfolio. Diversification does not protect against market risk.

The prices of small and mid-cap stocks are generally more volatile than large cap stocks.

Stock investing involves risk including loss of principal.

Bonds are subject to market and interest rate risk if sold prior to maturity. Bond values will decline as interest rates rise and bonds are subject to availability and change in price.

High yield/junk bonds (grade BB or below) are not investment grade securities, and are subject to higher interest rate, credit, and liquidity risks than those graded BBB and above. They generally should be part of a diversified portfolio for sophisticated investors.

Because of their narrow focus, sector investing will be subject to greater volatility than investing more broadly across many sectors and companies.

International investing involves special risks such as currency fluctuation and political instability and may not be suitable for all investors. These risks are often heightened for investments in emerging markets.

Investment advice offered through Stratos Wealth Partners, Ltd., a registered investment advisor.

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