KACHKOVSKY & FISHER

REGISTERED INVESTMENT ADVISOR

Summer 2018

John Adams, our second president, may seem like a crusty old character as he stares out of school history books, but the man knew how to celebrate. After the Declaration of Independence was approved in 1776, he wrote that the day should be marked by "pomp and parade," with shows, games, sports, bells, bonfires and illuminations, from "one end of this continent to the other, from this time forward forevermore." We have to say, we've made good on that request. Across the country, Americans celebrate July Fourth with backyard barbecues, community events, parades of all kinds, and even simple gatherings around the TV to take in Macy's fireworks display over New York City. However you chose to celebrate – whether boisterously or otherwise – we hope you had a wonderful, memorable holiday.

Let's take a look at the numbers.

| | (As of 6/30/18) |
|---|---|
| Dow Jones Industrials | - 1.81 % |
| S&P 500 Index | + 1.65 % |
| NASDAQ Composite | + 8.79% |
| MSCI EAFE Index | - 2.75 % |
| **Major Bond Indexes** | (As of 6/30/18) |
| Lipper U.S. Government | - 0.74 % |
| Lipper Short-term Investment Grade | + 0.11 % |
| Lipper Corporate A-Rated | - 2.67 % |
| **Major Mutual Funds Indexes** | (As of 6/30/18) |
| Lipper Large-Cap Core | + 1.69 % |
| Lipper Mid-Cap Core Index | + 1.93 % |
| Lipper Small-Cap Core Index | + 5.49 % |
| Lipper International Markets Index | - 3.57 % |

**Source: The Wall Street Journal and Barron's**

*Inclusion of these unmanaged indexes is for illustrative purposes only. Keep in mind that individuals cannot invest directly in any index and index performance does not include transaction costs or other fees, which will affect actual investment performance. Individual investor's results will vary. Past performance does not guarantee future results.

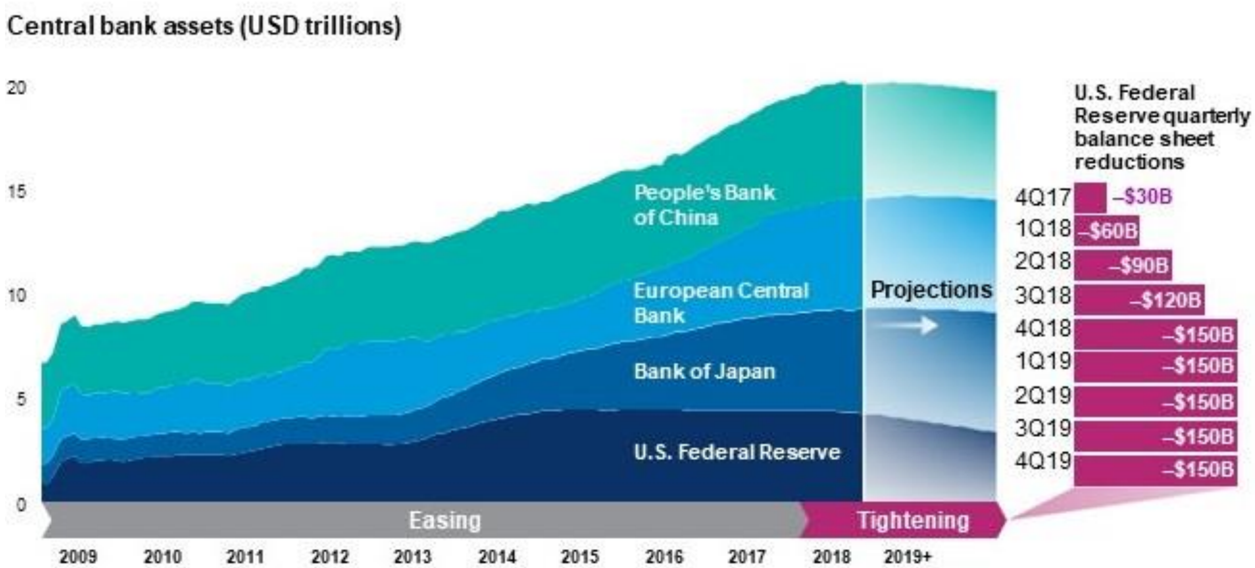
# FINANCIAL AND INVESTMENT PLANNING

**"It really gets grim until the competition begins. You have to wonder at times what you are doing out there. Over the years, I've given myself a thousand reasons to keep running, but it always comes back to where it started. It comes down to self-satisfaction and a sense of achievement."**

**— Steve "Pre" Prefontaine**

This is beginning to sound like a broken record, but sure feels like worth mentioning again – what an interesting last quarter we have had. From sudden rise, fall and rise again in volatility of world equity and fixed income markets to China's advance and the developing trade war, from North Korea's nuclear threat or lack thereof to Russia's election meddling, Novichok poisoning and the World Cup, the barrage of news and revelations are keeping us engaged and on our toes. As if in synchrony, economies throughout the world are undergoing a harmonized expansion. With many indicators mostly on the upturn (i.e. trade, employment, manufacturing, consumer confidence), said expansion is propelling global growth and is supportive of higher equity prices in the near term. With the exception of a few places like Japan, the world economy continues to advance and shows signs of continued pace for at least a bit longer. And, the International Monetary Fund seconds this notions, projecting 3.8% global GPD growth for this year.

Furthermore, the IMF states, "The global recovery now underway is the broadest in seven years, with growth picking up in countries accounting for three-quarters of world output. Global growth is supported by strong momentum, favorable market sentiment, accommodative financial conditions, and the domestic and international repercussions of expansionary fiscal policy in the United States." As we look forward, we must consider the monetary policy shift at home and in the developed world ex-US. The winds of change are here as central banks shift strategy from quantitative easing to quantitative tightening.




Sources: Capital Group, Federal Reserve, Thomson Reuters. People's Bank of China assets are as of 4/30/18. Other data and projections are as of 5/31/18.

Authors of the Midyear Outlook at the Capital Group state, "For nearly a decade, the world's major central banks have given new meaning to the term 'accommodative.' In the wake of the Global Financial Crisis, central banks around the world lowered interest rates to pump liquidity into a global economy on the brink of depression. The U.S. Federal Reserve was the first to take rates to zero, and when that was insufficient to spur growth, the Fed started making massive asset purchases to provide more economic stimulus. The chart shows central banks have reached an inflection point. The Fed began raising rates in 2015, and began selling assets in 2017. The European Central Bank and Bank of

Japan are reining in asset purchases, although neither has begun raising rates or reducing assets on their balance sheets. The assets of those three central banks still total about $15 trillion. The Bank of England hiked rates for the first time in a decade in November 2017. Accommodative policy has provided a significant tailwind to asset prices. Now, policy is tightening. This is uncharted territory for the global economy. How much of a headwind will assets face amid less supportive policy? That question is likely to influence markets for years as central banks begin to unwind the unprecedented monetary stimulus that has played a critical role in shaping the global markets since 2009."

At this point you may be wondering, what does this all mean for me and my portfolio. Will the equity markets break out to record highs, as if Steve "Pre" Prefontaine, perhaps the greatest American middle and long distance runner of all time, wills them to? Or, will the counterforces take over? Perhaps everything feels expensive - real estate, fine art, equities. Energized by nearly a decade of accommodative monetary policy, valuations on equities, fixed income instruments, real estate and nearly everything in between have escalated. Before earnings got a shot in the arm (and, P/E ratios recoiled) from the 2017 Tax Cuts and Jobs Act, U.S. equities were at their most expensive in a decade and a half. On the fixed income end, credit spreads are at their closest levels in years.

Capital Group adds that, "Now, as the Federal Reserve begins to unwind its balance sheet, a variety of asset classes that have benefited from unprecedented easy money may be in for a rougher ride. Investors should also be prepared for bouts of volatility. In fact, at the same time that the Fed is unwinding its $4 trillion balance sheet, it is also increasing interest rates. The Bank of Japan and European Central Bank are likely to follow the Fed's tightening lead. Passage of the Tax Cuts and Jobs Act of 2017 has put more cash in companies' coffers, and they have been ramping up spending on their businesses at the fastest pace in years. Capital expenditures — such as spending on factories, equipment and other capital goods — by S&P 500 companies totaled about $167 billion in the first quarter, the fastest pace in seven years and a record for a year's first quarter. Higher spending on technology, equipment and facilities could ease worries that S&P 500 companies have reached a peak in their profit growth. The spending could also give the U.S. economy a fresh set of legs, and help extend an expansion now in its tenth year. In addition to capital spending, a solid jobs market, rising corporate profits and healthy industrial production point to the U.S. economy continuing to grow through this year and possibly beyond. Naturally, all eyes are on interest rates. The 10-year Treasury note yield topping 3% only increased that focus. Short-term bond funds have tended to be less sensitive to changes in rates, and have become a popular choice for de-risking. But there's a snag: some funds may not behave as expected. That's because credit risk is lurking. For example, in short-term bond strategies - which should emphasize capital preservation and diversification from equities — credit fund-like behavior is surprisingly common. Later in the cycle, credit risk in bonds should also be front-and-center. Although Corporate America is prospering, debt burdens are rising. Moody's estimates that nonfinancial corporate leverage has reached a record high of just over 45% of U.S. GDP. And with short-term rates now higher than they've been for years, there's no need to stretch for yield. Shorter term funds that emphasize high-quality bonds can now offer solid income potential without taking excessive credit risk."

Looking across the pond to Europe, one can't help but wonder how the seemingly frail European Union will deal with the dawn of an extremist populist counterattack against free trade, capitalism, the establishment, a market environment characterized by less reliance on central banks, and escalating geopolitical conflict. Italy 's newly elected revolutionary anti-establishment regime aims to revive accommodative fiscal easing, while the European Central Bank is winding down its asset purchasing program. The enduring refugee crisis fuels geopolitical risk across the region.

As PIMCO forecasts in their latest Secular Outlook, "As the only truly federal institution in the eurozone with significant financial firepower, the ECB has been the glue holding the region together. But investors may not be able to count on the ECB in the same way going forward for several reasons. First, the ECB's asset purchase program is coming to an end, and restarting it may not be entirely straightforward given political opposition to the program in several countries. Second, the shift in ECB leadership in autumn 2019 raises uncertainty. Third, the ECB would likely find it hard to quell market stress by purchasing sovereign bonds if that stress comes from governments' euroskeptic ideologies and fiscally irresponsible actions. Last but not least, fiscal capacity is unevenly distributed across the eurozone, and common fiscal instruments, such as the European Stability Mechanism, are currently too small to accommodate the potential needs of large countries like Italy. All in all, the eurozone faces a challenging outlook over the secular horizon, which appears to be spilling over into the cyclical horizon."

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# PERSONAL

The 2017-2018 school year ended as quickly as it began. Hard to believe that Ava is going into first grade this fall and Elle will be starting kindergarten in two years. Summer is here and that means summer camp, beach days and staying up way past bedtime. The girls have thoroughly taken advantage of beach days - frolicking in the surprisingly warm Pacific Ocean, building sand castles only to stomp on them like Godzillas on the prowl, "rescuing and adopting" sand crabs, boogie boarding the gentle waves of Southern California coast, and, of course, practicing their gymnastics moves. Ava gets inspiration from older girls in her gymnastics camp and Elle mimics anything her sister does. Like in the rest of the country, San Diego has been very warm, which confirms why we are going through so much ice cream and popsicles.

In June, as part of the YMCA Adventure Guides, Garry and Ava plus one hundred or so other dads and their kids headed for Palomar Mountain State Park nestled in the Peninsular Range of northern San Diego County. The area is popular among the locals for its hiking trails, the Palomar Observatory and Hale Telescope. The 200-inch telescope was the world's largest and most important telescope from 1949 until 1992. To get to the observatory that Saturday morning father and daughter charged up the challenging mountain trail leaving many in their dust. The lecture captivated the dads while the kids fidgeted in the seats wondering what snacks hadn't been consumed on the hike. At night, away from the big city light pollution, Garry and Ava were mesmerized by the sea of beams up above.

It's coming. Once it happens, you know it will happen again. Maybe for a few more steps or maybe a few miles. On a Friday afternoon in May, Kris stepped cautiously, hoping not to feel that sudden drop. Not everything goes according to plan. His snowshoe punched through (postholing) and his heart raced. With one leg buried in the snow above his right knee, he placed his next step. Now his left leg was also knee deep in the snow. Knee deep lunges in the snow felt like a mean CrossFit workout in the middle of the hike. The quote, "Get busy living or get busy dying" by Andy Dufresne in 'Shawshank Redemption', kept running through Kris' head, as he was trying to enjoy the beauty and the suffering in the same moment. Living means different things to different people. In this moment, Kris was living! He and six of his friends had embarked upon a seven-mile snowshoe adventure to the Section House in the Colorado backcountry. Built in 1882, the house was for the railroad men and their families who maintained the section of railway that traveled over Boreas Pass. The hut sits at 11,481 feet. Within 100 feet of the cabin, Kris' friend, Tommy actually postholed up to his chest. The seven exhausted friends could not wait to get inside and remove their 50-pound backpacks. As challenging as the hike was, the backdrop of the massive snow-covered mountains set against a sharp blue sky and the comradery among friends made up for it. Due to the remote location, the friends had to melt snow for their drinking water all weekend. The following morning, the guys agreed to hike up one of the nearby 13,000-foot peaks. On the way down, the men agreed to glissade a low angle part of the mountain. Glissading is when you sit on your butt, lean back a little with your feet out in front and legs slightly bent. What a time saver! Weekends come and weekends go. Most weekends will be forgotten. Not this one.

With their pink camelbacks filled with water, a snack and their favorite stuffed animal, Kora and Macy were ready to hike Chief Mountain with mom and dad. Kris' brother Steve and his daughter Ali also joined in on the fun. The girls danced up part of the trail, had discussions on their walkie-talkies and often asked, "Are we almost there?" After making their way through the lodgepole pines, they finally arrived at the rocky summit above tree line. The family scrambled up the remaining boulders, had their favorite snack and took in the views of the continental divide. Angie and Kris are excited to see the girls love for the outdoors continuing to grow.

Kora called the window seat. Macy was happy to let her big sister look out the window on the way to San Diego. The Fisher family was excited to spend time at the Kachkovsky household. Ava and Elle greeted Kora and Macy at the door and the girls were inseparable all week. The parents had plans to take the Colorado girls around town to see the great sights, but soon realized Kora and Macy never wanted to leave the beach. Kids decided the beach was the ideal place to perfect the cartwheel. By week end Windansea Beach was renamed to Cartwheel Cove. Seeing the kids play so well together and hearing their endless laughter warmed their parent's hearts.

Thank you for your trust, confidence and friendship.

**"Genius is 1% Inspiration, and 99% Perspiration."**
**– Thomas A. Edison**

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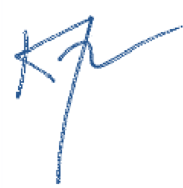
Financial Planner



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