LEDYARD
FINANCIAL ADVISORS
Plan well. *Live well.*

INVESTMENT THOUGHTS

APRIL 2018

DO YOU HAVE A SPRING IN YOUR STEP?

The warming sun brings us renewed energy. Our proverbial solar batteries are recharging as we build enthusiasm for adventures, projects and fun with friends and family. In my neighborhood the doggies are outside lounging in driveways, catching rays, perhaps pacing around but not quite ready to chase the squirrels. Greening grass. Beckoning trails. Baseball season in full swing. Life is good!

What about the markets? Is this a passing rain, a thunderstorm or a hurricane? First I offer time creation magic then some family legacy ideas and finally perspective on the stormy markets.

Spring cleaning

> *"Keep only those things that speak to your heart. Then take the plunge and discard all the rest. By doing this, you can reset your life and embark on a new lifestyle."*
>
> *Marie Kondo*

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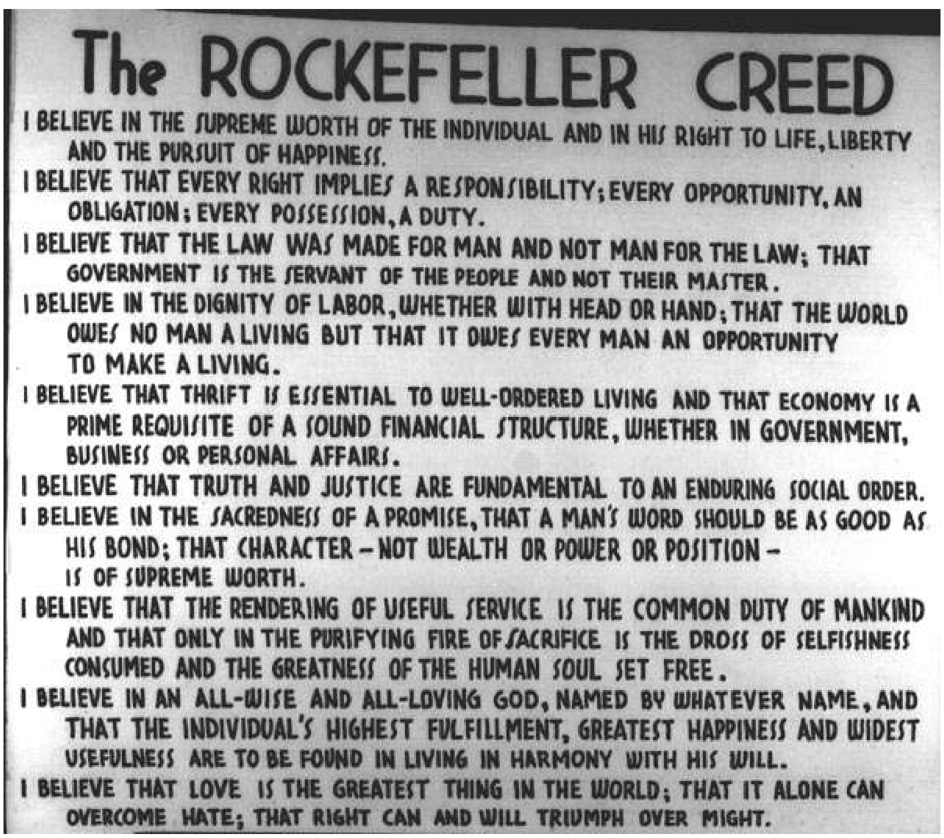
In keeping with Kondo's philosophy, we at Ledyard are here to help you simplify your life so you can focus on your goals, hobbies and relationships. Does bill paying speak to your heart? If not, let our capable professionals handle those pesky property tax, insurance and credit card bill payments from one of your accounts. After all, time is your most precious resource.

Add a spring to your legacy

Have you heard the expression "shirtsleeves to shirtsleeves in three generations"? A person builds significant wealth and his or her children benefit from it. Then the grandchildren and extended family expect it to continue without paying too much attention and before they realize it their wealth is gone, frittered away, evaporated into the winds of life.

I read an interesting article about the Rockefeller family which has managed to retain its values and its wealth over seven generations. Other families of great wealth from the same era have decidedly failed. John D. Rockefeller's values are actually inscribed in marble and on display at the Rockefeller Center in New York. His words are not a quick read, they have heft and are particularly poignant in today's world so I urge you to take your time absorbing them.



The ROCKEFELLER CREED

I BELIEVE IN THE SUPREME WORTH OF THE INDIVIDUAL AND IN HIS RIGHT TO LIFE, LIBERTY AND THE PURSUIT OF HAPPINESS.

I BELIEVE THAT EVERY RIGHT IMPLIES A RESPONSIBILITY; EVERY OPPORTUNITY, AN OBLIGATION; EVERY POSSESSION, A DUTY.

I BELIEVE THAT THE LAW WAS MADE FOR MAN AND NOT MAN FOR THE LAW; THAT GOVERNMENT IS THE SERVANT OF THE PEOPLE AND NOT THEIR MASTER.

I BELIEVE IN THE DIGNITY OF LABOR, WHETHER WITH HEAD OR HAND; THAT THE WORLD OWES NO MAN A LIVING BUT THAT IT OWES EVERY MAN AN OPPORTUNITY TO MAKE A LIVING.

I BELIEVE THAT THRIFT IS ESSENTIAL TO WELL-ORDERED LIVING AND THAT ECONOMY IS A PRIME REQUISITE OF A SOUND FINANCIAL STRUCTURE, WHETHER IN GOVERNMENT, BUSINESS OR PERSONAL AFFAIRS.

I BELIEVE THAT TRUTH AND JUSTICE ARE FUNDAMENTAL TO AN ENDURING SOCIAL ORDER.

I BELIEVE IN THE SACREDNESS OF A PROMISE, THAT A MAN'S WORD SHOULD BE AS GOOD AS HIS BOND; THAT CHARACTER – NOT WEALTH OR POWER OR POSITION – IS OF SUPREME WORTH.

I BELIEVE THAT THE RENDERING OF USEFUL SERVICE IS THE COMMON DUTY OF MANKIND AND THAT ONLY IN THE PURIFYING FIRE OF SACRIFICE IS THE DROSS OF SELFISHNESS CONSUMED AND THE GREATNESS OF THE HUMAN SOUL SET FREE.

I BELIEVE IN AN ALL-WISE AND ALL-LOVING GOD, NAMED BY WHATEVER NAME, AND THAT THE INDIVIDUAL'S HIGHEST FULFILLMENT, GREATEST HAPPINESS AND WIDEST USEFULNESS ARE TO BE FOUND IN LIVING IN HARMONY WITH HIS WILL.

I BELIEVE THAT LOVE IS THE GREATEST THING IN THE WORLD; THAT IT ALONE CAN OVERCOME HATE; THAT RIGHT CAN AND WILL TRIUMPH OVER MIGHT.

Can you describe your family's values? The Rockefeller family members meet twice a year to talk about goals, acknowledge their individual and group accomplishments, welcome new members and brainstorm new projects. They have their family traditions and find ways to record and keep alive their family history. They also use philanthropy to strengthen their family bonds.

On the other side of the world are many members of the Kong family. Have you heard of them? Perhaps you have heard of their original founder - Confucius. The Guiness Book of World Records has certified his as the world's largest recorded family tree. It spans 83 generations and over two million descendants. Groups of them meet regularly, participate in ceremonies and share traditions and values. Confucian values, which have become core social values in many Asian countries, include:

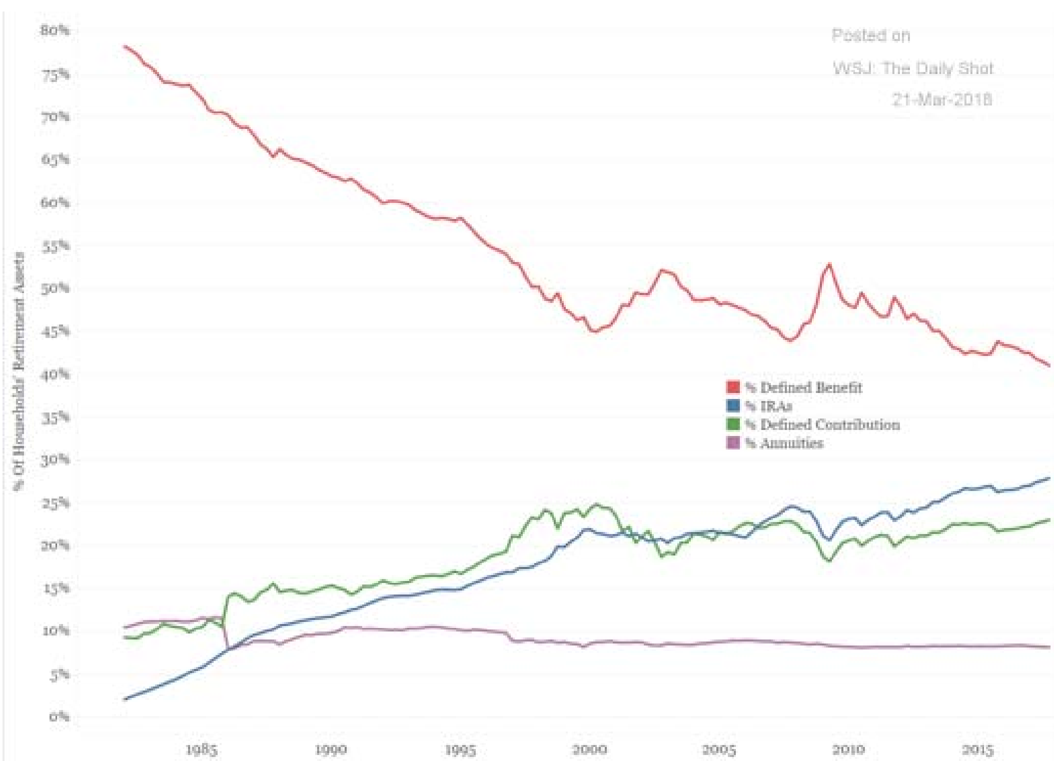
- Benevolence (humaneness toward others)
- Righteousness (acting morally)
- Propriety (proper conduct)
- Wisdom (knowledge of right and wrong)
- Fidelity (reverence to parents, bringing honor to the family)

Having watched interviews of Kong family members I was most impressed with a key concept they share with each other and emphasize to their children: be role models in society. After all, being descendants of one of the leading philosophers in human history I suppose they feel a little extra pressure to behave!

Beside trips to New York and China what can you do on behalf of your children's children and their children? I offer a few ideas and your Ledyard Financial Advisor team can offer more.

1) The era of companies taking care of their employees during their lifetimes is over. Pensions? See the rapidly dropping red line in the chart below. Perhaps gifting funds to your very youngest extended family members so they can open or add to Traditional or Roth IRA accounts can become a foundation for multigenerational financial security. Your family members will be less likely to be a burden to their parents, children or society and perhaps a family tradition will be established.

Figure 1 – Household Retirement Assets



Source: The Wall Street Journal, Bianco Research

2) The new tax law raised estate tax limits to $11.2 million per person ($22.4 million per couple). Those provisions expire in 2025 or perhaps sooner depending on future congressional and presidential elections. Although passing wealth to immediate heirs is easier now, there are asset protection trusts, generation skipping tax trusts and other estate planning vehicles that may make sense to protect the family assets from overspending, divorces and/or lawsuits. It worked well for the Rockefellers.

3) We can help with business succession planning from developing a transition strategy to building an advisory team to enhancing valuation.

4) Whether you already have family meetings or would like to plan your first one we would be glad to help with developing an agenda, providing a guest speaker or being available to give some basic financial guidance to younger members of your family.

The markets spring a leak

Complacency had settled in after last year's steady returns. However, at the end of January US bond and stock markets swooned on the prospect of higher inflation. International markets reverberated. Here is a longer term view on the Fed's favorite measure of inflation which it targets at 2%.

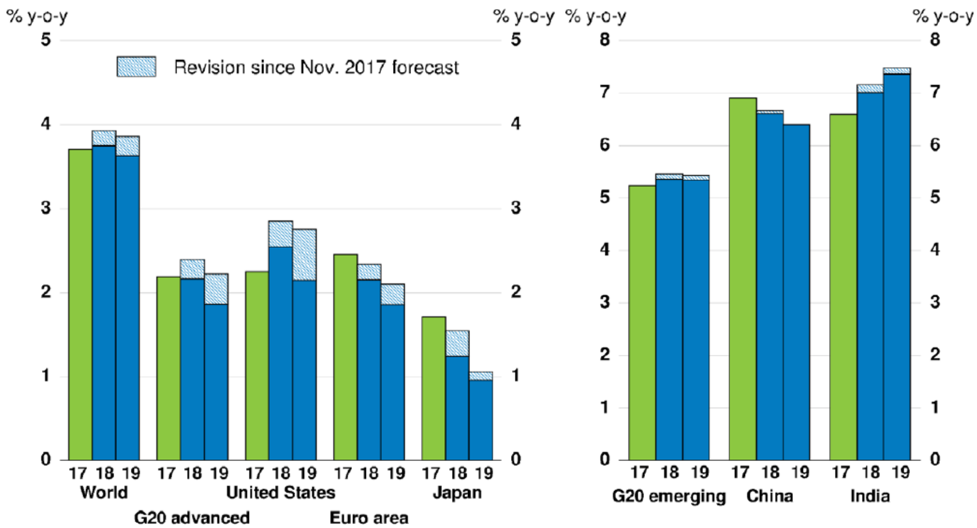
Figure 2 – Personal Consumption Expenditures (Core - Excluding Food and Energy)

Source: US Federal Reserve

Medical care and housing are large components of this index and could rise in the near term. However, baby boomers are shifting from corporate health plans to Medicare, which is gaining negotiating power with providers, and technology is beginning to affect medical costs. Mortgage lenders are unlikely to loosen their lending policies so real estate prices (outside of tech and financial hubs) will grow apace. Wage growth has the potential to drive inflation there are plenty of people who left the workforce in 2009 who are just now jumping back in. Technology applications are also delaying the need for employers to raise salaries.

Markets were revitalized in February with a string of good economic statistics and the perspective of a synchronized global economy.

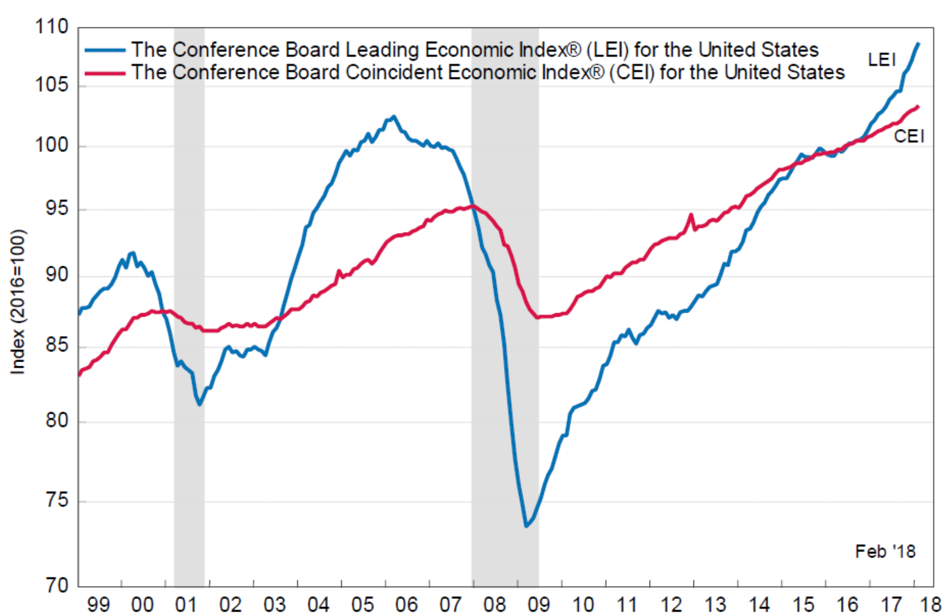
Figure 3 – Global GDP Growth Forecast (2017 - 2019, % year over year)



Source: Organisation for Economic Co-operation and Development (OECD)

US tax reform is adding meaningful profits to many public and private companies. A widely followed index of leading economic indicators showed recent strength.

Figure 4 – Leading Economic Indicator Index



Source: The Conference Board

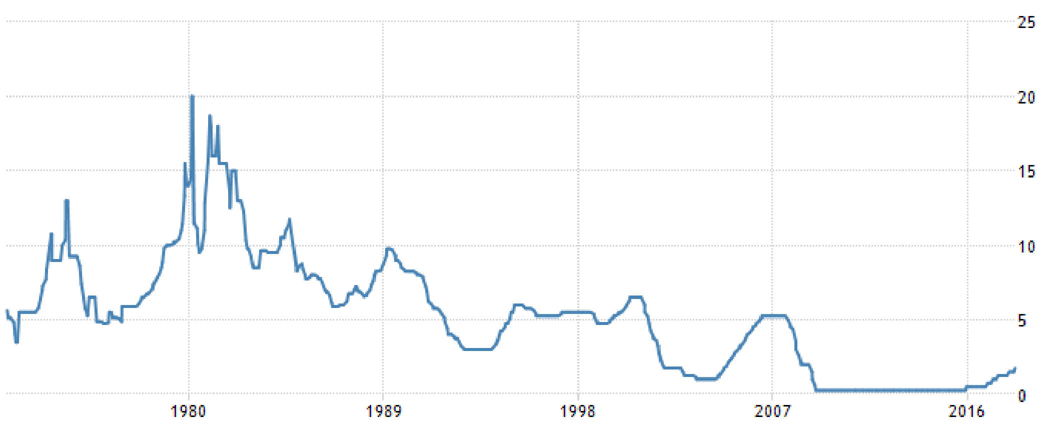
There are numerous components of the index including:

- Initial claims for unemployment
- New housing permits
- Hours worked and new orders in manufacturing
- Stock prices
- Consumer expectations for business conditions
- Bank and brokerage lending activity
- Borrowing costs

Most of these factors are holding strong. Notice in the chart above that in the several months prior to the two previous recessions (shaded in gray) the blue line took a significant dip. No dip, no recession. The rate of unemployment moves slowly and a reversal generally portends a significant deceleration in the economy. Corporate tax cuts and government spending on defense and infrastructure will certainly boost the economy but national debt and long term budget deficit projections loom as key concerns.

In March the new Federal Reserve Chairman, Jerome Powell, held his first news conference and earned some measure of respect from the markets for his caution and intent to continue established monetary policy. As expected, the Fed raised short term interest rates by 0.25% to a range of 1.5% to 1.75%. The figure below shows that the cost of capital is historically low. The Fed does need some running room in case something unexpected happens in the future and it needs to lower rates to support the economy.

Figure 5 – US Federal Funds Rate



Source: The Wall Street Journal, Trading Economics

Chairman Powell and his committee members are intending to raise short term rates by about another 1.75% to reach 3.5% by mid-2020. This would make the Prime Rate rise from 4.75% to about 6.5%. The economy will have to chug harder to climb that hill. Notably central banks in Europe and Japan are keeping rates lower for longer.

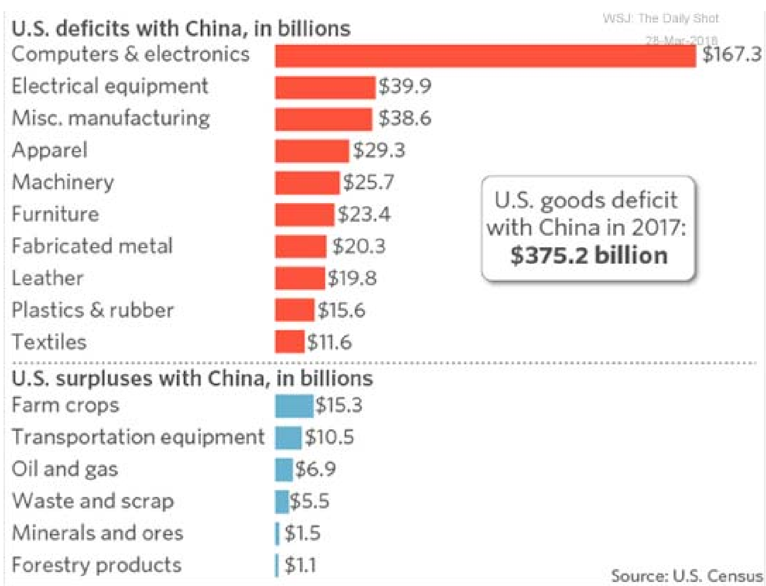
Springing into a mud puddle

How deep is the puddle? President Trump may find out as he steers the US into trade skirmishes with China and other countries. In 1930 the Smoot-Hawley Tariff Act was promised by Congress and President Hoover to protect American jobs and farmers. Over 1,000 economists opposed the legislation. The law raised tariffs on over 20,000 imported goods. Of course Canada and other countries retaliated. A global depression was already underway in 1929 so the Smoot-Hawley Act did not cause the depression but certainly exacerbated it. Unemployment rose from 8% in 1930 to over 20% in 1932. Senators Smoot and Hawley, bless their souls, were voted out of office in 1932.

If one country is good at making computers and another one has plenty of fertile land to grow wheat it makes complete sense that trade will benefit both countries. Obviously there are limits. Tariffs have always existed to protect certain industries that are important for national security or to keep people (voters) in certain industries or regions employed. The challenge is when too many tariffs become molasses for global trade. This causes inefficiencies and unnecessarily steeper prices. Inflation causes the loss of confidence in a country's currency and inflation expectations breed more inflation. If inflation rises faster than expected it is possible that the Fed will raise rates higher and at a faster pace.

In early March the President announced steel and aluminum tariffs aimed at China with exemptions for Europe and other regions. China returned the favor with extra charges on several food products from the US. Then the US announced planned tariffs on Chinese industrial, electronic, transportation and medical products so China counterpunched with duties on cars, airplanes and soybeans. Who will suffer the most? The US lower middle class will get stuck with higher prices and lose jobs. Ironically eliminating NAFTA, the free trade agreement among Canada, Mexico and the US would likely cause a surge in illegal immigration.

Figure 6 – US China Trade By Product Line



Source: The Wall Street Journal, US Census

A valid point is the issue of Chinese intellectual property theft. Counterfeit goods and stolen technologies are estimated to cost the US economy over $225 billion according to the National Bureau of Asian Research. Global supply chains will likely be affected by trade issues. Europe depends on trade more than the US. Emerging markets are integral to supply chains from commodity production to parts manufacturing and assembly. A slowing China will affect many other countries and regions. Hopefully the trade negotiators can take over from the politicians and settle on more moderate actions.

Think spring and autumn

We are holding steady at the helm because we believe there is a reasonable probability that the global economy can forge ahead. Business and consumer confidence are strong. Corporate earnings reports for the first quarter of this year will be announced soon and expectations are for solid profits, more stock buybacks and increased dividends. The technology sector will benefit from increased corporate spending and financials can do well with higher interest rates. International capital flows will continue being attracted to the higher US interest rates despite our budget deficits so there will be buyers of bonds. Inflation is present but muted. Protectionism and other populist policies are a risk but trade wars are unlikely. November elections are around the corner and the winds of change are feeling breezy. Markets and voters do not like uncertainty.

Cash is king and queen. Interest and dividend payments will form a strong base for your long term returns. We will continue monitoring our macroeconomic dashboard for signs of global deceleration. We will also continue searching for quality companies at attractive valuations with solid financial foundations.

Enjoy the warmer weather (when it arrives) and please let us know how we can help you save time and strengthen your family legacy. I welcome your comments.

Thank you.

Best regards,

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Additional sources:

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