HLM
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CAPITAL MANAGEMENT GROUP
of Wells Fargo Advisors

The Hefter Report - December 2017

As mentioned in our November 2016 Hefter Report, we believe the anticipation of infrastructure spending, deregulation, repatriation of funds held overseas and now the likely passage of tax reform has led to the rapid rise of stock prices. During this time, negative news, political stagnation, geopolitical threats and the like have permeated the economic discourse. In our opinion, we have long maintained that as long as fear and negativity prevailed, the market would continue its upward trend.

We believe the S&P 500 has been in an uptrend since 3/2009, but we are constantly watching for signs of a potential market reversal. If corporate profits start declining, if the yield curve inverts, if money supply liquidity begins to shrink, if the US 10 year yield passes 3 percent, and if we start seeing euphoria, we will most likely take action and reduce exposure to stocks. Thus far, we don't see many of these signs. However the yield curve has flattened and market sentiment has turned more bullish. We are starting to become concerned with the increasing optimism and are lightening up modestly on higher beta stocks.

With the 10 year US Treasury bond yielding 2.38% as on 12/5/2017, we believe that stocks are still a very attractive alternative. We would begin to grow more concerned if that yield approached 3 percent. As tax cuts kick in, we believe we could see GDP growth start annualizing between 3 to 4 percent and although that would be excellent for the economy, it could prompt the Fed to raise rates 4 or 5 times next year and push the 10 year treasury yield close to that 3 percent level. That alone would not turn us bearish but if liquidity is drained and the yield curve inverts, we would become much more concerned.

In our opinion, US tax reform could improve the value of US stocks relative to international markets, however, as of now, we still favor overseas investments. The dollar has gained recently vs. the yen but has turned lower against the euro. We think the dollar will trend lower and as US investors this should help in our international investments. Europe is still off all-time highs and is much earlier in earnings expansion and liquidity growth than the US. Japan is also well off all-time highs and is seeing economic growth greater than current US GDP growth.

Adjustable rate preferred stocks and higher yielding tax free bonds remain our favorite fixed income investments. US treasuries and corporates seem vulnerable as economic growth improves and interest rates rise. Cash has been the worst performing asset class and although that may change by the second half of next year, the opportunity cost of cash for the past 8 years has been painful for those who have shied away from preferred and common stocks. We continue to recommend preferred stocks as a possible cash alternative.

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All investing involves some degree of risk, whether it is associated with market volatility, purchasing power or a specific security, including the possible loss of principal. Stocks offer long-term growth potential, but may fluctuate more and provide less current income than other investments.

Past performance is not indicative of future results.

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