Colorado Capital
MANAGEMENT

SPRING NEWSLETTER / APRIL 2018

# CCM Update

Thanks to the continued growth of our business, we are pleased to announce a new addition to our portfolio management department and the advancement of two of our experienced team members. We would also like to warmly welcome the clients of Randy Kryszak, who merged his practice into our firm during the first quarter. Randy founded Randall L. Kryszak, CPA, PC, a tax and accounting services firm for small businesses, in Boulder, CO, in 1988. In 2000 the company became a Registered Investment Advisor licensed by the State of Colorado. Randy, a Personal Financial Specialist, will provide counsel, in conjunction with CCM staff, to those who were previously clients of his practice.

Zuzana Birova joined CCM in January as Assistant Portfolio Manager. She has a decade of experience in equity and fixed-income trading, portfolio reconciliation, client reporting, and asset class research. Originally from Slovakia, where she earned her undergraduate degree in International Business, Zuzana went on to pursue her passion in investment management by completing her MBA at Butler University in Indianapolis. After graduating she joined Deerfield Financial Advisors, Inc., where she managed investment operations and played a key role in implementing new technology for advisors. She is currently in the process of acquiring the Chartered Financial Analyst (CFA) designation.

We are also happy to announce the promotion of Kirsten Roeber from Assistant Portfolio Manager to Portfolio Manager. Kirsten has been with CCM for eight years, serving as a member of the portfolio management team and assisting in research, trading, portfolio construction, and investment strategy since 2014. She holds a bachelor's degree from the University of Colorado, the Accredited Asset Management Specialist designation, and is a Certified Financial Planner (CFP®) candidate.

Colleen Harvey, who joined our firm in 2014 as Portfolio Manager and chair of our investment committee, has also taken on new responsibilities. As of January, Colleen became a full-time financial advisor. With almost twenty years of experience in the wealth management industry, Colleen is well prepared for her new role. Colleen has a bachelor's degree from the University of Notre Dame, a master's degree from Tufts University, and holds the Chartered Financial Analyst (CFA) designation. We are delighted to share all of this good news, and hope you will join us in congratulating and welcoming Zuzana, Kirsten, and Colleen into their new roles.

*CCM staff ski day at Copper Mountain. Ladies who shred, left to right: Zuzana Birova, Liz Jacques, Julia Wentworth.*

# April Economic Update

**Growth.** During the final three quarters of 2017, the US economy grew at a relatively strong annualized rate (about 3%), but that growth appears to have slowed in the first quarter of 2018. Consumer spending eased, the volatility of financial markets increased, and real GDP growth likely slowed to roughly 2%—the same lackluster pace that has been the hallmark of the current long but unspectacular economic expansion. Despite the recent slowdown, the fundamentals of the economy clearly appear to support the case for continued economic expansion.

**Wage Inflation.** The tight labor market has finally started to drive faster wage growth, with wage inflation rising above 2%. This pace now equals or exceeds the pace of

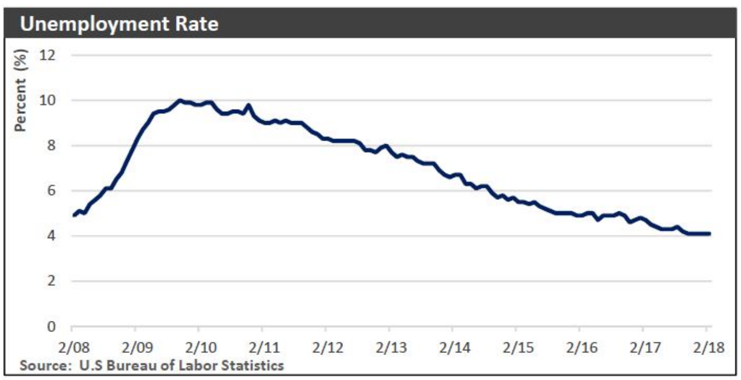
*Colorado Capital Management contributors and editors: Steven Ellis, Lee Strongwater, Colleen Harvey and Julia Wentworth.*

overall inflation, which has also been trending upwards. With workers becoming scarce and more expensive, businesses have ramped up capital investment.

**US GDP Forecast.** Higher wages, increased business spending, and the stimulative effects of the recent tax cuts are all expected to contribute to stronger economic growth. On the other side of the ledger, political uncertainties such as the increased risk of a trade war, could create a drag on economic growth.

**Housing Market.** Mortgage interest rates in the US are also rising and are now at their highest levels since 2014. Higher rates, together with increasing home prices, are pushing home ownership out of the reach of many would-be buyers, which has led to a sharp drop in home sale activity in recent months. These developments present a growing challenge to the housing market, which has been central to the economic recovery but can be very vulnerable to even modest headwinds.

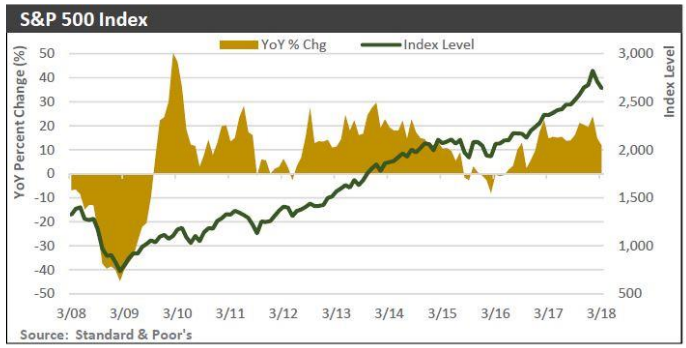
**Employment.** The unemployment rate reached and remained at a 17-year low in October. For every job opening in America, there has been barely more than one unemployed person available to take it.




**Global Growth.** A positive for the U.S. economic outlook is the widespread strength of economic growth around the world. While geopolitical risks are always present, global economic conditions appear very favorable. Global GDP grew 3.2% in 2016, 3.6% in 2017, and is projected to climb 3.5% this year. Last year's annual 2.5% growth in the Eurozone was the region's strongest pace in 10 years. While China's economy grew 6.8% last year, it is expected to gradually slow due to an aging population, increased debt levels, and a multi-year drop in investment.

**Fed Funds Rate.** The Federal Reserve is now faced with a tricky balancing act in weighing how quickly to raise interest rates given the uncertainty about how the economy will respond to tax cuts and likely spending increases. With inflation ticking up, in part due to rising wages and tariffs, expectations are that the Fed will raise interest rates three times or more in both 2018 and 2019. The Fed funds rate was increased by 0.25% in March to a 1.75% target.

**S&P 500.** The S&P 500 Index finally saw a return of market volatility back towards more "normal" levels and the Index witnessed a decline of 0.76% to kick off the first quarter of 2018. This decline marked the end of a long string of positive monthly returns for the index. Despite investor and business confidence remaining high, markets faced pressure around concerns of rising inflation, interest rates and trade tensions.




**Small-Cap.** Mid and small-cap stocks faced similar concerns, but did slightly better than their larger brethren to start off the year. The Russell Mid-Cap Index declined 0.46% in the first quarter, while the Russell 2000 Index representing small stocks was almost flat, declining only 0.08%. As a result, investors with allocations to these diversifying asset classes saw a potential marginal benefit from these exposures.

**Growth vs. Value.** Regardless of company size, growth stocks generally outperformed value stocks. Investors continued to pay up for those companies that could deliver higher levels of earnings growth, although some cracks started to show and selectivity became more pronounced. Many individual names in the S&P 500 Index, for example, faced more pressure than the Index itself which was supported by just a few larger weighted holdings.

**U.S. Corporate Earnings & P/E ratios.** Due to a dramatically improving earnings forecast, as well as modest market declines, many market indexes now trade at price-to-earnings levels that are the same or lower than where they were one year ago. Nonetheless, current values remain above longer-term average levels. According to the Wall Street Journal the S&P 500 Index now trades at less than 17 times forward earnings estimates.

**Foreign Stocks:** Developed equity markets outside the U.S. also struggled to start off 2018, after outpacing domestic stocks in 2017. The MSCI EAFE returned -1.53% for the quarter. Many developed foreign markets declined by larger amounts in local currencies, however U.S. dollar weakness benefited returns to American investors. Emerging Markets stocks grew 1.4% and were one of the few areas showing positive returns for the quarter (also benefiting from a weak U.S. dollar). Performance was supported from investor flows into the asset class following outsized returns in 2017.

**Bonds:** The Bloomberg Barclays U.S. Aggregate Bond Index declined 1.46% in the first quarter as interest rates moved higher. The U.S. 10-Year Treasury closed the quarter with a 2.74% yield, up sharply from the 2.40% level where it ended 2017. In late February and early March the yield had settled in near 2.9% and looked like it might make a run to cross over 3%. But late quarter weakness in stock markets led the rate to decline somewhat as investors sought the safety of Treasury securities. Similar 10-year government notes in Europe and Japan offered much more modest interest rates that were relatively unchanged during the quarter, but also benefited from a falling dollar. For the quarter the Bloomberg Barclays High Yield Corporate Index was down 0.86%.


**Real Estate & Commodities.** Commodity-related investment returns did not move materially higher on average, although oil prices rose. WTI ended the quarter near $65, up from $60 per barrel at the end of 2017. Meanwhile U.S. natural gas started the year near $3 and reached a peak of $3.66 toward the end of January, only to decline sharply in subsequent weeks and close the quarter near $2.66. Lower natural gas prices and changes to FERC rate policies disrupted interest in MLP investments and the Alerian MLP Index declined 11% for the quarter.

Real estate investments also saw periods of volatility over the quarter as investors wrestled with moves in interest rates and the perception that rates would continue to move higher over time. Rising interest rate environments are generally viewed negatively by real estate investors that fear negative impacts to property values. However, often times these fears prove short-lived, particularly in markets with positive fundamentals and rental rates adjusting higher. Real estate investment returns in the first quarter of 2018 saw a fair amount of variance depending on the particular focus of the strategy or index. In the first quarter of 2018 the FTSE NAREIT Equity REIT Index returned 1.16%.

## Outlook

The recent changes to corporate tax policies have added to expected corporate earnings growth in the coming year as analysts increased their 2018 forecast for the S&P 500 Index by $11 since last quarter (earnings are now expected to come in near $156 for 2018, from about $145 as the year began). Stock prices also declined modestly. As a result, market valuations have improved. There is no question that valuation levels remain stretched above longer-term averages, and this in and of itself provides reasoning to err on the side of caution from getting excessively bullish. On the other hand, inflation and interest rate levels remain low by historical standards, dramatic earnings growth is expected this year, and anticipated strength and recovery in global economies remain supportive of equity markets.

As interest rates move higher, fixed income investments could face sizable headwinds, although there certainly will be periods of stability. Based on recent economic and market trends and forgoing a significant change to current inflation trends, the Federal Reserve has forecasted 3 interest rate hikes in 2018, one of which occurred at the March meeting. Market expectations seem to be aligned with this Fed forecast at the moment with additional 25 basis point hikes at the June and September meetings. However, should the current economic and inflationary trends strengthen, there is increased likelihood of a fourth 25 basis point hike at the December meeting as well.

As strategic investors, we prefer to focus on maintaining a disciplined long-term positive perspective on capital markets. While short-term disruptions from economic and geopolitical events are inevitable, no attempts are made to make substantial portfolio adjustments as markets ebb and flow. Our approach is to make meaningful and purposeful portfolio allocations, with regular rebalancing, and few significant changes other than those mandated by the evolving needs and circumstances of our clients.

*Sources: Morningstar, Wall Street Journal, Capital Market Consultants and other paid subscription services.*

# Parenting Your Wealth

In the face of political drama at home and abroad, it's certainly been a winter for trying our patience, hasn't it? For anyone who has ever been a parent or a child – that is, for everyone – there are several comparisons we can draw between good parenting and good wealth management. For both, plenty of patience is one of the most important qualities to embrace.

### *Patience is Your Greatest Strength*

As an investor, you probably have plenty of "those days" when you wonder whether your money is ever going to grow up. It doesn't do as you hoped for. It misbehaves. It runs with the wrong crowd. It ignores your best efforts to protect it from harm. But then there are those other days. Suddenly, your money hits a growth spurt, exceeding all expectations! It's then that you realize that many of the greatest challenges you and your investments faced along the way are the same ones that are contributing to its strength and shaping its character over time.

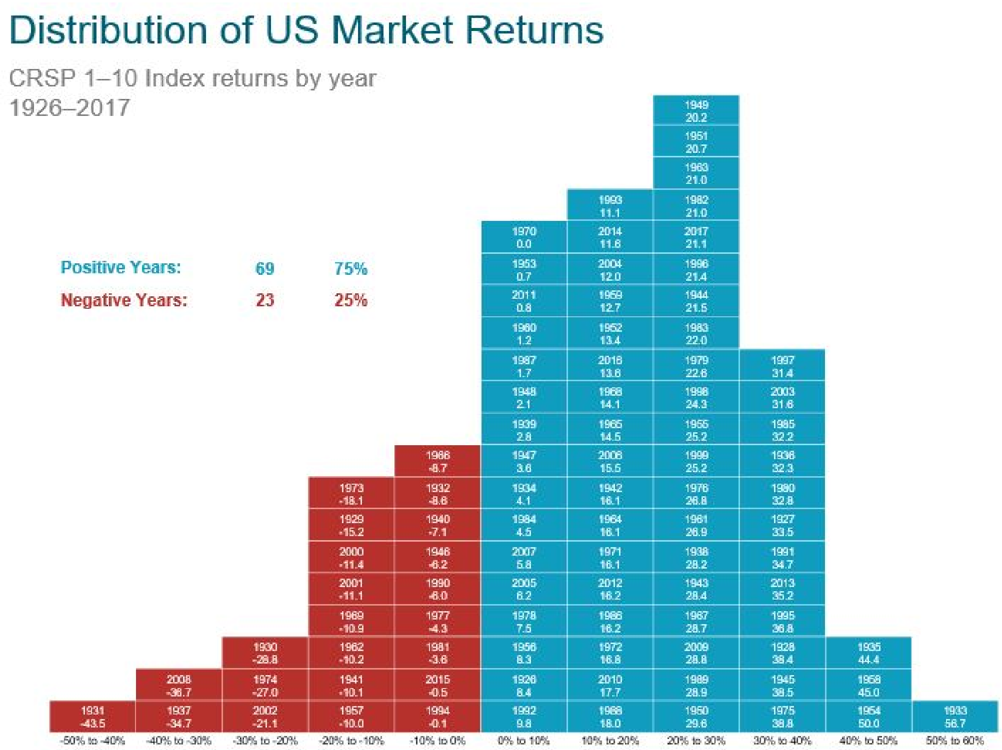
### *In the Markets, "Unusual" Is Business as Usual*

As much as we would prefer our wealth to mature in a calm, orderly way, there is solid evidence to demonstrate that returns are far more likely to occur in these sorts of anxiety-generating fits and starts. For example, you may recall that January 2016 was an unsettling time in the market, with particularly petulant returns. Some pundits blamed China and oil. There was no incredibly obvious reason; it was just in one of those moods. On the flip side, in the wake of the June 23, 2016 Brexit referendum, when we might have expected the market to remain in a funk for a while, it took a dive but then mostly continued upward, especially in the U.S., where stock market indexes experienced a number of record highs in July.

The Center for Research in Security Prices (CRSP) index returns by year show that from 1927 - 2017, the market experienced 68 years of positive returns (75%) and 23 years of negative returns (25%). Therefore, although the occurrence and degree of corrections and bear markets might make an investor uncomfortable, long term returns continue to demonstrate that patience and discipline are the best responses to market turmoil.

Most investors are wise to offset the heated risks involved in pursuing higher expected returns with an appropriate helping of "cooler" holdings. We also suggest employing global diversification to manage the market risks that you do take on. Spreading your risks among multiple kinds of holdings around the world can be compared to raising several children, without choosing a favorite. Each is expected to contribute in its own special way.

With investing you should avoid the temptation to jump in and out of uncertain markets. We know they are going to often misbehave and sometimes disappoint. We even know that they may never deliver as hoped for. But once you have done everything you can to position your portfolio for the outcome you have in mind, you've also done everything you can to stack the odds of success in your favor. The rest is where that patience comes in.







Colorado Capital MANAGEMENT
Enriching Lives

4430 Arapahoe Ave.
Suite 120
Boulder, CO 80303

Phone: 303.444.9300
Fax: 303.444.2027
info@coloradocap.com
www.coloradocap.com