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July 19, 2017

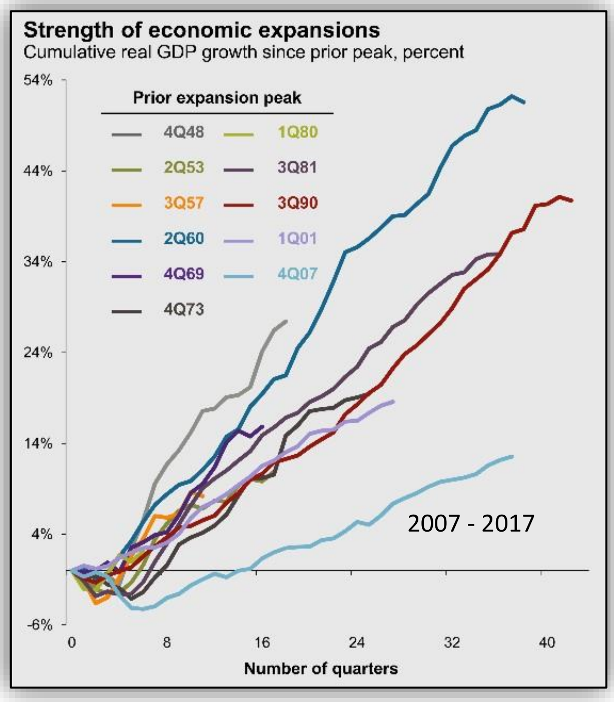
Our Economic & Market Outlook is "Cautiously Optimistic" – Alex Petrovic III, CFP®

Wow, half of 2017 is already behind us and, so far, it has been a good 6 months for the U.S. and global economy. Although there are always risks, at this point in time, we do not see a U.S. recession around the corner over the next 6 – 12 months. Barring some shock, the U.S. economy for now doesn't look at risk of imminent recession, though we continue to believe we are in the later stages of our economic growth cycle. Let's hit the economic highlights shall we!

U.S. Economic Growth: U.S. Federal Reserve officials continue to expect U.S economic (Gross Domestic Product, or GDP) growth of about 2.2% for 2017.

As you can see from the chart, this is the slowest economic expansion in the post-WWII era. This cycle of U.S. growth has averaged a little over 2% a year. Economists say there are multiple reasons for this, but slower labor force growth is one of the key factors. Unfortunately, economists have increasingly come to accept the view that slower U.S. labor force growth will limit our future domestic growth rate. Financial markets may have yet to fully embrace this "new normal." The silver lining though could be that this economic expansion ends up being one of the U.S.'s longest on record.

Regarding Trump's economic plan of reducing corporate and personal taxes and a large infrastructure plan, little progress has been made so far. We believe these will be difficult to achieve at the levels Trump and the financial markets had initially hoped. However, with or without these plans, U.S. economic fundamentals appear to remain sound.



Source: BEA, NBER, J.P. Morgan Asset Management.

U.S. Jobs: According to the U.S. Bureau of Labor Statistics, the unemployment rate was 4.4% in June, below what the U.S. Federal Reserve (or the Fed) considers to be a long-term equilibrium rate. "Wage inflation has been moderate, but officials fear a sharp pickup in inflation if the unemployment rate were to decline further," according to Raymond James Chief Economist Scott Brown. This is one of the key reasons why the Fed is raising interest rates, even though U.S. inflation remains below the Fed's target of 2%.

U.S. Interest Rates: The U.S. Federal Reserve has raised interest rates 4 times since December 2015, and the Federal Funds rate currently sits at 1%. The Fed is targeting 3% by the end of 2019, and the only way it will achieve rates close to 3% is if the economy and jobs outlook remains positive the next couple of years. Most market prognosticators don't believe the Fed will be able to increase rates continuously through 2019 given how soft growth and inflation have been.

The Fed also plans to begin reducing the Fed's enormous $4.3 trillion balance sheet later this year. The effect of both of these moves is to gradually reduce the stimulus that has been applied to the U.S. economy since 2007. Both the interest rate increases and the planned balance sheet reduction may (eventually) have a substantial impact on our economy and financial markets. Investors are anxiously hoping the Fed can successfully navigate 'taking away the punch bowl' from the economic party.

Global Growth: The Economist Intelligence Unit increased its forecast for global growth in 2017 to 2.7%, from 2.6% previously. The driver of the increase was an upward revision to its forecast for the euro zone, to 1.8%, from 1.6% previously, owing to a strong first quarter. The U.S., Europe and the broader global economy are currently all growing concurrently. This may not last for long, but it is most welcome. European and global stocks have performed very well this year as a result.

Chinese Risks: The health of the Chinese economy is probably the biggest risk to the global economy. China represents roughly 15% of global GDP, but it makes up approximately 25% of global GDP growth. In 2016 it grew by 6.7%, but this was achieved at the cost of a further increase in indebtedness. This credit expansion has continued largely unabated since 2008, and as a result, China's total debt-to-GDP ratio has ballooned from 162% in 2007 to 258% currently. The build-up in debt, particularly in the corporate sector, is unsustainable, and we think that once the president, Xi Jinping, has consolidated his power at a party conference in late 2017, he will sanction policies to rein in credit growth. As a result of these necessary policies, The Economist Intelligence Unit forecasts growth will slow sharply in 2018, to 4.6%, from 6.6% in 2017.

This kind of shift is unprecedented in modern China and will come at a time when the global economy is still weak and central banks have very limited scope to react. At a minimum, we think the world's second largest economy will keep slowing; at a maximum, it will suffer a crisis that impacts the globe given increasing trade and financial links.

In Closing: We are cautiously optimistic about the U.S. and global economy. In the U.S., Europe and China, these economies are trying to slowly reduce the stimulus that has been applied uninterrupted for almost 10 years. Thankfully, slow global growth continues, and could continue for years to come, but navigating high debt levels and rising interest rates will most likely be a bit bumpy in the coming years.

Market Recap – Jim Stoutenborough, CFP®

Let's do the numbers:

- The U.S. stock markets continued forward in June with the S&P 500 gaining 0.62%, the Dow Jones Industrial Average up 1.74% and the Russell 2000 providing most of the energy with a 3.46% gain. International markets coasted in with a 0.09% gain and bonds were down a diminutive (-0.1%).
- Year-to-date returns for 2017 through June 30th - Large U.S. companies, the S&P 500 Index and Dow advanced in tandem with 9.34% and 9.35% gains respectively and the Russell 2000 Index (small U.S. companies) despite its good June still lagged its larger brethren with a 4.99% gain. The international index, the MSCI World ex US is still the year-to-date leader up 12.82%. The Barclays U.S. Aggregate Bond Index (quality U.S. corporate and gov't bonds) was up 2.27%.

Asset Class	Index/Category	2017 YTD	2016	2015
Cash & cash alternatives	Average 1-yr CD Rate (annual yield)	0.35%	0.32%	0.27%
U.S. Bonds	Barclays US Aggregate Bond TR Index	2.3%	2.7%	0.6%
U.S. Large Stocks	S&P 500 TR Index	9.3%	12.0%	1.4%
U.S. Small Stocks	Russell 2000 TR Index	5.0%	21.3%	-4.4
International Stocks	MSCI EAFE NR USD TR Index	13.8%	1.0%	-0.8%

Sources: Morningstar.com and Bankrate.com

Inclusion of these indexes and other information herein is for illustrative purposes only and should not be considered indicative of future results. Individual investor's results will vary. Information included herein has been obtained from sources considered to be reliable, but we do not guarantee that such material is accurate or complete. Expressions of opinion are as of this date and are subject to change. Nothing contained herein should be considered an investment recommendation. You should consider any tax or legal manners with the appropriate professional.

Are You Making Money? Here's A Year-to-Date Investment Recap – Sandi Weaver, CPA, CFP®, CFA®

History repeats itself. It is different this time. Ditto for your investment asset classes! We are pleased with the portfolios' performances – your return – this year. Below is a recap of where we have your money invested, what's doing well and what's not.

U.S. large-cap stocks were one of last year's winners and continue to do well. Corporate earnings were robust in the 3rd and 4th quarters of last year, and have continued that trend in the 1st and 2nd quarters of this year. Interest rates remain low, a la the Federal Reserve Bank. President Trump is paring back regulations which hinder business growth, and has plans to take down corporate taxes if he can. Trump's threats of increasing trade barriers have softened, furthering the revenues and earnings of large-cap businesses with sizable operations overseas. For example, General Motors has more employees overseas than here in the U.S. They sell more cars overseas than here. In 1st quarter 2017, Apple took in 65% of their revenues from overseas; they sold only 35% here in the U.S. In 2016 Coke sold 15% of its products in North America, which includes not just the U.S. but Canada and Mexico. That means Coke got 85% of its sales overseas. We have a large portion of your money invested in these kinds of large-cap U.S. companies.

Last year's superstars though were **small-company stocks** which gained over twice as much as the S&P 500's large companies. This year? Small companies are making only half as much as the big firms. Small companies are more volatile, risky. These continue to benefit from good earnings and the low interest rates in the U.S., but they don't get the boost from the healthy overseas business. We have a significant portion of your money invested here, but not nearly as much as in the above large-caps.

Another big chunk of your dollars is invested overseas. Last year's return from these investments was blah, a mere 1%. In fact, it's been 7 years since returns from **overseas stocks** have bested those of our U.S. stocks. But those two continually swap for first place. Prior to those 7 years, we made more money from international stocks in 6 of the 7 years before that. So, overseas matters. Although China's economy is huge, their stock market is only 10% of the global market. (The U.S. is 36%.) China is only a minute portion of your investments. So overseas in Europe matters more. The Eurozone's corporate earnings grew twice as much as ours in 4th quarter last year, and their prospects remain upbeat.

Bonds are a necessity in case of trouble, but returns have been low when compared to earlier bond returns. During a bear market, bonds seldom lose and are often the only investment in your portfolio making money. Last year returns were meager – below 3% across the spectrum. This year investors have made the same – in six months. That return is not expected to double by year's end though. Short and intermediate-term government bonds have returned 2% to 2.5%, but the dip in yields isn't expected to fall further. Municipals have recouped some from last year's slide. Returns on mortgages, mortgage-backed bonds, and TIPS have returned well below 2% this year, while municipal bonds, corporate bonds and high yield bonds are ranging around 3% to 4%. We have a significant portion of your money invested here, usually across several types of bonds.

Even though the Federal Reserve is expected to continue to slowly increase interest rates, depressing bond prices (*i.e.*, you lose money), history shows that doesn't always portend losses in your bonds. Usually bonds face headwinds for a couple years, and then performance begins to bring in those higher yields for investors. In some years, returns were healthy during the period of rising rates. The reports we discuss in your review meetings have this chart of information so you can see the recent periods and what happened to returns.

Are changes in your portfolio ahead? Yes, we're evaluating all bond investments, particularly now that the Federal Reserve's plan to gradually increase interest rates appears to be underway. We're working with research specialists on current and prospective bond funds, to help ensure we have your money well-positioned. We continue to compare your bond funds to others investing similarly, to pinpoint troubled funds which may need to be booted from your portfolio. Our investment committee monitors the stock mutual funds and ETFs where we place your money, to evaluate whether we need to make a change due to poor returns or other reasons. A high majority of the funds and ETFs we use are institutional, with significantly lower expenses than most can access. But our future efforts are focusing on more shifts into passive ETFs and funds when studies show a low probability of beating an index. Those passive or index investments have lower expenses as well.

What You Need to Know About Kansas's 2017 Income Tax Increase – Sandi Weaver, CPA, CFP®, CFA®

The grand experiment, a la the Laffer curve, ended in June for Kansas. The legislature overrode Governor Brownback's veto, and is raising income taxes. Get ready to pay more.

Rates and Brackets: To see how much more you'll pay, take a look at your 2016 tax return. Assuming your financial situation stays mostly the same, then your tax rate moves to 5.7% if your taxable income is over $60,000, assuming you're married. It was 4.6%.

If your taxable income ranges from $30,000 to $60,000, you'll pay at 5.25%, up from 4.6%. If it's below $30,000, you'll pay at 3.1%, up from 2.6%.

These new rates start in 2018. You'll pay 2017 taxes at rates of 5.2%, 4.9%, and 2.9% to phase-in.

For single tax filers, the new tax rates are the same but brackets are cut in half, so the upper bracket (5.7%) starts at income over $30,000. The middle bracket is $15,000 to $30,000. The lower bracket is under $15,000.

Deductions and Credits: The child and dependent care tax credit will return in 2018. Low-income taxpayers will have to pay, starting at $5,000 of income (rather than $12,500) if married; $2,500 if single.

You can deduct some medical expenses starting in 2018, and phase in to a 100% deduction by 2020. You can deduct more mortgage interest in 2019, and phase back in fully by 2020.

Businesses: For business owners using LLC's and S-Corps, your non-wage income will be taxed again starting 2017. Some businesses had crossed the state line to take advantage of the prior exemption.

Play Parent One More Time

Has your child recently gotten their first job? Bought their first house? Gotten married? Had their first child?

Set them up with a phone or office meeting with us. We will review the financial planning steps to take to get started on the right foot.

No charge.

Do you have a Capital Access account at Raymond James? – Jeannine Shaffer, Client Service Associate

If so, you can start paying at the store with your smartphone! You can endorse and deposit checks right into your account from your kitchen!

Your debit card on your Capital Access account is now compatible with Apple Pay, Android Pay, and Samsung Pay. Remote check deposit is also available.

If you have questions you may call the following number for help: 800.759.9797. Or if you have questions or want a demo, please contact Jeannine at the office. If you want us to open a Capital Access account for you, please let us know.

<u>Inside & Outside of PWFS</u>

Alex Petrovic III – The past few months of spring and early summer have been very busy but enjoyable. However, June was a tough month for the family. My father and Peggy's 9th wedding anniversary would have been June 6; he would have been 69 years old on June 14; and celebrating Father's Day was not the same. We still can't believe he is gone.

Dasha and I are enjoying parenthood, and it has been our source for smiles and happiness. Benny is 19 months old and edging closer to the terrible twos. Most of time he is an inquisitive, happy, loving little boy. Then there are the other times… ☺ He's a great sleeper (so far), so that more than makes up for any temper tantrums in my opinion. It's been fun teaching him colors, counting, shapes, and body parts … more than I would care to, though.

A couple of houses away is our home association's park. For 8 years we have lived next to it but rarely utilized it. The pendulum has swung the other way in 2017! It was just renovated, and its playground, tennis court and kiddie pool have been a hit with our family. "Pool time" is already uttered by Benny without prompting, as is 'bubbles'! Indoors we try our best to limit his amount of TV and iPad time. His favorite videos are of cows and Elmo. Not exactly sure why he has an affinity for cows, but Elmo is losing out as the favorite.

Thankfully he loves books. One of his favorites was also one of my favorite 40 years ago. Richard Scary's *Best Word Book Ever*. My mom kept mine all these years and gave me my old book when Benny was born. I had to buy Benny a new version since mine had many pages partially or completely torn and the remaining pages were abused by my early attempts at 'art'. I expect Ben's edition to have the same fate eventually.

The family at Denna Rose Farmstead. The baby goat is nibbling at his shirt!

Over Father's Day weekend, Dasha, Benny and I joined friends of ours and their 2 children who are ages 6 and 8 for a trip to Deanna Rose Children's Farmstead. The weather was perfect, and the baby goats were adorable. All of us had a good time. We'll definitely go back.

Over the next few months, Dasha and I are looking forward to a few small vacations, with and without Benny. In September, my mother's side of the family, including out-of-town family members, are gathering for a family vacation to celebrate my grandma Doris' 90th birthday. It will be great to see and have everyone in town and to celebrate grandma's 90th!

Sandi Weaver – I spent a weekend in the Flint Hills, hearing the KC Symphony and getting lost on country roads since none of us had reliable cell phone service.

We had to resort to reading a paper map – almost a lost art!

Jim Stoutenborough – This Memorial Day I did the "Run for Rachel" 5k in Grain Valley. It is a nice run for a good cause. I ran it in 2013, in its second year and decided that it would be good way to start off this summer. I was happy to see about a 3-fold increase in the number of runners from my first attempt. Since I am a city runner, a more rural run was a nice change of pace. However, it is a challenging run with lots of hills but the last quarter mile is downhill making for a good ending.

For me it was one of my better times but before I started thinking too much of my performance, the 10k runners started crossing the line about 2 minutes after my finish.

Marsy Gordon – As always, it's been a busy spring and early summer. A fun event in my life was going to a dinner theater with my sister and two sisters-in-law recently. We had a great time, laughed a lot, and wondered why we hadn't done that before.

Probably the best part of the last few months at our house was when our kids visited at the same time in June. We managed trips to the lake, a trip to a Children's Farmstead, chasing fireflies, planting flowers (which I have managed, so far, to keep alive), and generally fun times together. One of my goals was to get a picture of all five grandkids (ages 9 months to 6 years old) together. Out of the myriad of pictures that were snapped that week, I think there is *one* that shows everyone's face, and nobody is in a really bad mood. That picture has an extra kid on it, though – oh, well!

Ann Kloster – Update on my flower garden. Butterflies and bees are around which is wonderful. But they came accompanied by a herd of rabbits. Adorable, fluffy tailed, whisker-twitching-hoppity-locust-bunnies. My flowers and plants literally disappeared in a few days. Now, I don't want them dead, I just want them gone. So, the backyard now reeks of fox urine and hot pepper wax, and my neighbors think I'm nuts (get in line), but those adorable munching bunnies are now in their yards.

On a good note, my husband is going to Ireland in a few weeks to "see family on the old sod." I think that is code for drinking Guinness with his brother-in-law in a pub while watching golf. No matter, we will both enjoy his trip.

LaDonna Parker – All the labor I put into my flower beds in the spring is now paying off! I planted Creeping Vincas in one bed and it is now a sea of color. My Begonias are also thriving. However, I had to dig up one of my rose bushes and I think the second one is on its way out. Now the question is – what to plant in that space?

Jeannine Shaffer – My summer started with a wonderful trip to Monterey California with my husband.

We had a few days before his conference began so we had a chance to relax and enjoy the spectacular scenery in Monterey County. We drove down Highway One, which included the fabulous 17-mile drive and stopped at Pebble Beach, had a delicious dinner at Client Eastwood's Mission Ranch, and watched a beautiful sunset on the beach in Carmel.

We visited a few wineries along River Road in the Carmel Valley and tasted some nice wines. It was foggy on Monterey Bay the day we went out to go whale watching but we were still able to sight at least 5 gray whales.

Despite the chilly 60-degree temperatures I was not prepared for, we had a great time. I miss waking up to the sound of breaking waves and barking sea lions!

Sandi Weaver

Alex Petrovic III, CFP®
President

Sandi Weaver, CPA, CFP®, CFA®
Senior Advisor