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K&S, LLC Financial Fitness Winter Newsletter January 2018 "Up, Up and Away"

We had an excellent global stock market rally led by the technology sector and International stocks in 2017. The stock market's strong start may be an indicator of another good year in the financial markets in 2018. In this newsletter, we discuss the fact that we have not had a 5 to 10% stock market correction in over two years. Historically, the stock market has had a 5 to 10% correction roughly every 6 to 12 months. As each month goes by that we do not have a 5 to 10% correction, the greater the chances are that we may have one. U.S. stocks have been recovering in value for nine years now and their prices reflect this. International and Emerging market stocks which were relatively flat for eight years prior to rallying last year are considered by analysts to be undervalued.

The following are excerpts from three articles that we thought that you may find to be of interest:

1. Economies Overseas Rebound – In the article "Five Economic Trends" in the January 2018 edition of *Money Magazine*, it discussed that the S&P 500 U.S. stock index returned 8.3%, whereas the International MSCI EAFE index and Emerging Market stocks returned less than 2% and less than 1% respectively over the past decade. In 2017 there was a reversal of this trend as both International and Emerging Market stocks outperformed the S&P 500, returning 23% and 30% respectively.

One of the trends that we see is the continued improvement of global economic growth. The U.S. economy is expected to grow 2.5% this year while global GDP is forecast to 3.2%.

Investors who are over weighted in U.S. stocks may want to consider shifting a portion of their holdings into International stocks. Foreign shares based in developed markets such as Europe and Japan look relatively attractive. The price/earnings ratio for foreign shares, based on 10 years of corporate profits, currently stands at a modest 17, which is 33% lower than their historical valuation. By contrast, U.S. shares trade at a P/E ratio of 31, which is 90% higher than their historical median.

Meanwhile, the European Commission predicts the EU grew at its fastest pace in a decade in 2017 and should grow faster yet in 2018.

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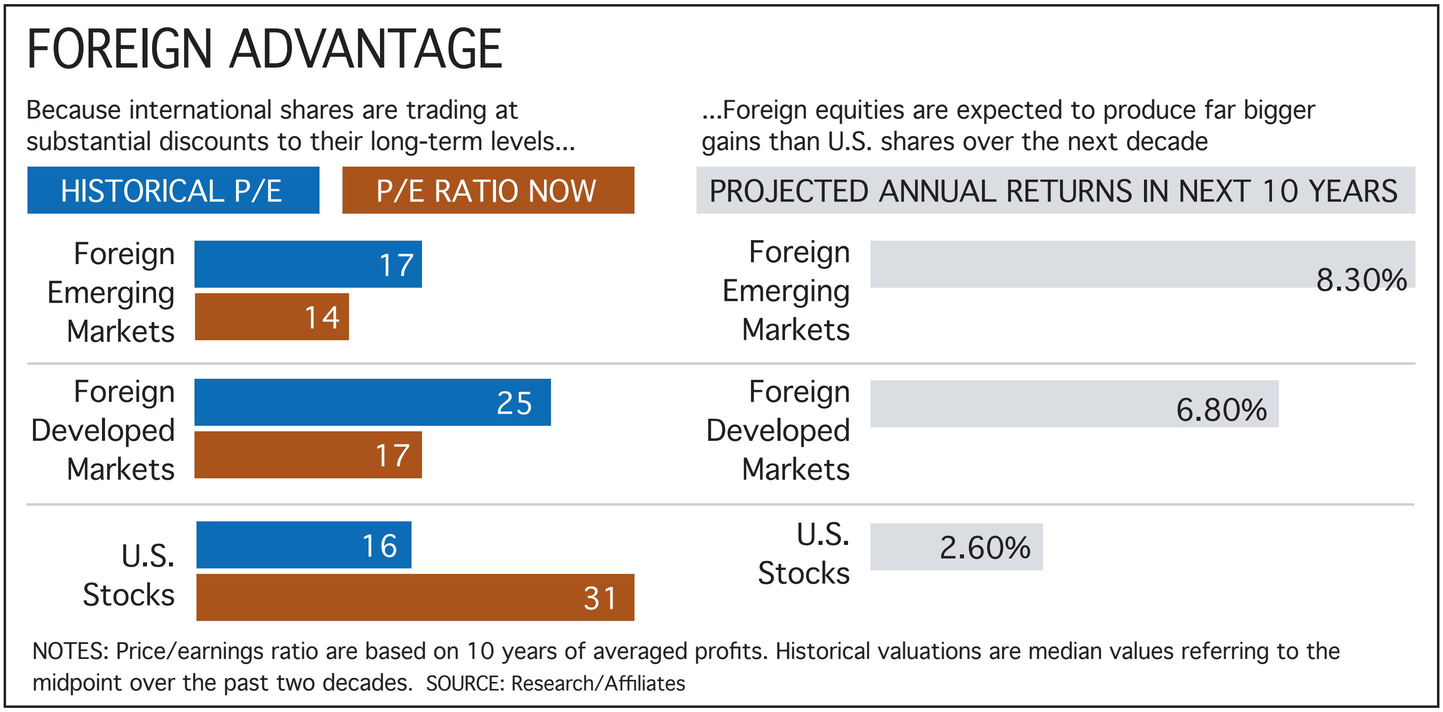

Emerging markets should also continue producing gains – though probably not as big as last year's, especially if the dollar were to gain strength (a strengthening dollar reduces the gains of Americans investing abroad while a weakening dollar amplifies your gains). For long-term investors who can stomach the risk, emerging markets offer the best growth potential.

2. The following is an article written by Ben Eisen in the Wall Street Journal on January 4.

Just because stocks had a banner year in 2017 doesn't mean they have to have a bad year in 2018.

The 19% rise in the S&P 500 last year and the 25% gain in the Dow industrials have fueled expectations for more volatility in 2018. Byron Wien, the Blackstone Group L.P. vice chairman who's been making a widely-watched list of year-ahead predictions for more than three decades, said in his newest list that he believes there will be a correction of at least 10%.

Given how calm 2017 was, it would be practically unheard of for the market to get any calmer in 2018. But that doesn't mean stocks have to end the year lower than where they started. With corporate earnings growing briskly and global economic growth accelerating, many investors see more gains ahead. That includes Mr. Wien, who believes stocks will finish the year higher, despite the correction he expects to hit at some point in the next 12 months.

Continued gains have been the case after strong years for stocks more often than not. When the S&P 500 has risen at least 19% in a year, it's climbed 68% of the time the next year, or 17 out of 25 years, according to The Wall Street Journal's Market Data Group. The average move has been a rise of 8%.

Similarly, when the Dow has finished the year up at least 25%, something it's done 23 times, the following year has offered up an average gain of 9.6%. It's been up 15 of those years

And when the Nasdaq Composite has risen at least 28%, like it did last year, it has averaged a gain of 17% the following year, the Market Data Group found. Indeed, the Nasdaq started off strong on Tuesday, climbing 1.5% to close above 7000 for the first time ever.

That's not to say there won't be more volatility along the way. And history is certainly not a perfect guide to the future. But even after the market strength of 2017 — and perhaps because of it — it looks a bit early to call time on this bull market.

3. The following is a summarization of the *Wall Street Journal* article "Growth-Stock Funds Dominated the 2017 Charts" by Suzanne McGee on January 8, 2018.

Investing in growth stocks was all that a mutual fund manager needed to pursue to reap a healthy return in 2017. The year was one of the few times that we have seen synchronized global growth. While interest rates remain near their historic lows. It was the best period of coordinated, above-trend global growth in almost a decade.

When risk taking is richly rewarded and investors feel confident that little will rock their world, growth takes the lead.

The question, of course, is whether investors should keep betting on growth, or whether it's time to shift toward nearly forgotten "value" stocks, which tend to trade at a lower price relative to their fundamentals. How much of the good news to come – the heart of any growth stock – is already captured in market valuations?

According to data from S&P Dow Jones indices, stocks in the S&P 500 currently trade at about 23.31 times estimated 2017 earnings or 19.67 times forecast 2018 earnings. That compares with an average of 17.13 since 1936. What's more the stocks of a handful of big name growth companies – Apple Inc., Microsoft Corp., Amazon.com Inc., Facebook and Google parent Alphabet Inc. – accounted for about 23.7% of last year's gains in the S&P 500, with Apple alone generating 7.44% of the index's returns. Information technology accounts for around 22.5% of the total capitalization of the S&P 500, yet it accounted for 38.1% of the total return last year.

That's a lot of good news, and many are wondering how much is priced in already.

But lower tax rates are a one-time boost to slower-growth stocks, and that could mean value quickly returns to the back seat.

Certainly, the data suggest that growth has an edge. Some of the same classic growth companies in the technology arena that propelled certain funds to the top of the heap in the past 12 months are expected to contribute most to S&P 500 earnings in the fourth quarter of 2017. Analysts already are predicting that technology companies will post a 28% year-over-year jump and set a record for corporate profits when they report their results for the fourth quarter of 2017.

There is solid research that indicates that when looking out over three, five and ten-year rolling periods, the more likely it is that value-investing strategies outperform growth.

Over the long term, valuation rules everything. If you have a long time horizon, a strategy of simply buying the cheapest stocks has provided the greatest alpha and return. But it's a terrible short-term indicator.

Some pundits are saying it's time for fund investors with a long time horizon to begin allocating some of their assets toward value.

It's not about writing off growth; it's about prudence.

The following is commentary from the Capital Group's December 2017 Investment Insights.

What 2018 Tax Reforms Mean for Investors

Congress' sweeping overhaul of the tax code presents a range of planning opportunities for investors.

For individual taxpayers, the headline provisions include a lowering of the top tax rate to 37% from 39.6%. There could also be secondary benefits to investors resulting from lower corporate taxes.

A deeper look at the new tax law, though, reveals equally important changes beyond tax rates, especially for business owners. Individuals are also potentially affected, especially when it comes to their retirement accounts, philanthropy and education savings accounts.

WHAT'S CHANGING

1. Big breaks for business owners who qualify for pass-through income.

Pass-through income is generated via business income from business structures like partnerships, S corporations and sole proprietorships.

The new tax rates have a large effect on pass-through income, since this form of income is currently taxed to the end taxpayer, not at the corporate level. In 2017, this popular type of business income potentially faced the maximum tax rate of 39.6%.

That changes in 2018. If you're eligible for the pass-through deduction, 20% of taxable income gets taken off the table for tax calculation purposes. That means if you're in the new highest 37% tax rate for 2018, this rule lowers your effective tax rate to 29.6%.

2. Limits rise even more for estate and gift taxes.

Federal estate taxes affect a small subset of high net worth investors now, but that number is likely to dwindle even further. That's because new tax rules double the federal estate tax exclusion to $11 million for individuals and $22 million for couples. Very few estates are this large, making this type of planning even more of a specialty for advisors.

3. Expansion of 529 education savings accounts make them even more useful.

Since their creation in 2001, 529s could only be used for college expenses. But now, for the first time, these accounts can be used for primary and secondary education up to $10,000 a year per student. This is a big expansion of the appeal and utility of 529 plans.

4. The cap on state income tax deductions and doubling of standardized deductions changes the math.

Many of the tax changes are positives for investors, at least in the early years, but not all. Over time, some taxpayers could end up in higher brackets due to a change in the way the annual increases to the brackets are calculated.

The end result? Roughly 30% of taxpayers itemize now. That number will likely be far smaller following the tax changes.

WHAT'S NOT CHANGING

Standard Deduction: The New and the Old

	2017 Standard Deduction	2018 Standard Deduction
Individual	$6,350	$12,000
Married Couples	$12,700	$24,000

1. **Tax rates on dividends and capital gains remain unchanged.**
2. **Tax benefits to retirement accounts, such as 401(k)s and IRAs, stand.**
3. **Tax-lot selling rules stay the same.**
4. **Municipal bonds' appeal is unchanged.**

The reduction of the top tax rate could reduce the appeal of municipal bonds for some taxpayers. But at the same time, munis get more interesting due to the loss of itemized deductions. The bottom line: Munis remain important options for tax-aware investors.

Three Information Sources Which Promote Healthiness and Longevity

I. In the article "Foods for a Strong Heart, Brain, and Bones" John Donovan discusses that eating the right foods can lead to a longer, healthier life. Michele Bellantoni, of the Johns Hopkins University School of Medicine, points out that you need to eat them in the right amounts, too. It looks like the optimal calories for most older adults will is around 1,800 a day. She suggests splitting those calories up into proteins for your muscles, calcium for your bones, and a basic heart-healthy diet.

A basic heart-healthy diet can help you control your weight which is important because more than a third of people 65 and older are obese. Obesity can lead to diabetes, some cancers, and heart disease.

A heart-healthy diet is one that includes:

1. Fruits and vegetables, 2.Whole grains, 3.Low-fat dairy products like yogurt and cheese, 4. Skinless poultry, 5. Lots of fish, 6. Nuts and beans, vegetable oils (olive, corn, peanut, and safflower oils).

Salmon and other fish, like trout and herring, are high in omega-3 fatty acids, which help lower your chances of heart disease and may help with high blood pressure. Aim for two servings a week.

II. Eating To Break 100: Longevity Diet Tips From The Blue Zones

The people who live in the Blue Zones — five regions in Europe, Latin America, Asia and the U.S. researchers have identified as having the highest concentrations of centenarians in the world — move their bodies a lot. They have social circles that reinforce healthy behaviors. They take time to de-stress. They're part of communities, often religious ones. And they're committed to their families. But what they put in their mouths, how much and when is worth a close look, too.

To qualify as a Blue Zone, these communities also have to be largely free of afflictions like heart disease, obesity, cancer and diabetes.

Scientists interviewed hundreds of people who'd made it to age 100 about how they lived to figure out what they had in common.

The researchers' findings on what all the Blue Zones share when it comes to their diet.

- Stop eating when your stomach is 80 percent full to avoid weight gain.
- Eat the smallest meal of the day in the late afternoon or evening.
- Eat mostly plants, especially beans. And eat meat rarely, in small portions of 3 to 4 ounces. Blue Zoners eat portions this size just five times a month, on average.
- Drink alcohol moderately and regularly, i.e. 1-2 glasses a day.

III. Scientific Research Study: A Ketogenic Diet Extends Longevity and Health span in Adult Mice

A Ketogenic diet is one that supplies a large amount of fat and minimal amounts of carbohydrate and protein. Ketosis is a metabolic state which may be the consequence of a diet that is very low in carbohydrates.

Highlights

- A low-carbohydrate, ketogenic diet extends longevity in adult male mice
- Motor function, memory, and muscle mass are preserved in aged ketogenic mice
- Calorie restriction, without malnutrition, has been shown to increase lifespan.

We continue to encourage investors to allocate their assets in a comfortable mix between stocks and bonds, globally diversifying their holdings and focus on the long term. Since we believe the stock market is going to slowly move higher over the next few years, we would view a short term pull back in the stock market as an opportunity to add to your investment positions if you have excess cash.

We hope that you are having a good start to the New Year and look forward to talking to you soon.

Sincerely,

Andrew J. Krosnowski & Melissa Scott Paine

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