BRIAN D. LOWDER, INC.

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FINANCIAL MARKET OVERVIEW

The U.S stock market continued to climb during the second quarter of 2017 and posted a reasonable 3% gain. Unlike the first quarter when all of the 3-month gain was earned in one month (February), stocks posted a modest return in each month during the second quarter.

Even after the swift decline in tech stock prices during the month of June, the technology sector performed better than the overall stock market for two quarters in a row. Over six months, the tech sector posted a 14% return.

Growth stocks outperformed value stocks once again and the differential is quite large – growth stock performance increased over twice as much as value stocks during the first six months of the year. Large companies performed better than mid and small-company stocks once gain.

Gold and silver prices declined less than 1% during the second quarter. For the second quarter in a row, international stocks (world index excluding U.S.) were up significantly during the second quarter posting more than a 6% return or double the return on U.S stocks. Emerging market stocks (small international companies) performed best and posted the largest gain of over 18% during the first six months of 2017.

Energy companies and energy mutual funds were the best performing sector in 2016. However, energy stocks posted negative returns during the second quarter of 2017.

Fixed income or bonds continue to rise and fall modestly in reaction to the gradual increases in interest rates with additional small increases expected for the foreseeable future. Short-term bond returns ended the second quarter with a fractional gain (+0.18%) and intermediate-term bonds posted a modest positive return of 1.43%. The 10-year U.S Treasury Note started the year paying 2.39% interest and finished the second quarter offering 2.3% for new purchases.

Real estate (REIT's) prices were up modestly during the second quarter, with the total return (price change plus income) advancing 1.74% during the second quarter and up 2.55% during the first half of 2017.

The following chart displays sample returns of various asset categories during the second quarter of 2017:

Yr-To-Date 2017	**2nd Qtr. 2017**	**Index Return (*includes dividends reinvested*)**
+ 8.03%	**+ 3.32%**	**Dow Jones Industrial Average (^DJI)**
+ 9.17%	**+ 3.06%**	**Standard & Poor's 500 Index (^GSPC)**
+ 8.90%	**+ 3.06%**	**DJ U.S. Total Stock Market (VTI)**
+13.80%	**+ 4.59%**	**Large-company stock-Growth (IWF)**
+ 4.44%	**+ 1.28%**	**Large-company stock-Value (IWD)**
+11.19%	**+ 4.15%**	**Mid-Size Stocks – Growth (IWP)**
+ 5.02%	**+ 1.33%**	**Mid-Size Stocks – Value (IWS)**
+ 9.85%	**+ 4.40%**	**Small-company stock- Growth (IWO)**
+ 0.35%	**+ 0.64%**	**Small-company stock- Value (IWN)**
+14.75%	**+ 6.35%**	**International (EFA)**
+18.82%	**+ 5.61%**	**Emerging Markets (EEM)**
+ 2.75%	**+ 1.74%**	**Real Estate Investment Trusts (VNQ)**
		Fixed Income
+ 0.39%	**+ 0.18%**	**Short-term U.S. Treasury (SHY)** *(includes appreciation)*
+ 2.47%	**+ 1.43%**	**Intermediate U.S. Treasury (IEF)** *(includes appreciation)*
		Alternative Investment Category
+ 7.68%	**- 0.58%**	**Gold (GLD)**

All returns calculated using adjusted historical quotes from finance.yahoo.com

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FINANCIAL MARKET OUTLOOK

Approximately one-half of investors believe the financial markets will continue to advance and the other one-half are pessimistic and waiting for the bubble to burst. It seems the majority of investors on both sides are primarily influenced by political beliefs and personal feelings rather than focusing on the main variable that provides the best indication of financial market performance over the mid-to-long term: economic growth.

All countries are continuing to experience economic growth rates **below** their long-term average. In the U.S., economic growth has been below our 3% long-term average since 2009. The revised 1st quarter 2017 GDP (gross domestic product) expanded at a 1.4% annualized rate. This GDP growth rate has been adjusted up from the earlier 1.2% estimate.

Measuring the U.S. GDP growth rate by itself does not provide enough information. Considering the growth rates of other countries around the world helps determine whether the U.S. financial markets are overvalued or undervalued compared to other investment opportunities in other financial markets around the world.

China's growth rate has plummeted from near 10% to less than 2%. The GDP growth rate in Japan, Germany, Canada, France, and the United Kingdom are less than 1%. Russia and Indonesia have negative economic growth.

Therefore, if investors only consider our 1.4% GDP growth rate and then review the recent above-average historical performance of U.S stocks over the past few years – especially since the election (up 15%), it's very easy to conclude that U.S. stocks are way too high. The current U.S. economic growth rate is less than one-half our long-term average while our stock market is currently at an all-time high.

But when the same economic data is compared to other countries around the world, the U.S. economy (despite the recent anemic growth) looks much better than nearly all other nations. So, if you are an investor, and you are willing to invest in growth stocks, the relative safety of our financial markets compared to other countries partially explains why the U.S. stock market is much higher than expected.

There are other factors to consider. The recent rate of return on financial assets (stocks, bonds, mutual funds, etc.) exceeds the expected rate of return on starting new businesses, investing in plant and equipment, expanding your current business etc. Starting a new business, expanding a current one, or investing in plant & equipment is expensive and can take years to pay off (if ever). Expenses increase, interest must be paid on new loans, and higher payroll costs must be absorbed. When you compare the longer time period for a payoff and the greater risk of starting or expanding a business verses simply investing in financial assets, it is easy to see why investing in paper assets (stocks, bonds, mutual funds) appears more simple and rewarding. And best of all, an investor can buy or sell paper assets quickly on any business day of the week.

In summary, paper assets or financial assets have been delivering above-average rates of return. Trading or holding U.S. stocks has become more rewarding compared to starting or expanding real businesses and paper assets have much better liquidity compared to committing investment capital to grow businesses that will in turn increase economic growth. It seems investors have become more willing and comfortable holding and trading paper assets rather than creating businesses and expanding economic growth. Additionally, our politicians on both sides are more interested in preventing each other from accomplishing anything rather than representing and serving the people who will be directly impacted by their gamesmanship.

The final piece of the puzzle that may have the biggest impact and will directly determine the near-term direction of our financial markets is *U.S. economic policy and tax reform*.

Our economy and the world economies are stuck in low gear in spite of the fact that interest rates (cost of borrowing by businesses and families for home ownership) are still near a 65-year low. We should be further along economically by now.

Our economic and tax policies need to be adjusted. In large part, the U.S. stock market is already "assuming" some changes will eventually be enacted – particularly lowering the 35% corporate income tax. Stock returns over the past 3 years are much higher than what would be expected during a very slow growing economy. And the 15% stock market rise since the election isn't based on anything else. The financial markets expect some level of economic and tax policy changes. Nearly every other country has a lower corporate tax rate and these countries are the new competitors in attracting and hosting new businesses and the relocation of other businesses. It's simply a fact.

In addition, corporations, like Apple, have billions in profits in overseas corporations and entities. If Apple were to bring those profits home, the company would pay a 35% tax rate. It is our current high corporate tax rate (35%) verses other countries' average of 15% corporate tax that is preventing these profits from returning home.

Further, any family knows they can't keep spending more than they earn. Our federal government has amassed a 20

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trillion dollar deficit. Spending has to match revenues. It is the **expectation** of change toward a better matching of expenditures with revenues and adjusting our economic policies that are keeping stock market at such a high valuation. If no changes or adjustments are made, the U.S. financial markets are at risk of losing at least the 15% gain earned since the November election and likely more.

Other world events can and do impact our financial markets – the most obvious is terrorist acts on a level that requires a military response. A military response causes countries to choose sides. Choosing sides increases the likelihood of multiple and scary skirmishes around the world. When escalated to this point, military might and strategy becomes the focus and it takes priority over economic growth and the general well-being of people. The financial markets and our citizens don't want this unpredictable scenario.

If adjustments and progress are made, then our country can avoid hardship. The financial markets are signaling that this scenario has the favorable odds at this time. That is the expectation.

Investment Outlook and Recommendations

Our outlook has not changed. The probability of a rising stock market ***1-2 years from now*** is higher than the probability of a lower stock market valuation. The transition will be challenging, but ultimately many of the changes outlined by the new President will happen in one form or another.

Again, the big question is: **When** will we know what the new policies (healthcare, income tax code, trade agreements, etc.) will be? Expect some volatility during this calendar year. We have waited patiently for better or fair stock market valuations before increasing our clients' exposure to equities. It never came. Yet, the risk of sudden stock market declines will always be.

During the second quarter, we reduced our clients' money market balances and reinvested those funds into stocks. The probability of better economic growth in the U.S. and worldwide continues to improve slowly. Additional investing of client funds into international, emerging markets and U.S. stocks occurred during the second quarter and we expect to continue with the shift into stocks until we reach the levels clients had in mid-2016.

We have also identified actions we will take if the improving U.S. and worldwide economic growth scenario does not unfold as expected or after a reasonable passage of time. In summary, we expect to continue increasing our clients' allocation into the same growth areas that we had reduced back in August 2015.

We have identified multiple purchase selections for each client and there are many ways to invest during the transition. **We have returned to the policy of including the Blue Recommendation sheets you are accustomed to receiving at quarter-end in this mailing. Note, in many cases the recommended purchases EXCEED the amount of available cash in the account(s). The reason is our purchase recommendations could change in the opposite direction and those (opposite security) selections are included with other buy recommendations we would make under a positive financial market scenario.**

For new clients, the Blue Recommendation sheets are simply our way of sharing our investment ideas, selections and changes with you. It doesn't mean we are waiting for your approval nor does it mean that all of the suggestions will be implemented immediately. If you have questions, comments or want to discuss any of the investments identified on the blue recommendation sheets in greater detail, please call for a discussion or a time and date to meet in person.

IRA Rollover Limits Compared to IRA Transfers

If necessary, investors can withdraw funds from their IRA and then put the money back into another IRA without incurring a tax bill – basically a short-term loan. However, if an investor tries rolling over part or all of their IRA account(s) again within a *12-month period*, the total amount withdrawn will be subject to income taxes and a 10% penalty tax if under age 50 ½ (there are other exceptions like using funds to purchase a home for the first time or medical expenses not covered by health insurance or disability).

Investors can only do ONE 60-day IRA rollover in a 12-month period regardless of how many IRAs you own. Before 2015, the one -per-12-month rule could be applied to each IRA owned – meaning you could rollover multiple IRA accounts in a 12-month period. The big misunderstanding IRA owners have today regarding this new rule limiting one IRA rollover per 12-monh period is not realizing that **all** IRAs are included, even SEP IRAs, Roth IRAs and regular IRAs. One Rollover per 12-month period is the new rule regardless of how many different/separate IRAs you own.

The easy solution (if you are not simply withdrawing the IRA money to use it for 60 days and then put it back into an IRA) if you want to change the current IRA custodian (bank,

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brokerage firm, credit union etc.) to another bank or brokerage firm is to make the switch through a *direct trustee-to-trustee transfer*. This means your current IRA custodian sends the funds directly to your new IRA custodian. Or, this means the IRA owner does not take possession of the funds (meaning does not receive a check made payable to him or herself) but rather the check is made payable to directly to the new custodian (such as another bank or brokerage firm) even if the check is delivered to the IRA owner. You can still take possession of the check and deliver it to a new IRA custodian, but the check <u>must be made payable to the new IRA custodian</u> (for example: Bank of America IRA custodian fbo Jane Smith).

Be aware of the one IRA Rollover per 12-month period rule – as a mistake can be costly.

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Best Regards