SEM
WEALTH MANAGEMENT ™

Economic Update & Preparing for the Election – Part II

Using Scientifically Engineered Models

A smooth road to lifelong investing.

Data through September 2024

"Thanks for the 60-minute Kamala Haris commercial."
-webinar attendee, 10/2/2024

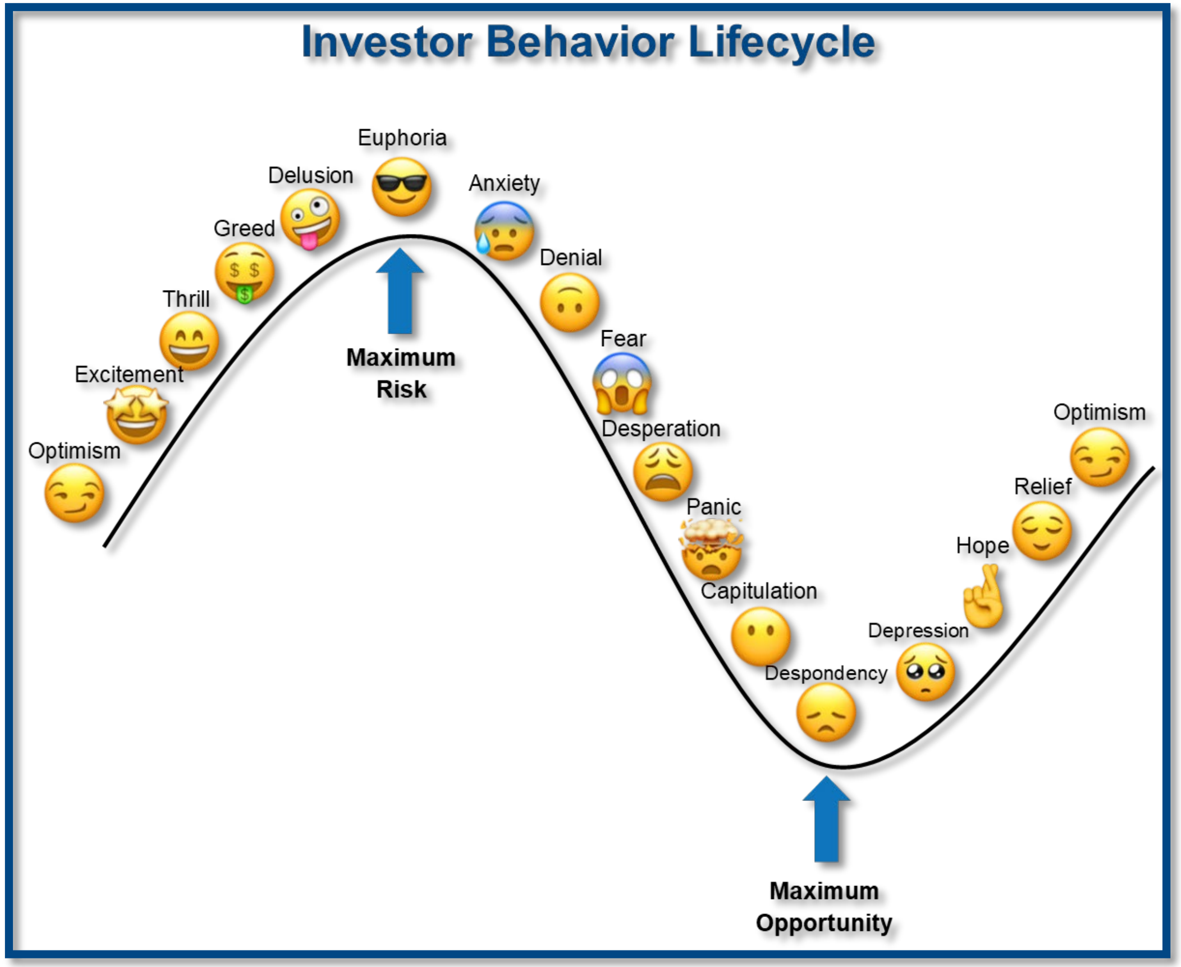
"Jeff may as well have been wearing a MAGA hat."
-webinar attendee, 10/2/2024

"Why is this the only place I'm seeing this data?"
-webinar attendee, 10/2/2024

"This was the definition of fake news."
-webinar attendee, 10/2/2024

"I couldn't tell which candidate Jeff endorsed."
-webinar attendee, 10/2/2024

Understanding Human Behavior


Investor Behavior Lifecycle
Optimism
Excitement
Thrill
Greed
Delusion
Euphoria
Maximum Risk
Anxiety
Denial
Fear
Desperation
Panic
Capitulation
Despondency
Maximum Opportunity
Depression
Hope
Relief
Optimism

The stock market is a story of **cycles** & of the **human behavior** that is responsible for **overreactions** in both directions.

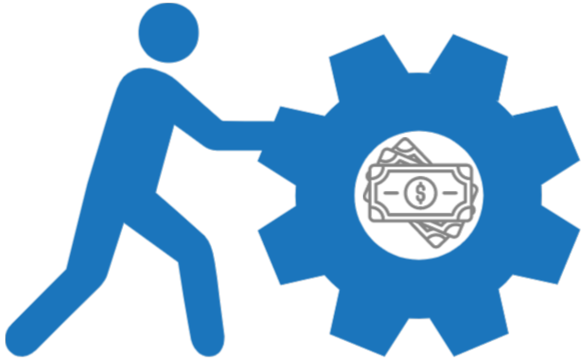
– Seth Klarman

For current market updates go to: tradersblog.semwealth.com

Potential GDP Equation

How many people are working?

+

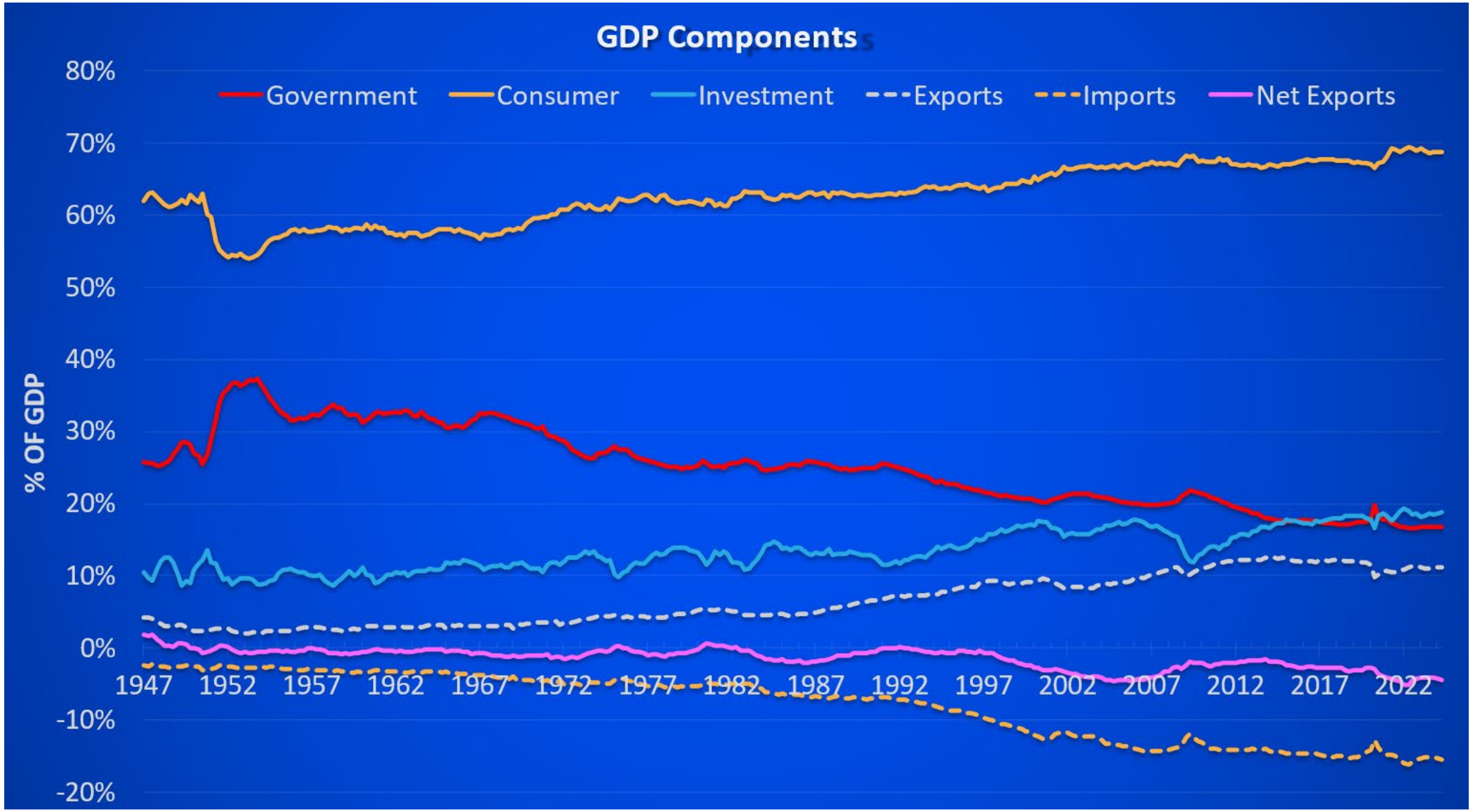


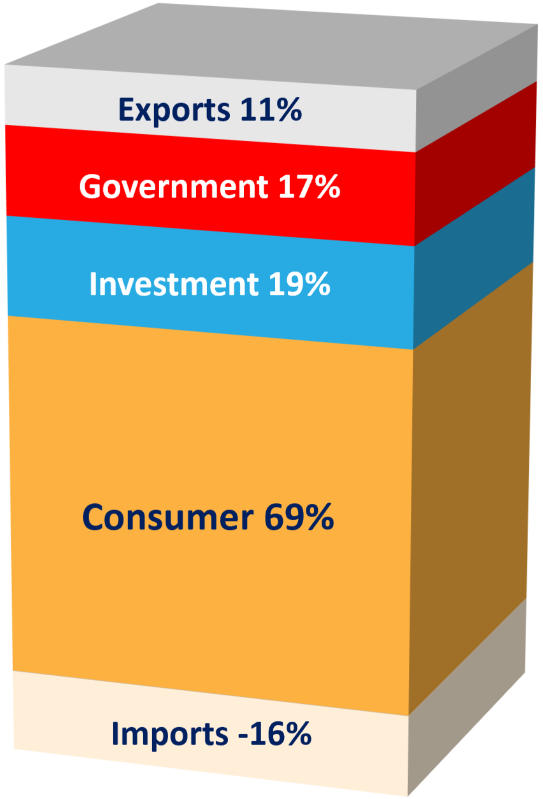
How much are they producing?

GDP Equation

Consumer + Investment + Government + Net Exports

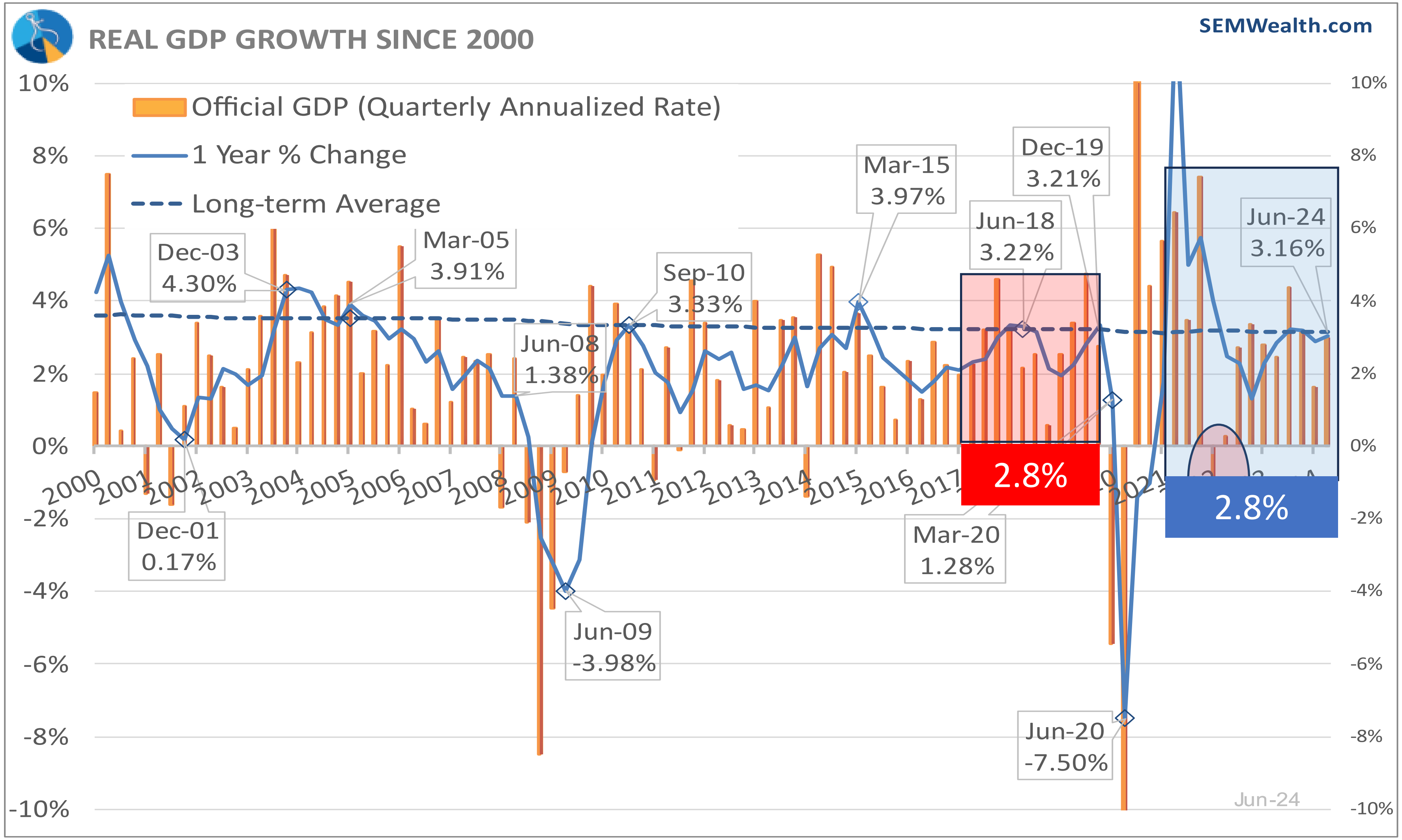
GDP Components





Understanding GDP Reports

- Official GDP numbers can be misleading
- "Seasonally adjusted annual rate" causes large swings
- Focus should be on 1-year rates of change
- We have had few periods this century above the long-term average



Leading Economic Indicators

Jobs / Workers

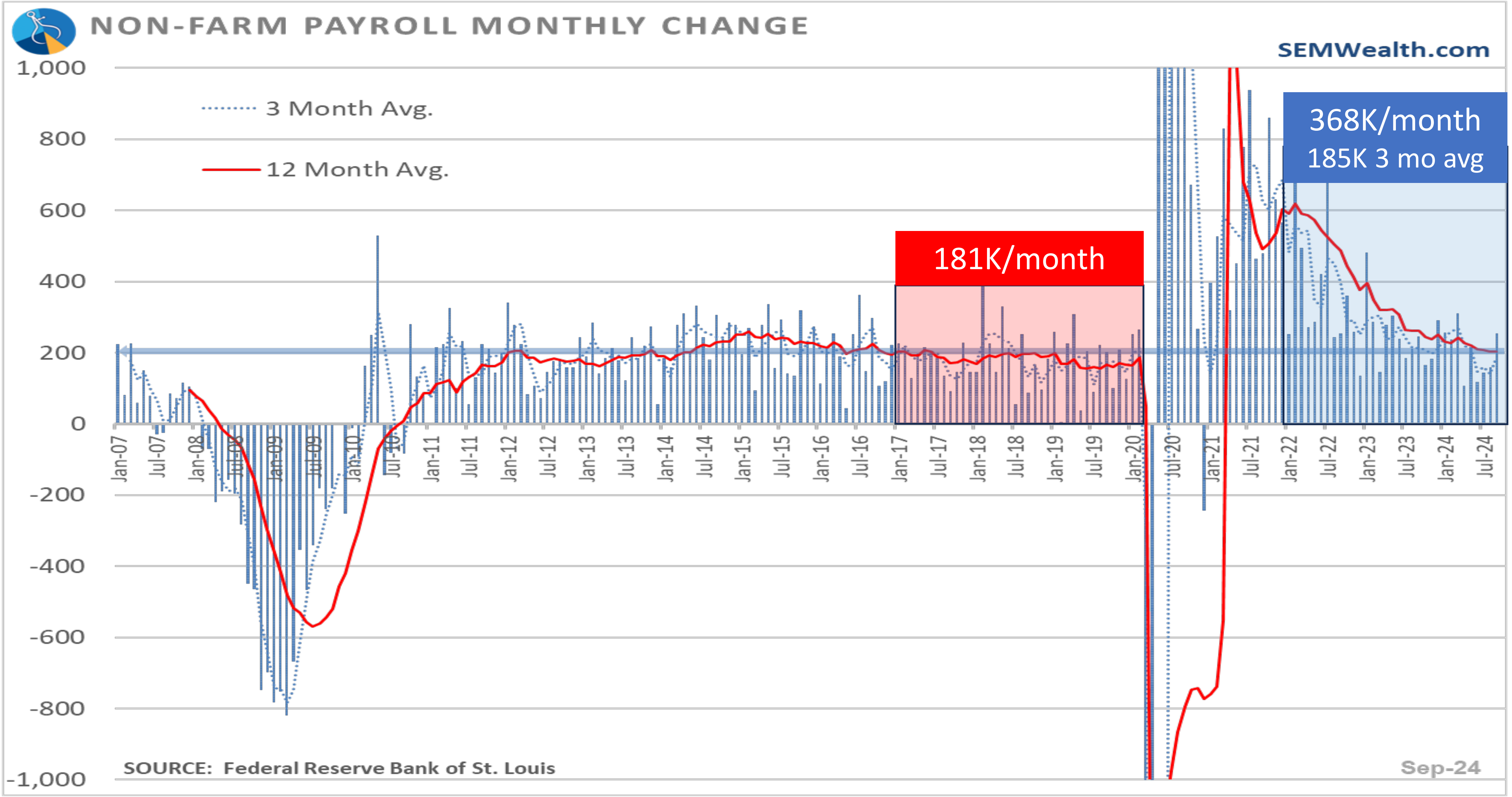
CREDIT CARD
4654 2146 7564 8514
06/21

Consumer Spending / Confidence

Investment / Housing / Manufacturing

Government Activity

Employment Indicators



SOURCE: Federal Reserve Bank of St. Louis

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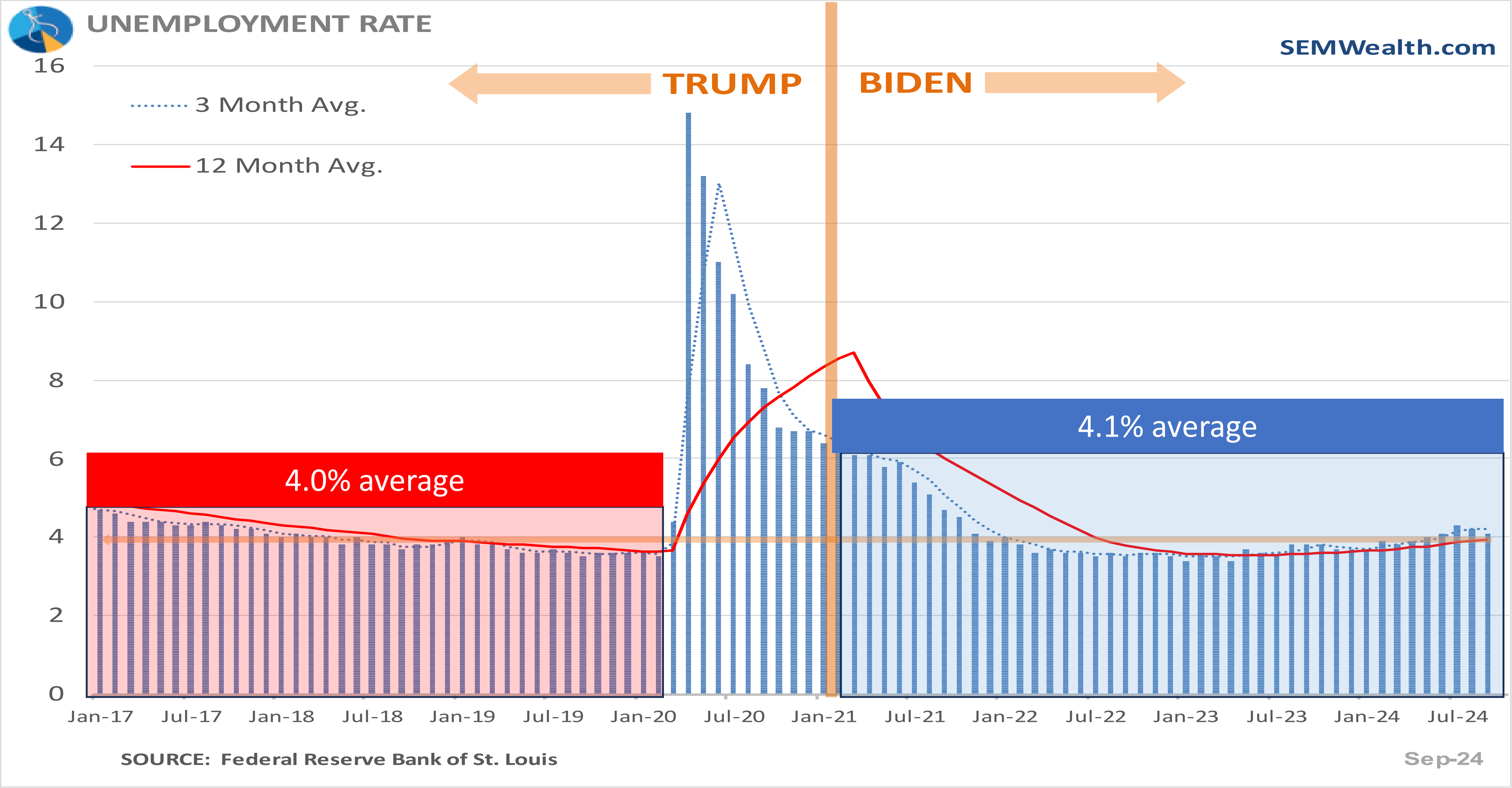
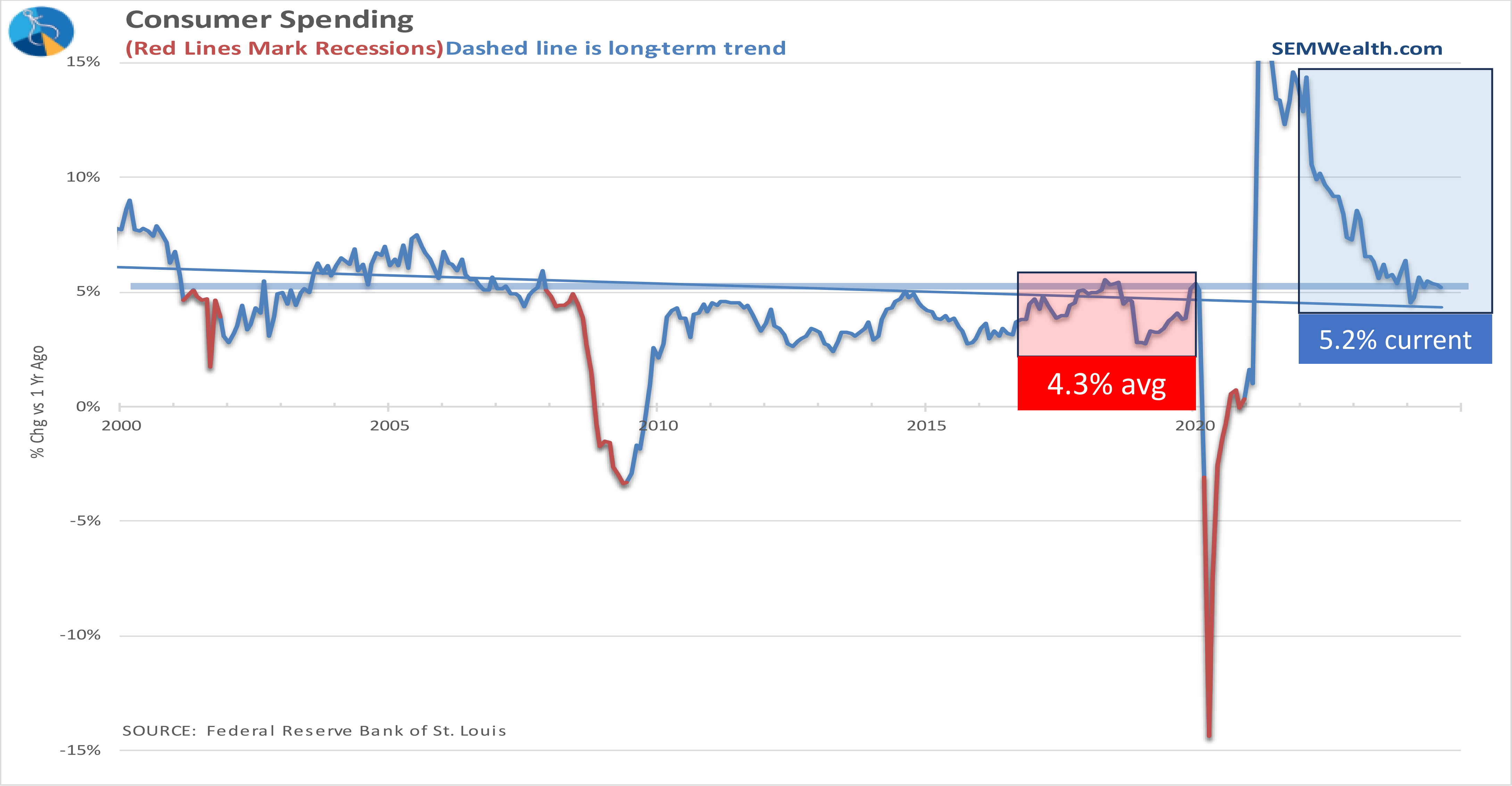
Employment Indicators



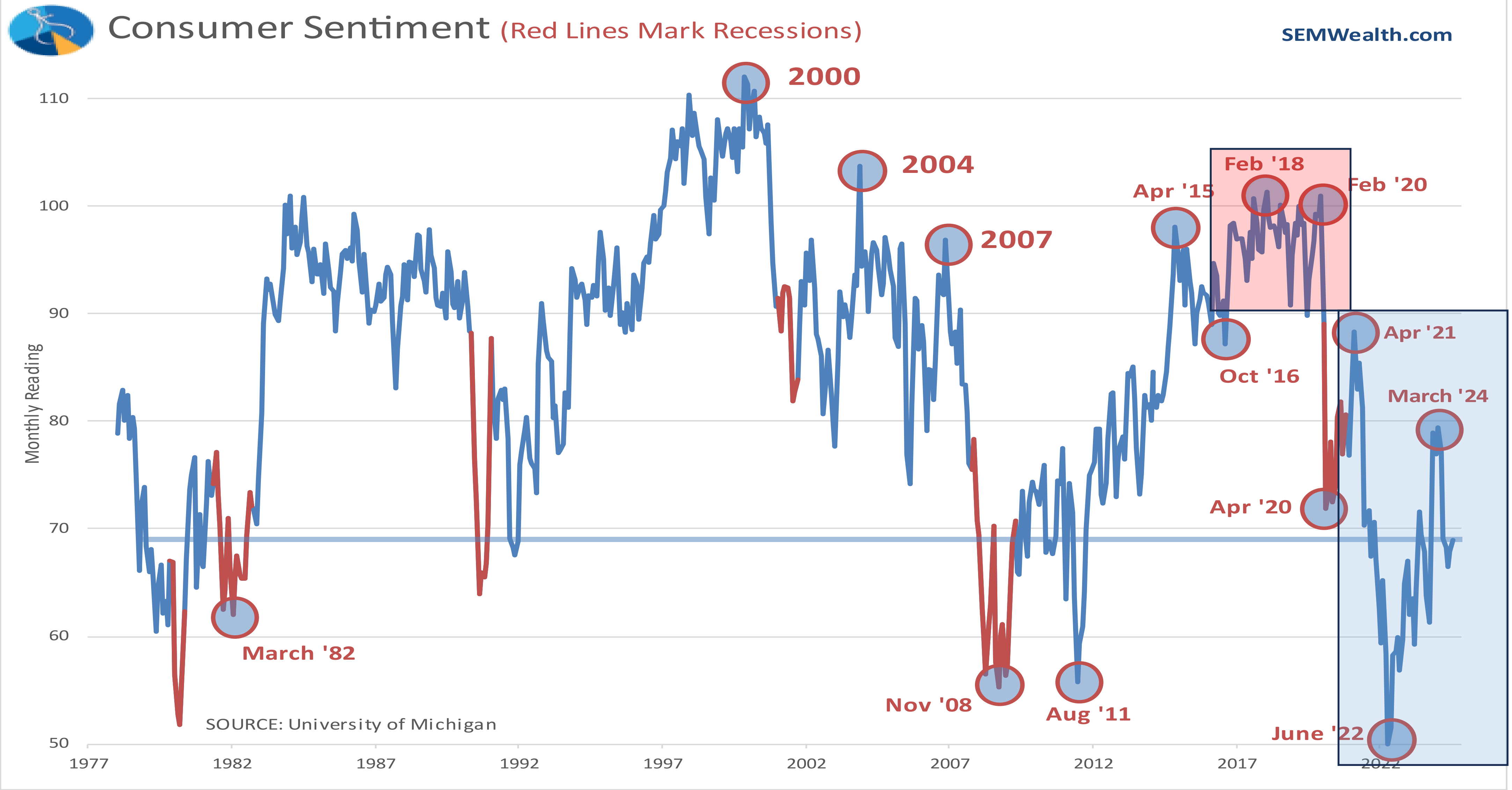
SOURCE: Federal Reserve Bank of St. Louis

Consumer Indicators



SOURCE: Federal Reserve Bank of St. Louis

Consumer Indicators



SOURCE: University of Michigan

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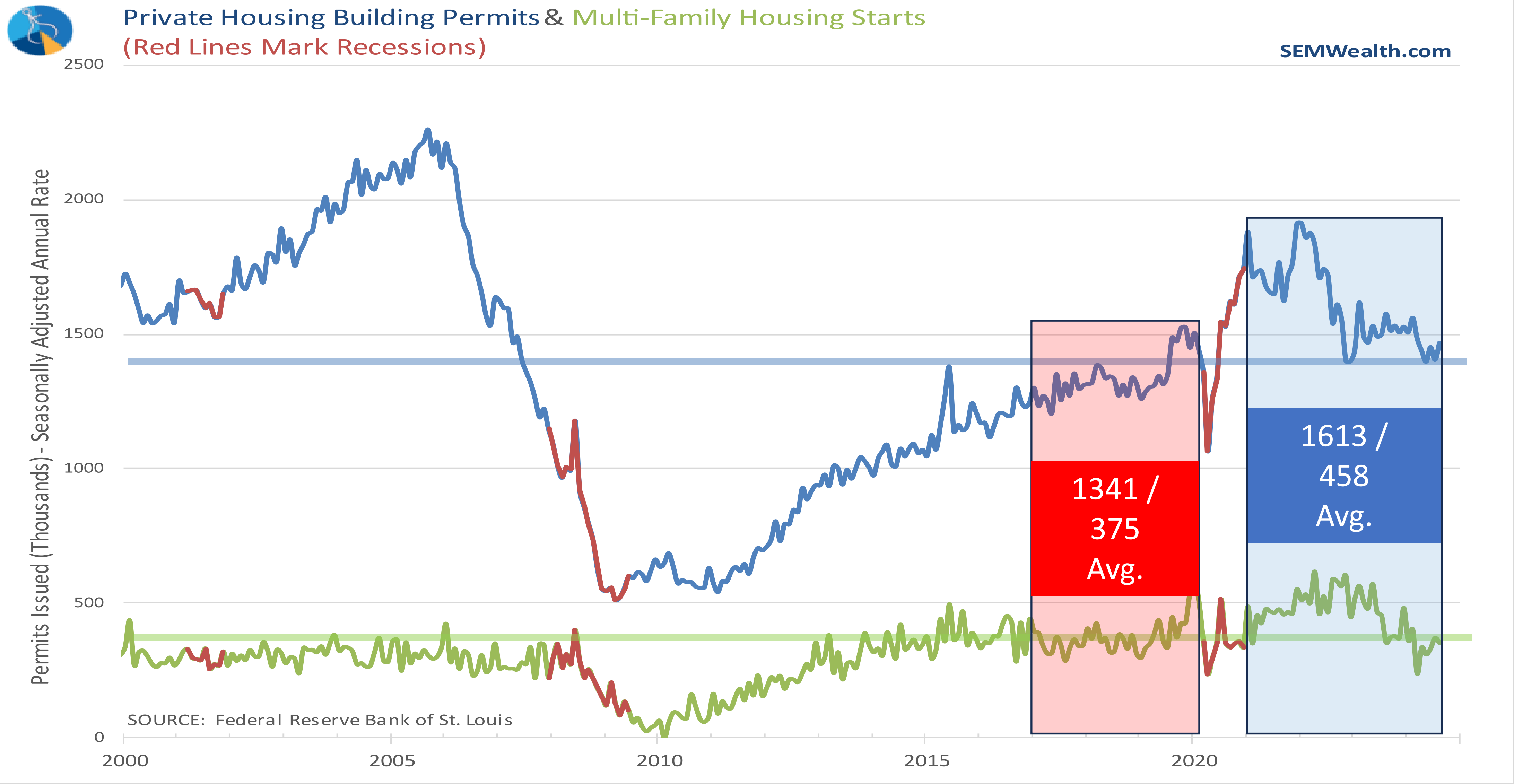
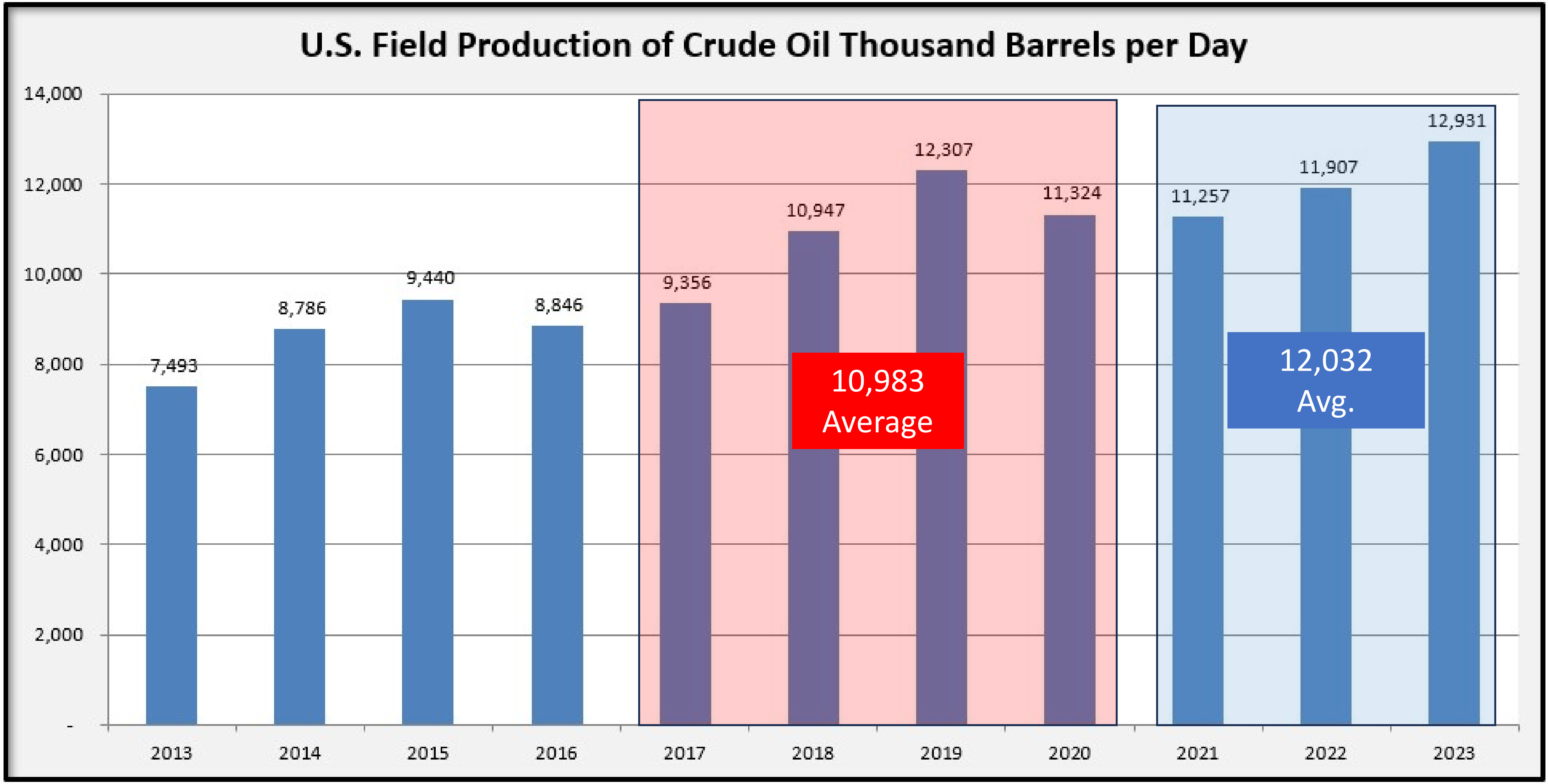
Investment Indicators

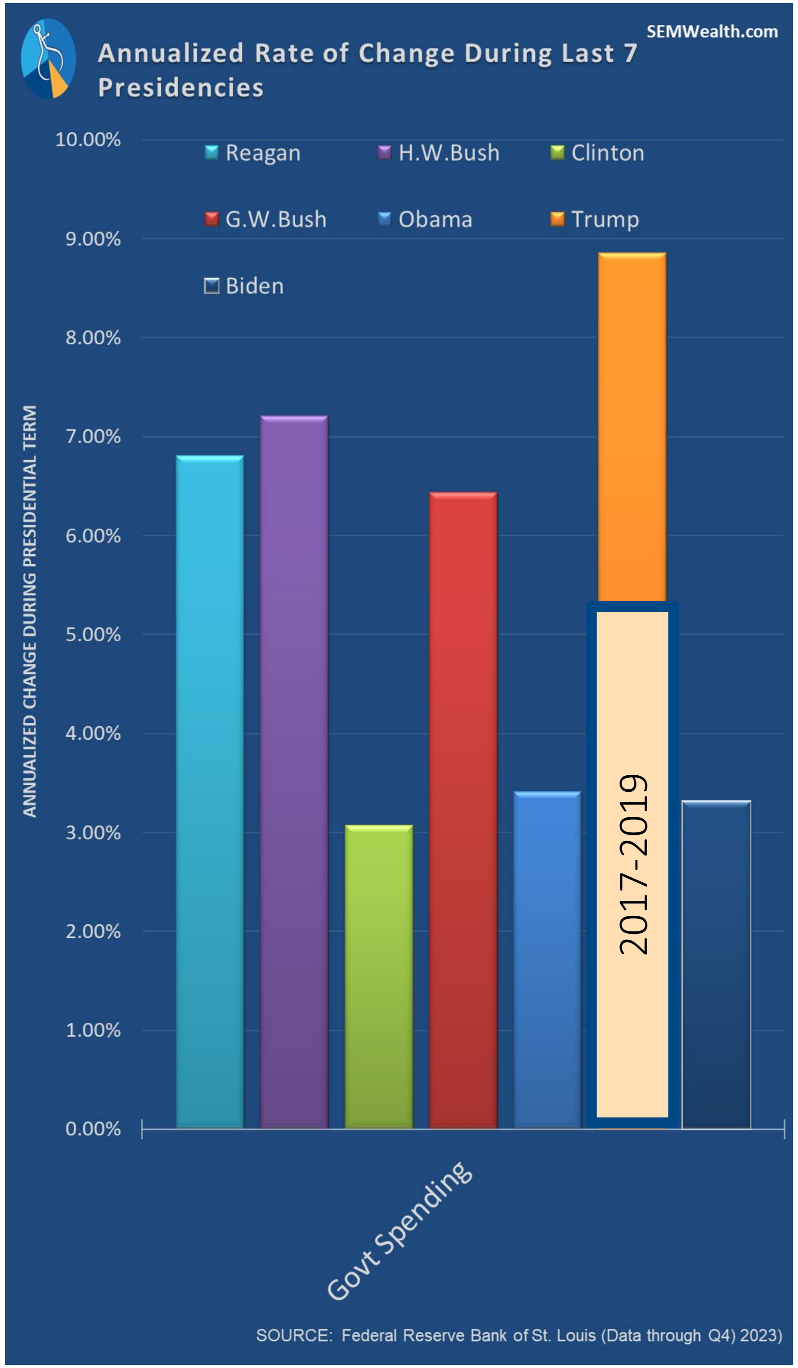


SOURCE: Federal Reserve Bank of St. Louis

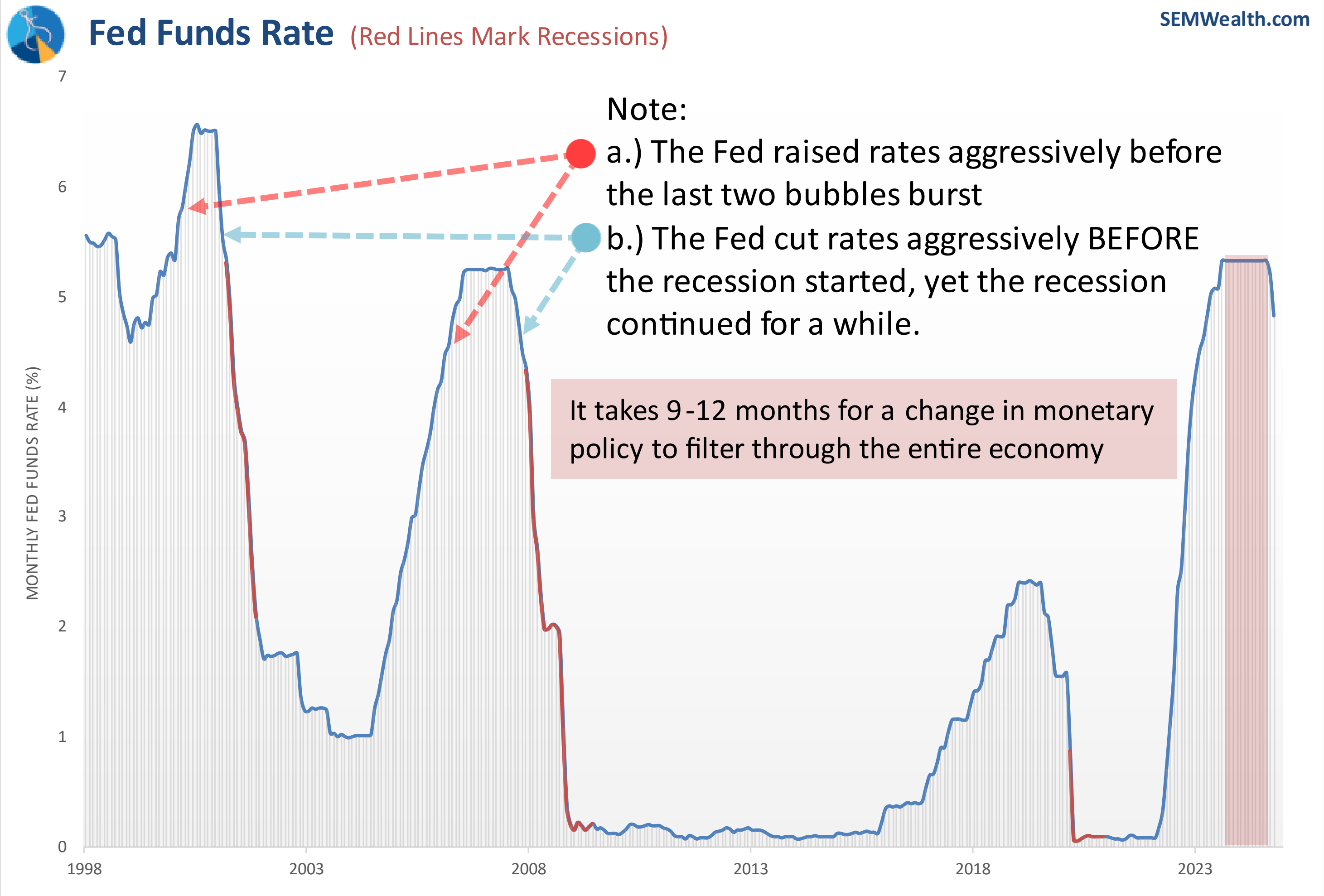
Investment Indicators



Government Indicators



SOURCE: Federal Reserve Bank of St. Louis (Data through Q4) 2023)



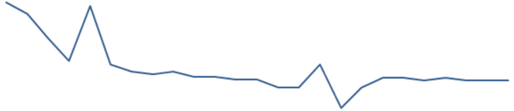
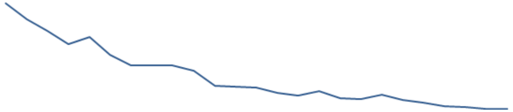
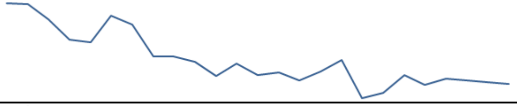
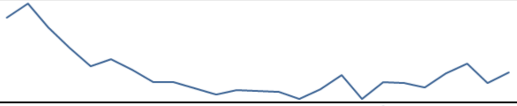
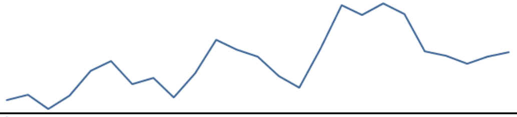
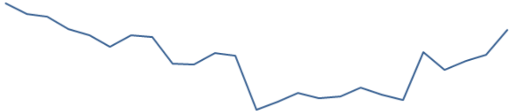
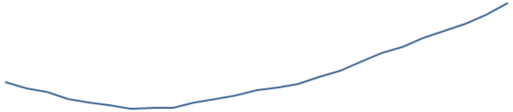
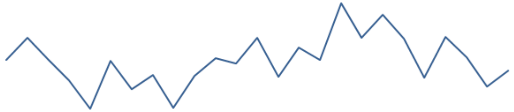
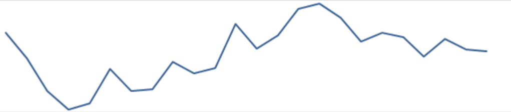
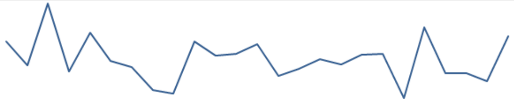
Note:

a.) The Fed raised rates aggressively before the last two bubbles burst

b.) The Fed cut rates aggressively BEFORE the recession started, yet the recession continued for a while.

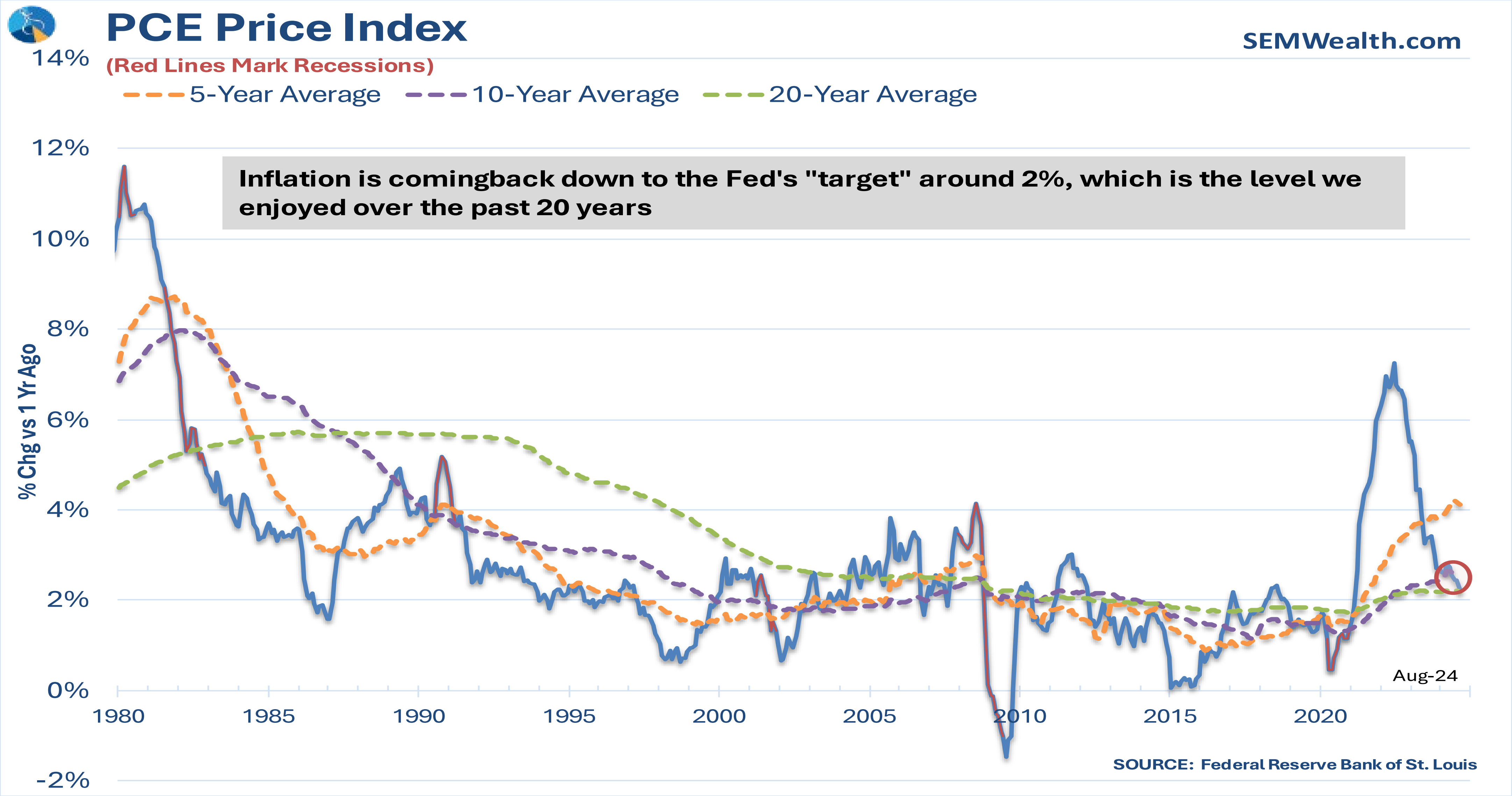
It takes 9-12 months for a change in monetary policy to filter through the entire economy

Economic Dashboard

Leading Indicator:	24 Month Trend:	GDP Indication:
Hours Worked		↔
Jobs		↔
Consumer Spending		↔
Capacity Utilization		↔
Consumer Sentiment		↓
Money Supply		↔
Stock Prices		↑
Consumer Goods Orders		↓
Building Permits		↓
Service Business Activity		↔

Economic Growth Drivers	
Well Above 2019 Levels	
Money Supply	216%
Consumer Spending	135%
Stock Prices	179%
Consumer Goods Orders	117%
Slightly Above 2019 Levels	
Service Business Activity	105%
Jobs	104%
Hours Worked	104%
Building Permits	101%
At 2019 Levels or Below	
Capacity Utilization	100%
Consumer Sentiment	68%

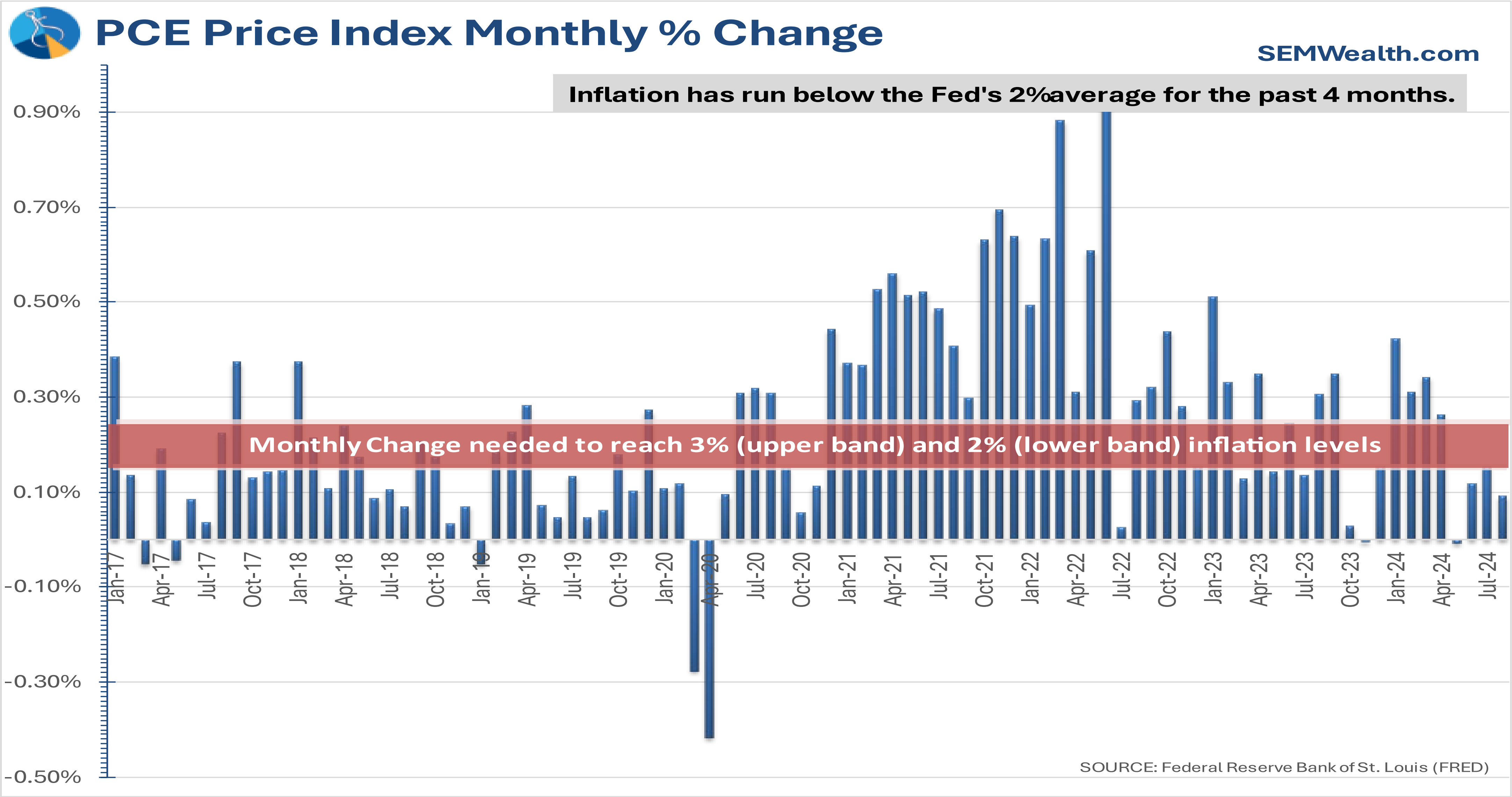
What about inflation?



Inflation is comingback down to the Fed's "target" around 2%, which is the level we enjoyed over the past 20 years

SOURCE: Federal Reserve Bank of St. Louis

What about inflation?



PCE Price Index Monthly % Change

SEMWealth.com

Inflation has run below the Fed's 2%average for the past 4 months.

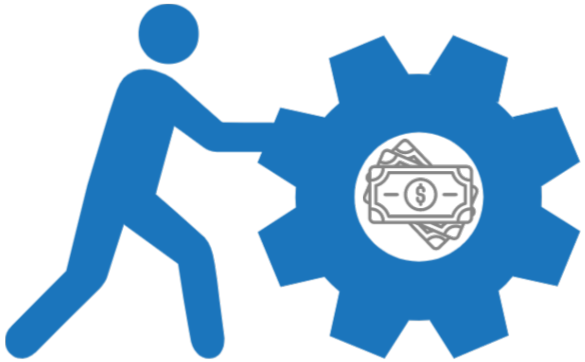
Monthly Change needed to reach 3% (upper band) and 2% (lower band) inflation levels

SOURCE: Federal Reserve Bank of St. Louis (FRED)

Revisiting the Potential GDP Equation

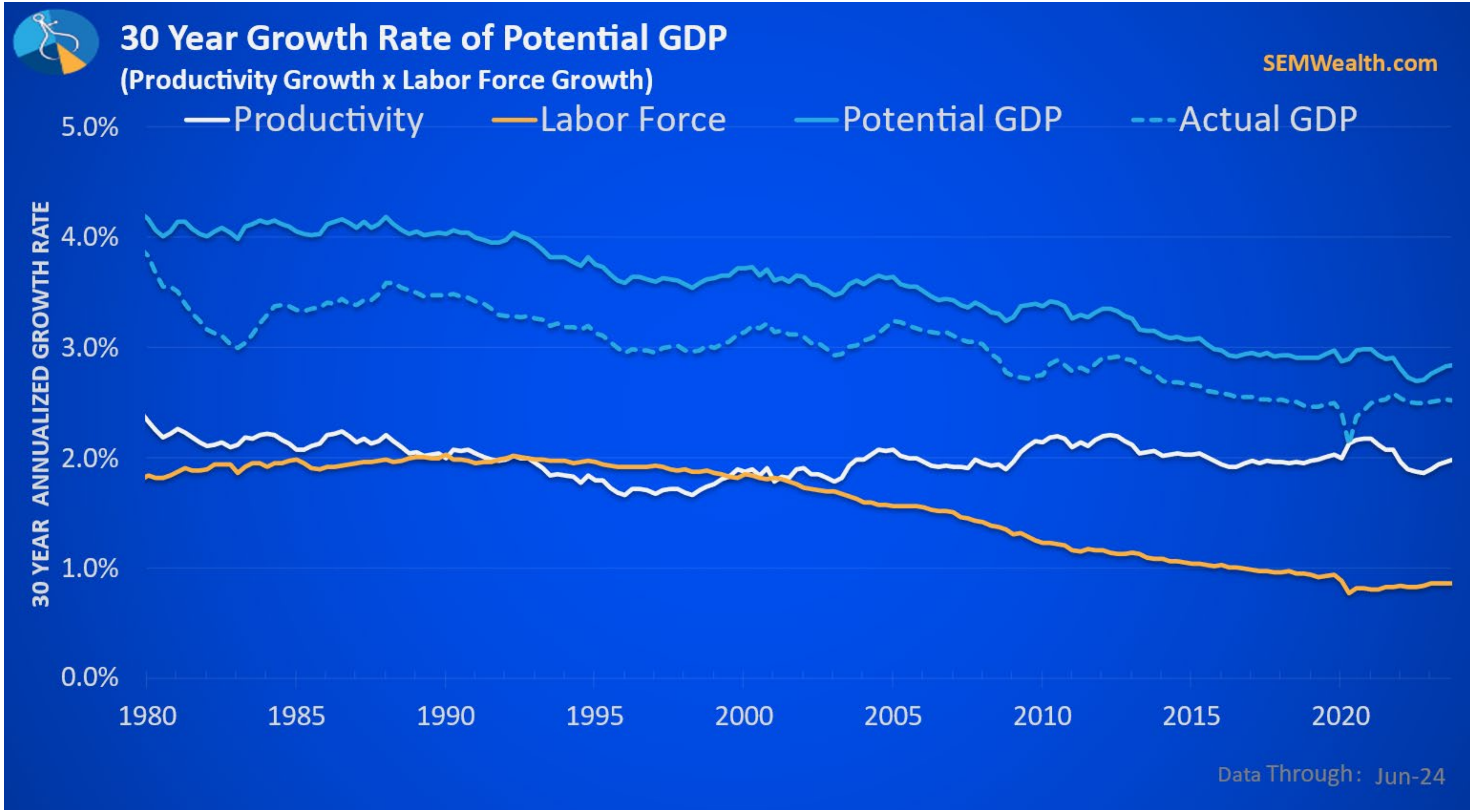
How many people are working?

+

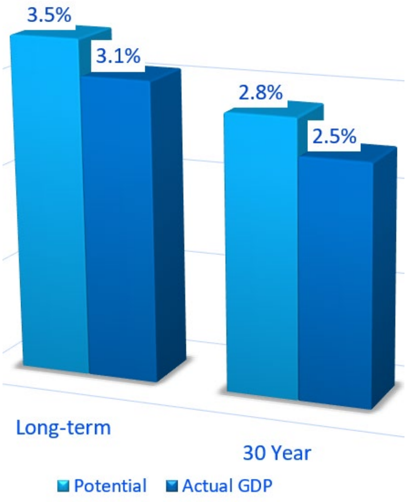


How much are they producing?

Revisiting the Potential GDP Equation



GDP has consistently grown below potential



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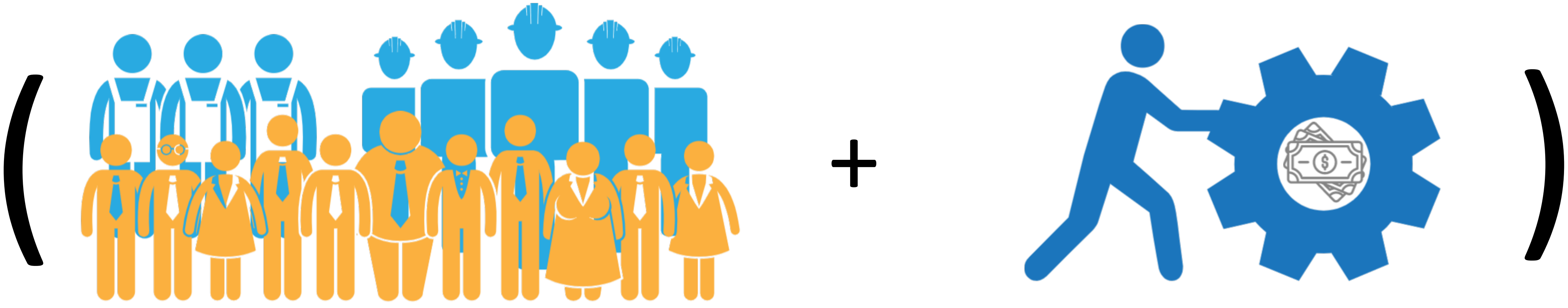
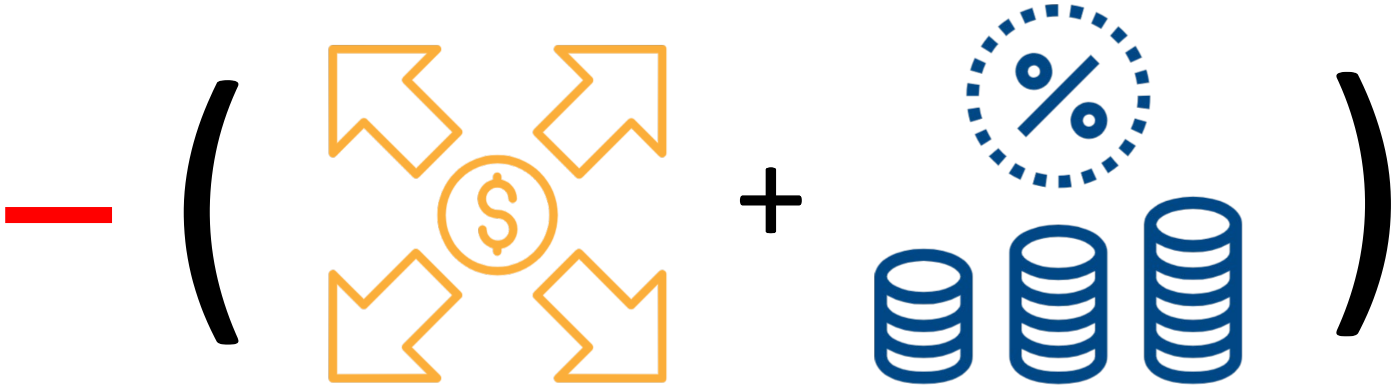


How many people are working?

How much are they producing?



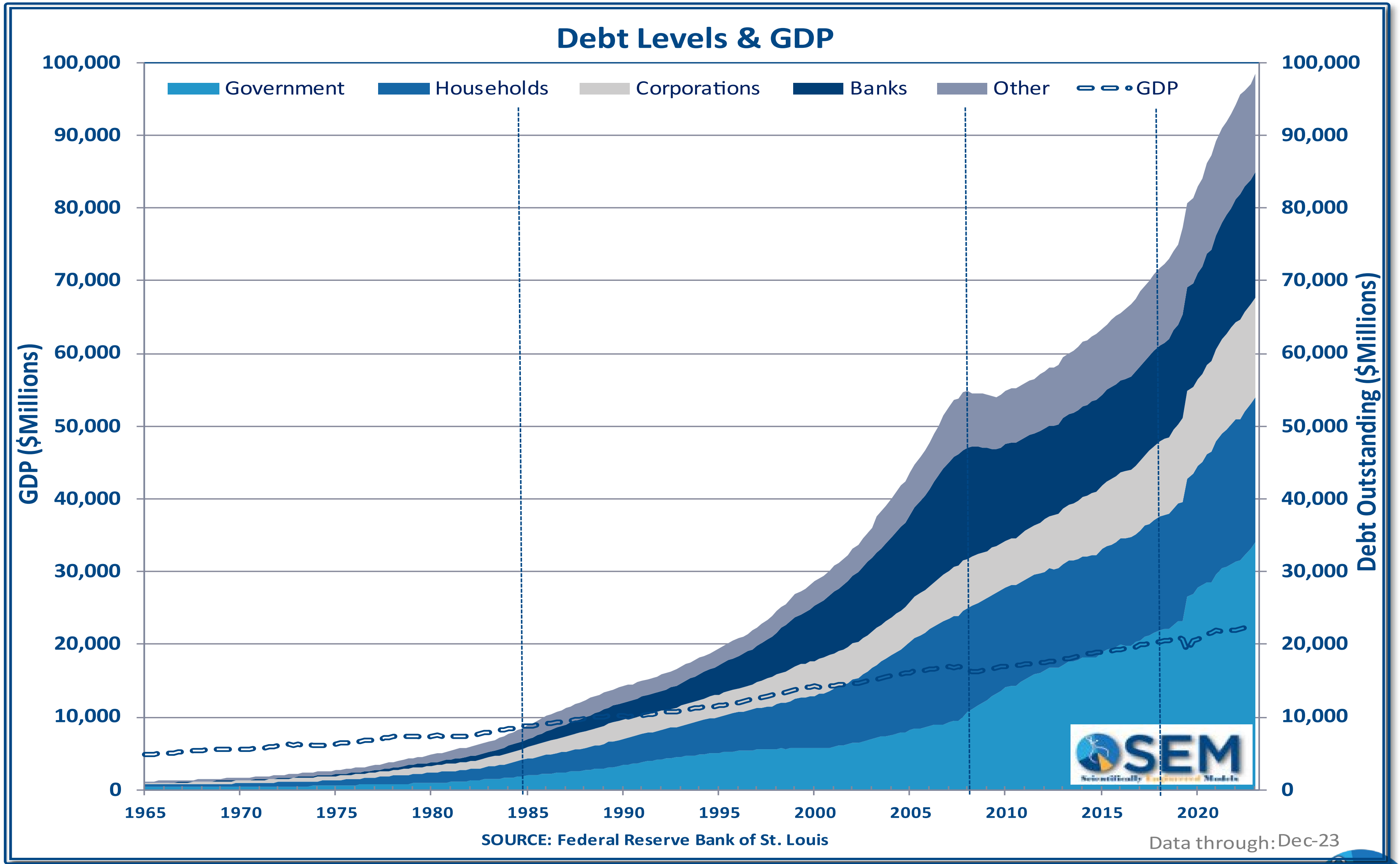
Net Exports

Interest Expense

Debt = Future Spending Brought Forward

- Debt is useful if used to INVEST in areas which will increase the growth rate
- If used for current spending, it is a drag on future growth
- Key turning points: 1984, 2009, 2012, 2018

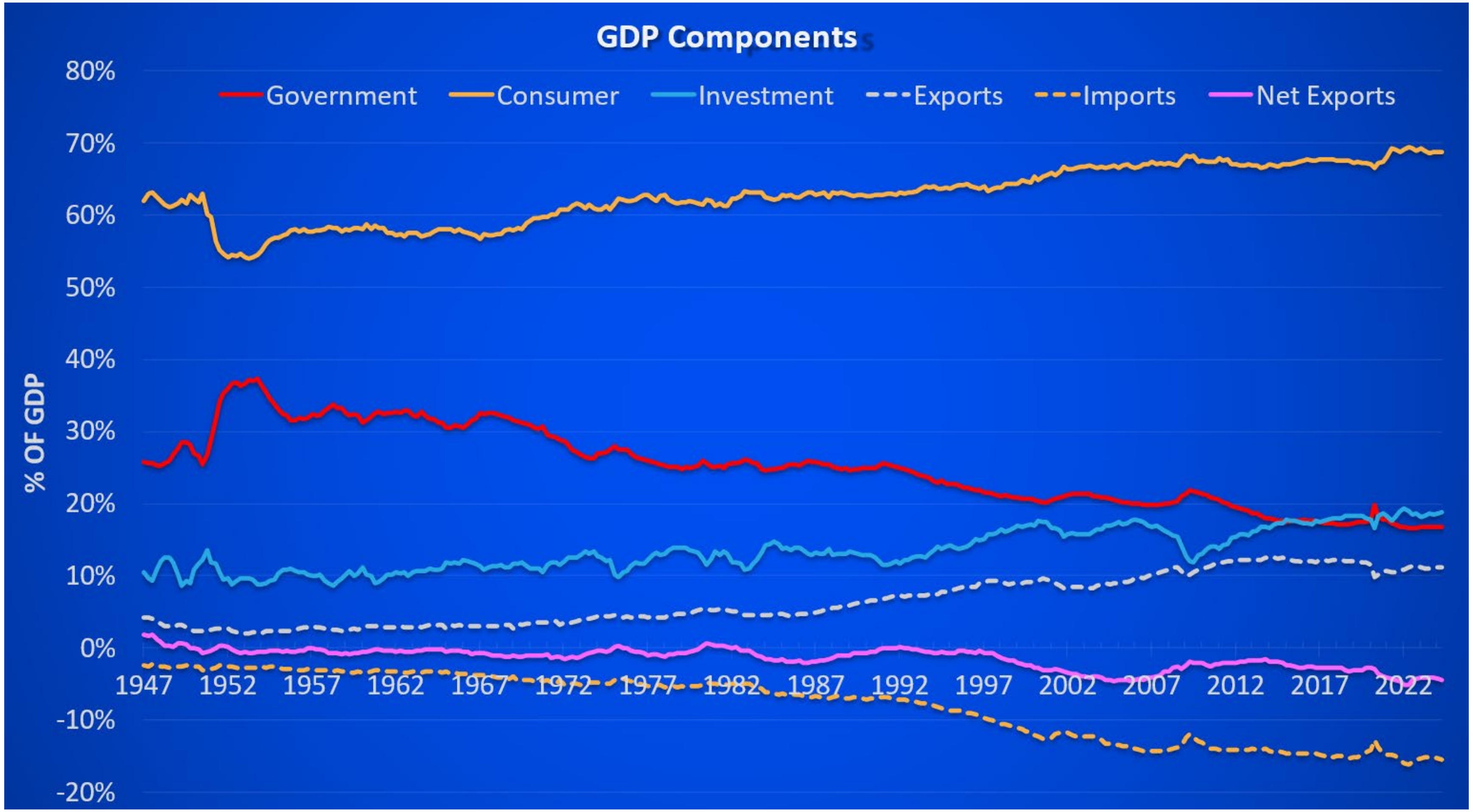
Debt Levels & GDP

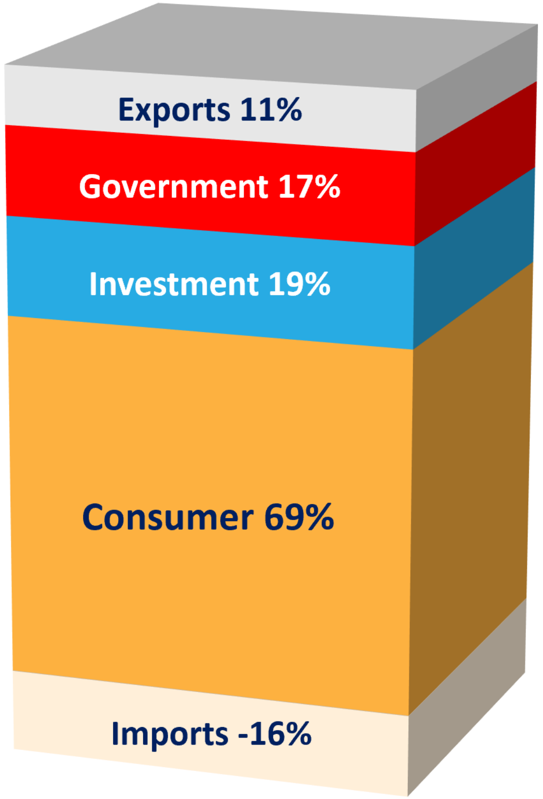


SOURCE: Federal Reserve Bank of St. Louis

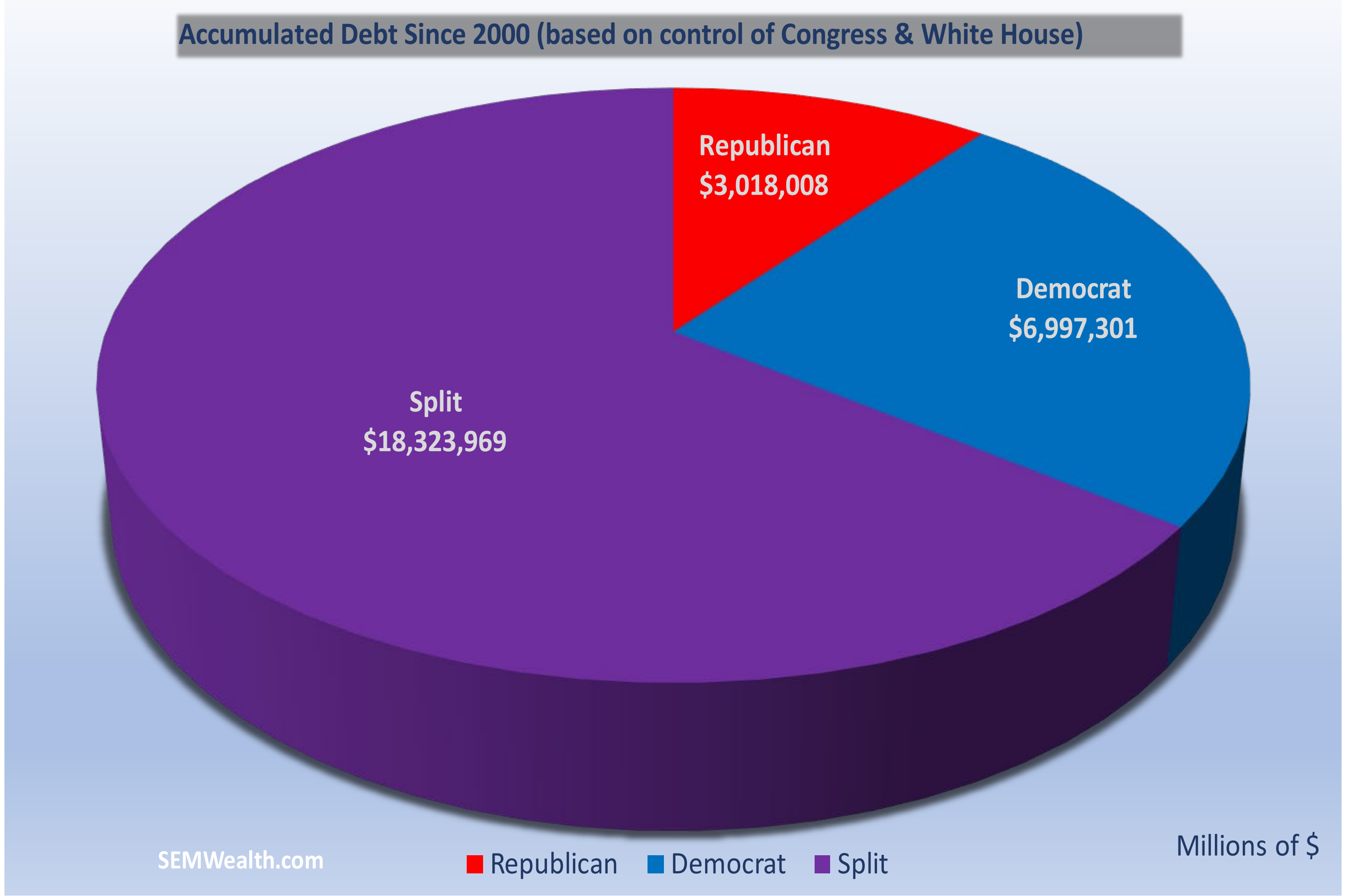
Data through: Dec-23

GDP Components





Who is responsible for the debt?



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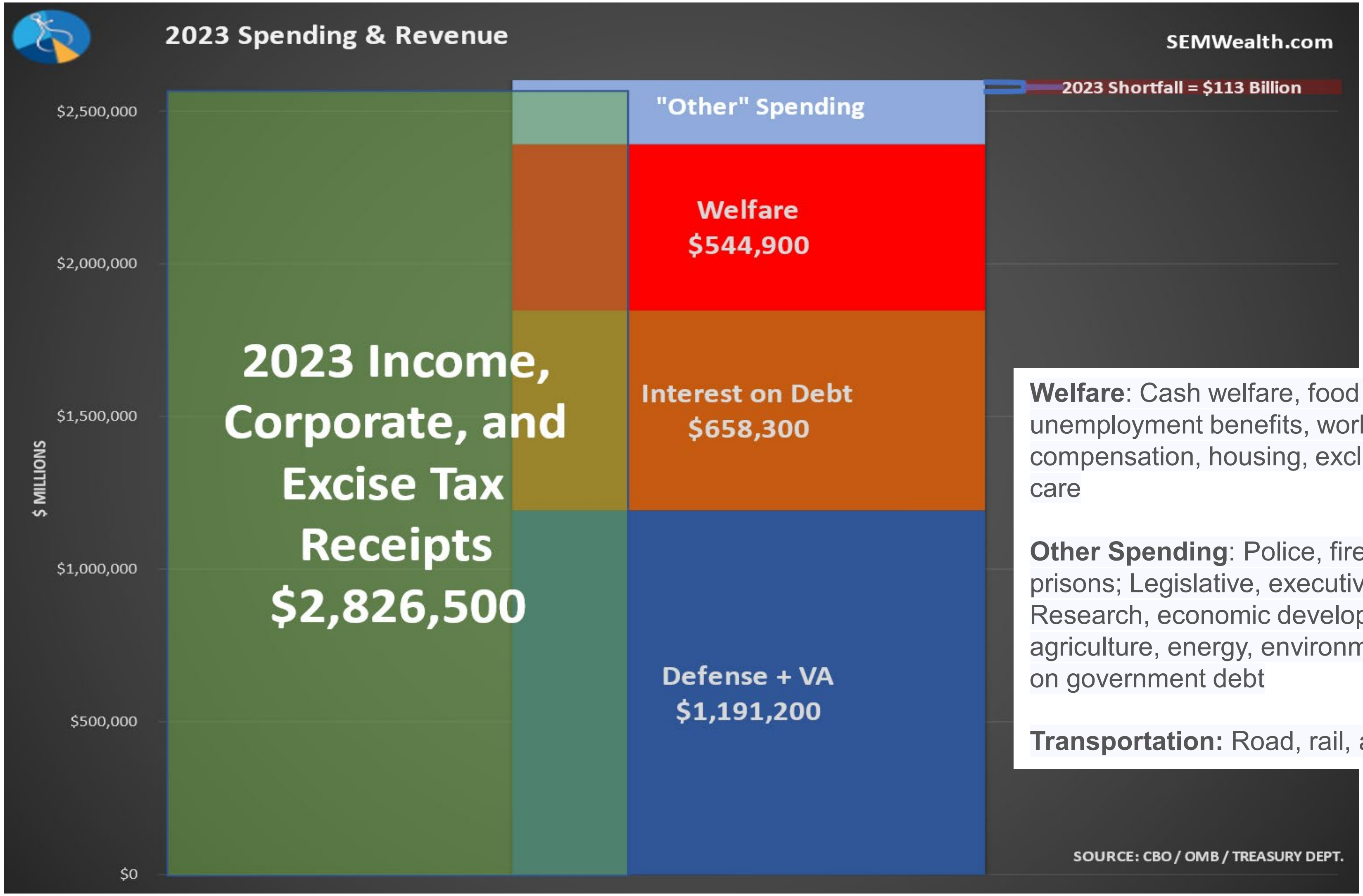

SOURCE: CBO / OMB / TREASURY DEPT.

Welfare: Cash welfare, food stamps, unemployment benefits, workers compensation, housing, excluding health care

Other Spending: Police, fire, law courts, prisons; Legislative, executive, finance; Research, economic development, agriculture, energy, environment; Interest on government debt

Transportation: Road, rail, airports

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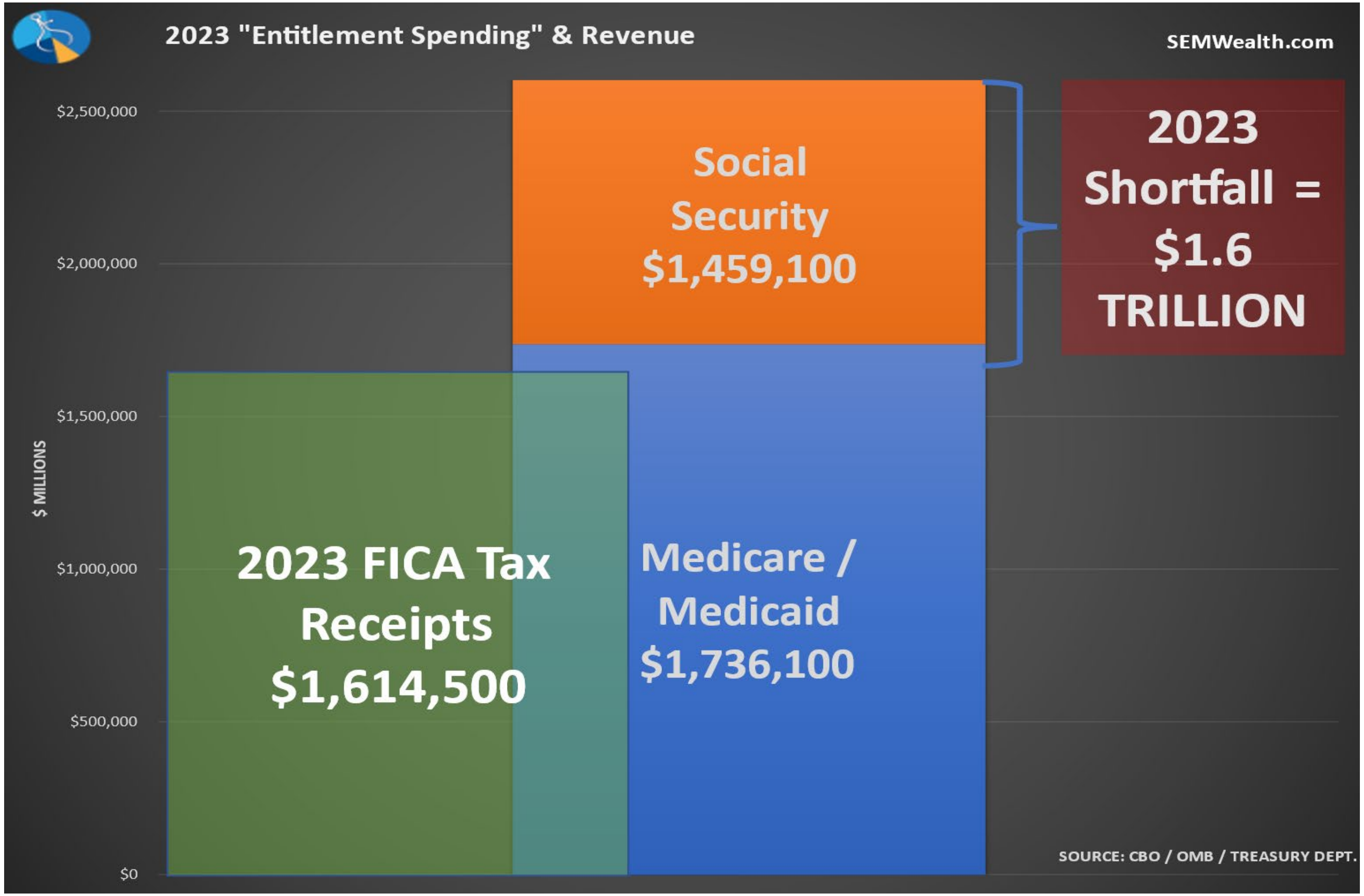

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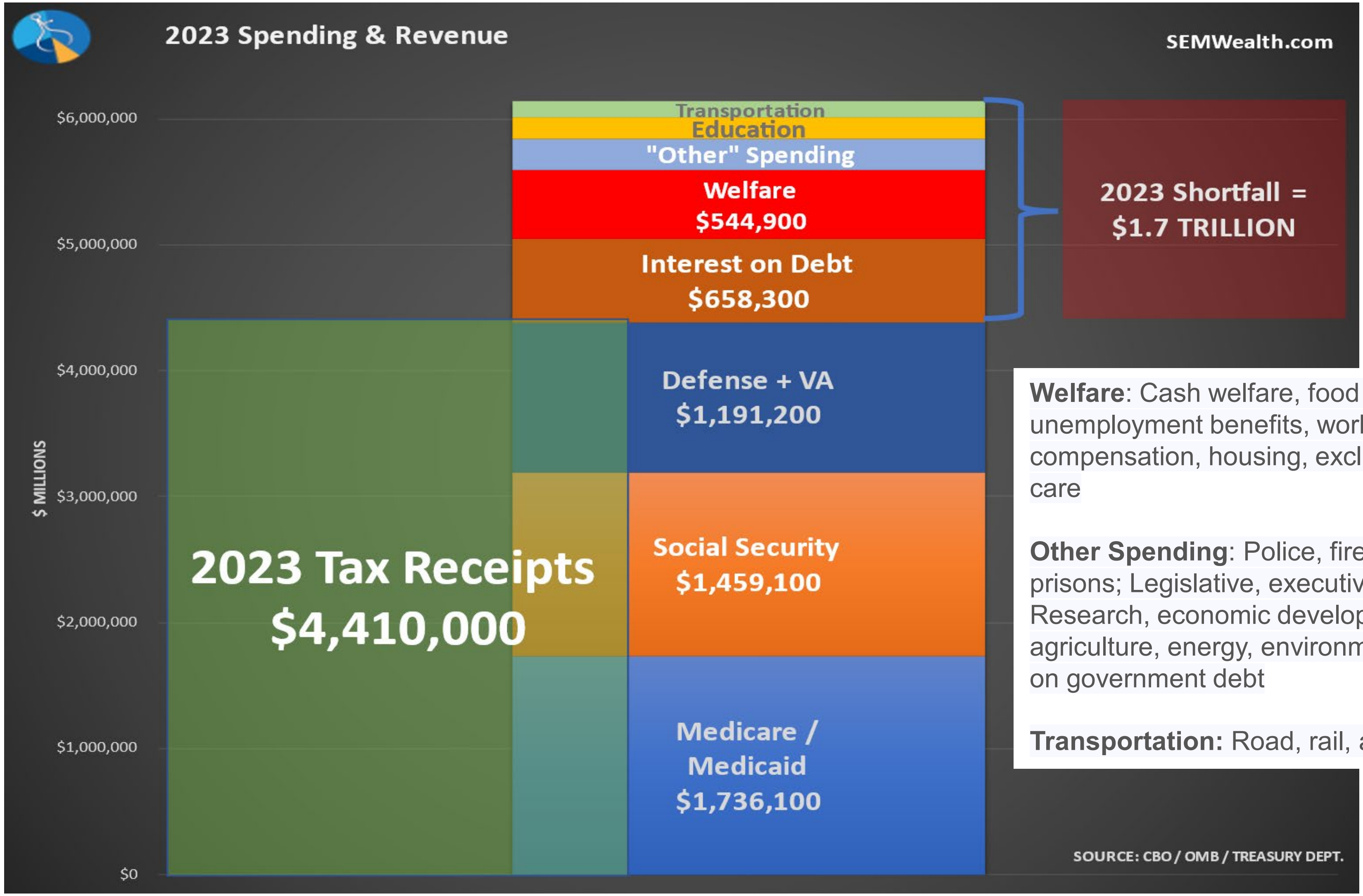

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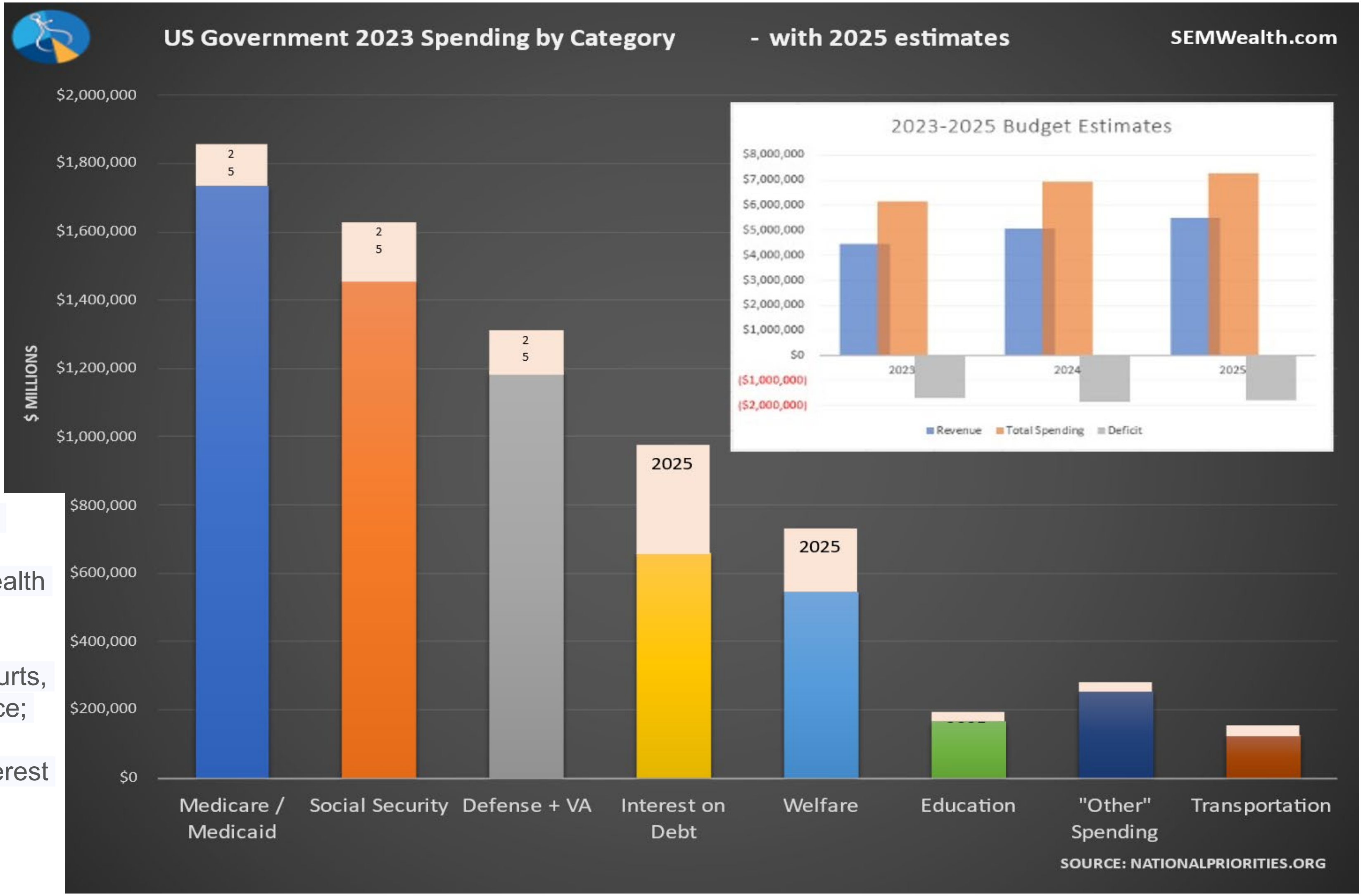

SOURCE: NATIONALPRIORITIES.ORG

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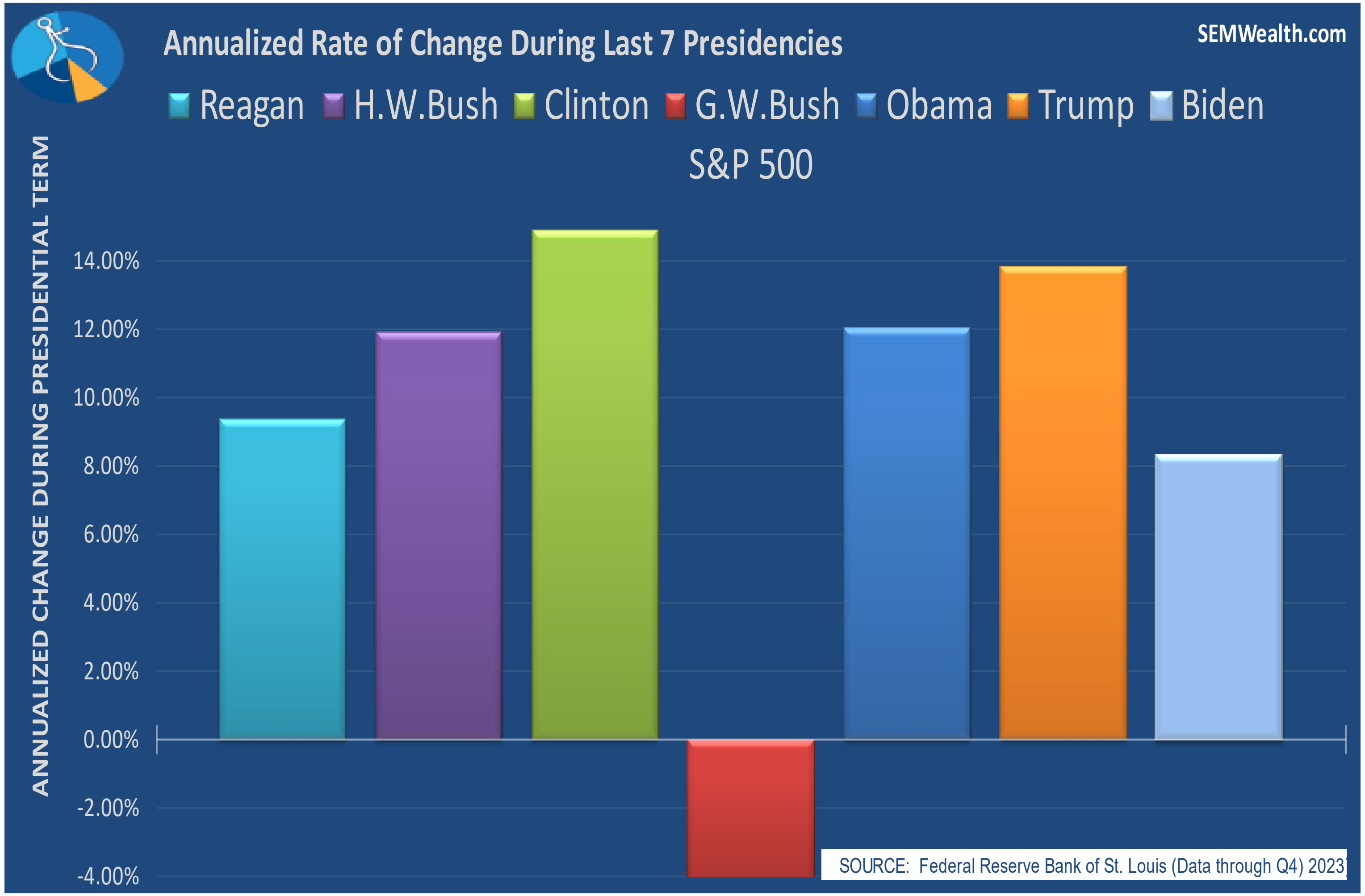
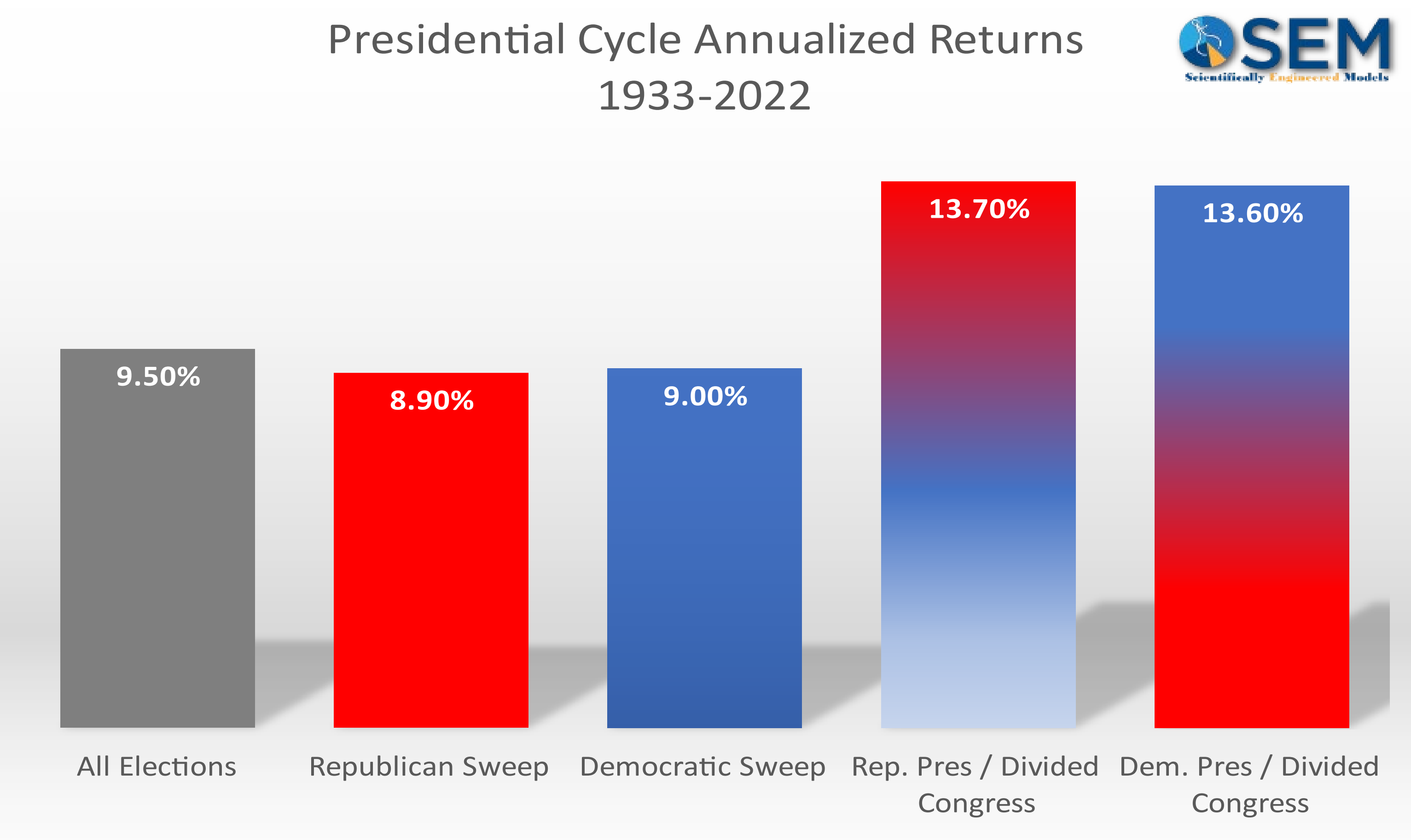
Which party does the market love the most?



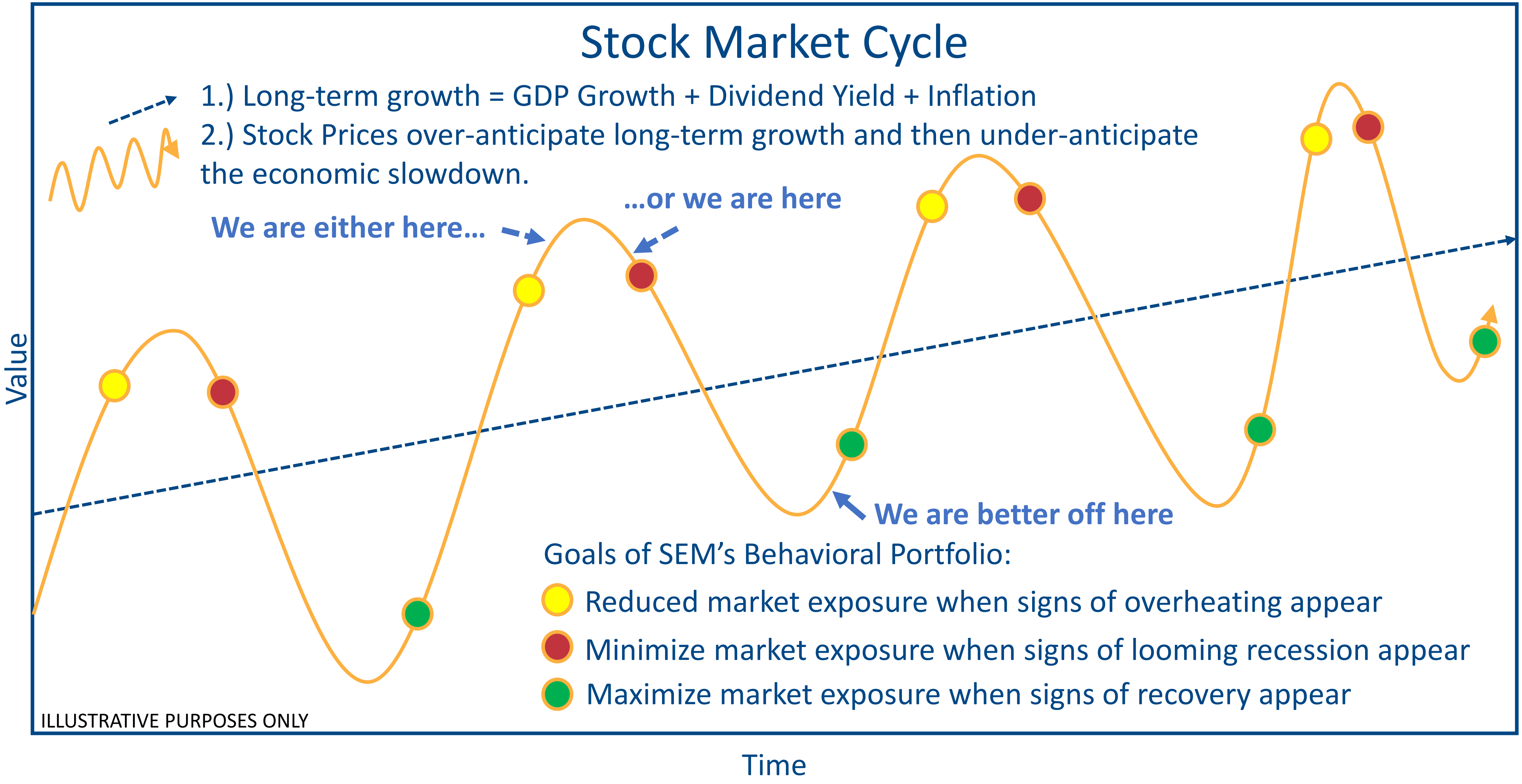
SOURCE: Federal Reserve Bank of St. Louis (Data through Q4) 2023

Which party does the market love the most?



SOURCE: Fidelity | INFORMATIONAL PURPOSES ONLY,NOT CONSIDERED INVESTMENT ADVICE | Past performance is not a gurantee of future results. Data shows the S&P 500 returns for the 4 year presidential terms since 1933.

Why use a Behavioral Approach?



Stock Market Cycle

1.) Long-term growth = GDP Growth + Dividend Yield + Inflation

2.) Stock Prices over-anticipate long-term growth and then under-anticipate the economic slowdown.

We are either here…

…or we are here

We are better off here

Goals of SEM's Behavioral Portfolio:

- 🟡 Reduced market exposure when signs of overheating appear
- 🔴 Minimize market exposure when signs of looming recession appear
- 🟢 Maximize market exposure when signs of recovery appear

ILLUSTRATIVE PURPOSES ONLY

High Valuations – Low Future Returns

Forward 10-Year Return Expectations (Annualized)

MORNINGSTAR

- US Stocks: +4.6%
- US Bonds: +4.3%

60/40 Portfolio: +4.5%

(as of 12/31/2024)

Vanguard®

- US Stocks: +4.2%
- US Bonds: +5.0%

60/40 Portfolio: +4.7%

(as of 8/31/24)

BlackRock®

- US Stocks: +6.1%
- US Bonds: +3.9%

60/40 Portfolio: +5.2%

(as of 8/31/24)

Long-term Annualized Returns (1926-2024)

- US Stocks: +10.2%
- US Bonds: +5.5%

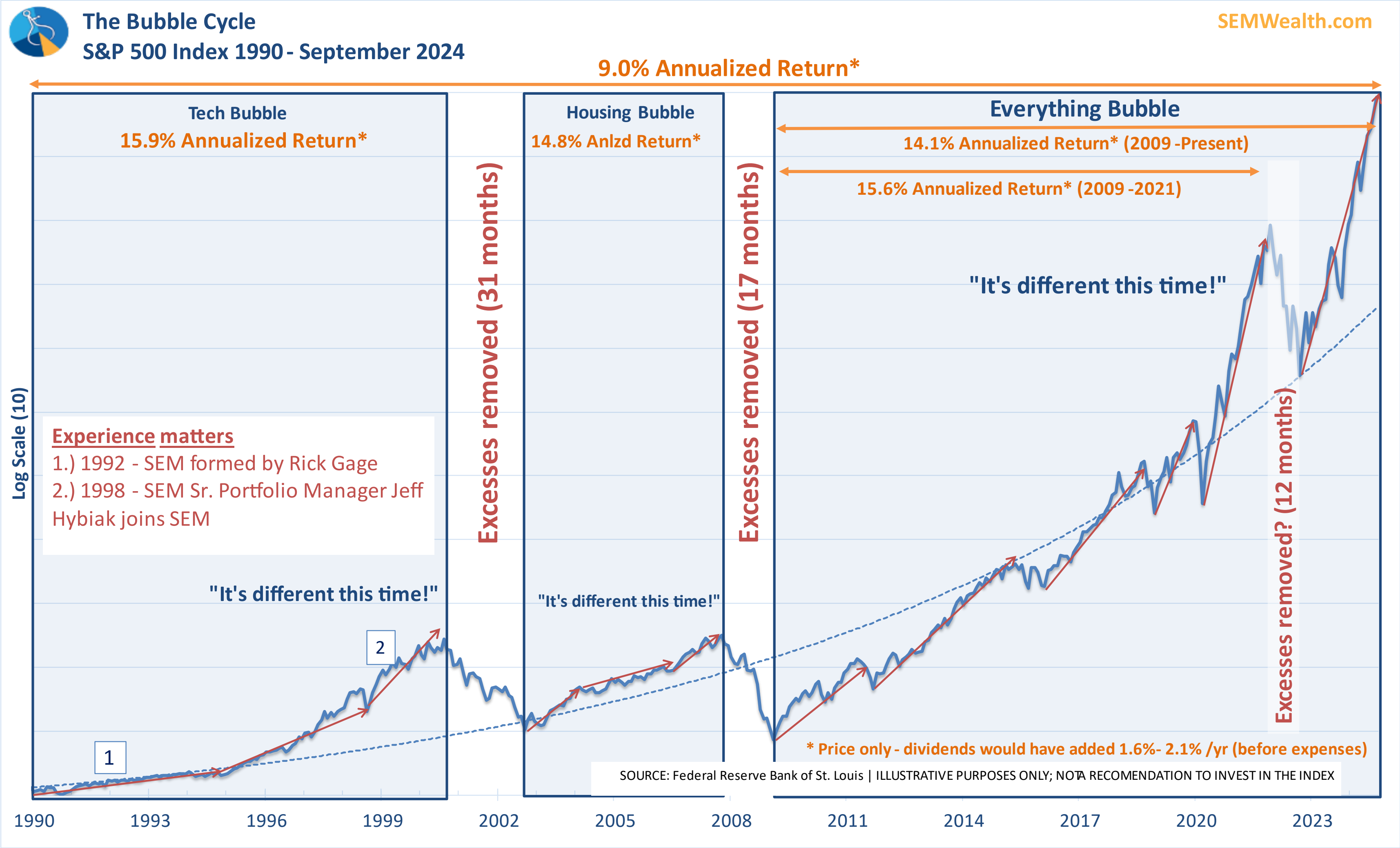
60/40 Portfolio: +8.3%

SOURCE: Ibbotson / CFA Institute

Long-Term Outlook

Investors often look at the past bear markets and with hindsight believe they could have avoided it. This leads to overconfidence in their ability to recognize the next looming bear market. In addition, the longer the market moves higher the more likely conservative investors are going to abandon their lower risk investments and move into riskier assets.

Stocks are a “mean-reverting” asset, meaning after prolonged periods above the long-term average, they will go through a sharp correction.



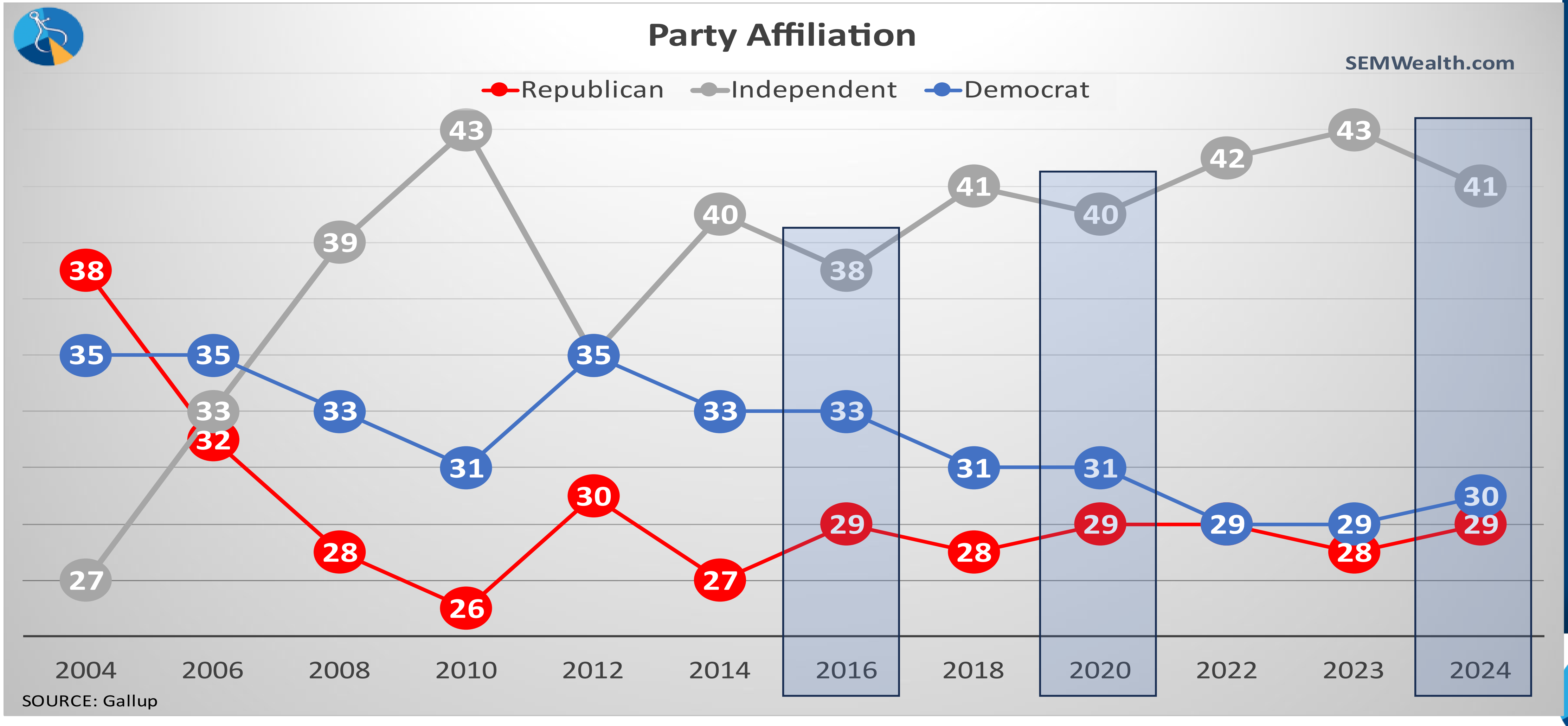
The Bubble Cycle
S&P 500 Index 1990 - September 2024

Experience matters
1.) 1992 - SEM formed by Rick Gage
2.) 1998 - SEM Sr. Portfolio Manager Jeff Hybiak joins SEM

* Price only - dividends would have added 1.6%- 2.1% /yr (before expenses)

SOURCE: Federal Reserve Bank of St. Louis | ILLUSTRATIVE PURPOSES ONLY; NOT A RECOMENDATION TO INVEST IN THE INDEX

Whomever wins, it will not be a 'mandate'



SOURCE: Gallup

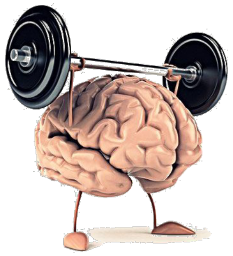
We must understand…..

- Major **economic policies** do not change on day 1 (only regulatory guidance as allowed…..after legal challenges)
- Campaign **talking points** do not always become priorities once the election is won
- It is difficult to pass **economic polices** which both sides do not agree with
- The stock market is a 'forward-looking mechanism', meaning it will **anticipate changes BEFORE they happen**
- We will have **plenty of time to adjust** to any major financial changes BEFORE they become law
- The stock market historically **prefers a SPLIT** in Washington

Behavioral Finance 101

Drs. Daniel Kahneman & Amos Tversky

Your Two Brains



Dr. Richard Thaler

Econs (Robots) vs Humans

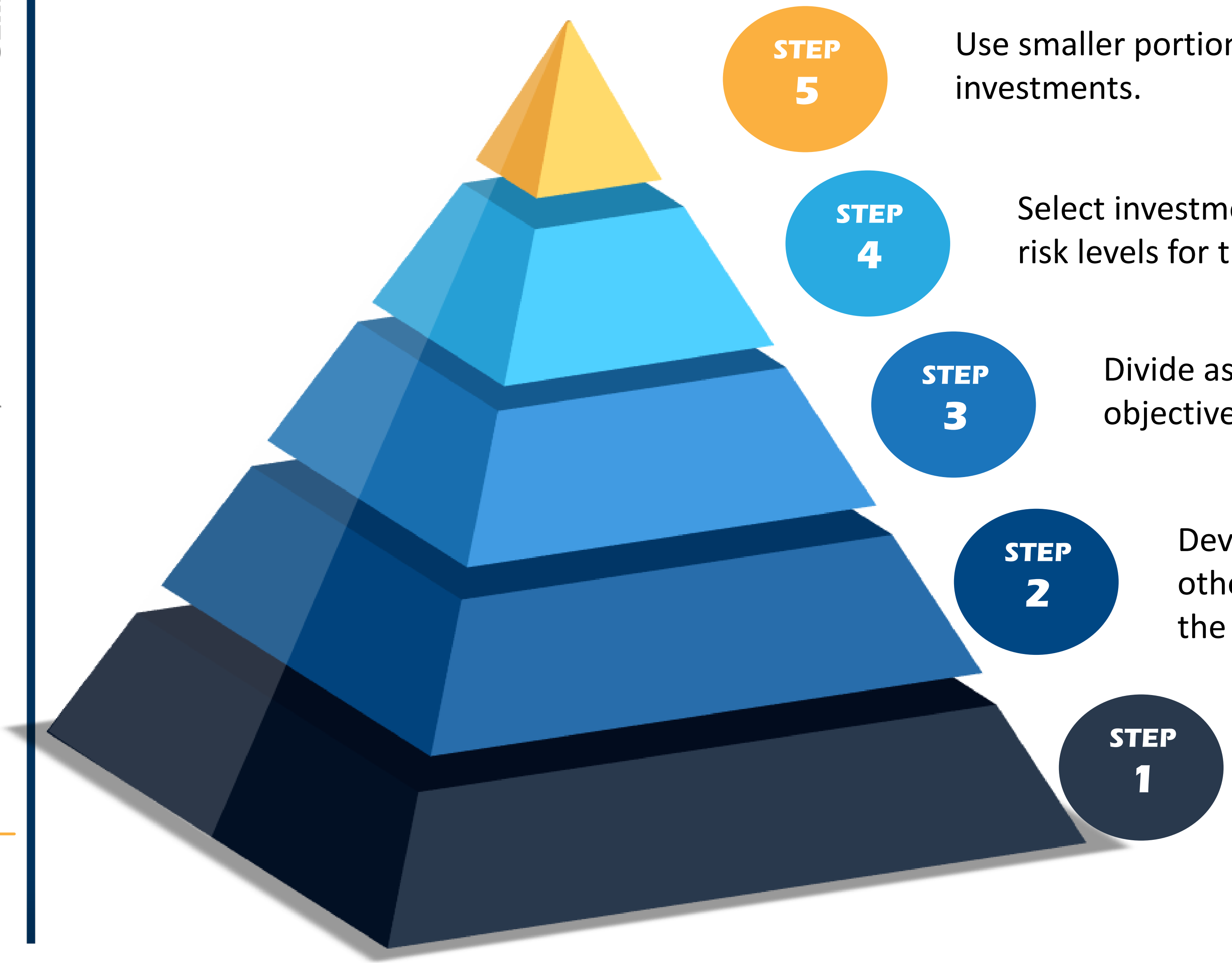
CLEARANCE
SALE

Key of Behavioral Finance:

1.) Our brains use short-cuts to make difficult decisions

2.) Our actions do not match the economic models

A Behavioral Portfolio Approach



STEP 5 Use smaller portions of portfolio for concentrated or riskier investments.

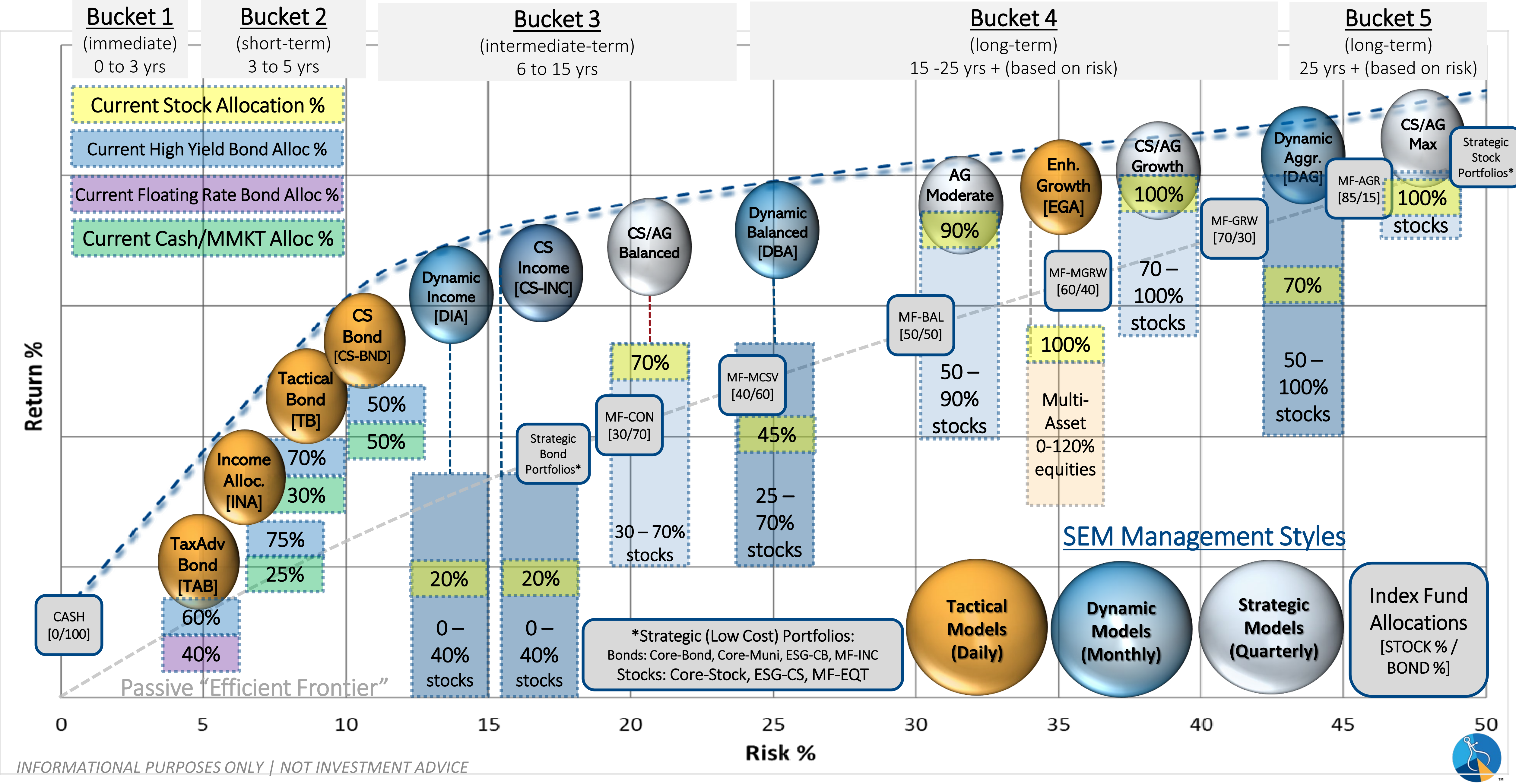
STEP 4 Select investments that align with specific objectives and risk levels for that layer.

STEP 3 Divide assets into specific layers and set specific goals and objectives for each layer.

STEP 2 Develop cash flow strategy taking into consideration cash and other low risk investments. This reduces short-term risk and the likelihood of making short-term, emotional decisions.

STEP 1 Construct complete financial plan with specific goals and objectives.

Process in Motion – Allocations as of 9/30/2024



Bucket 1
(immediate)
0 to 3 yrs

Bucket 2
(short-term)
3 to 5 yrs

Bucket 3
(intermediate-term)
6 to 15 yrs

Bucket 4
(long-term)
15 -25 yrs + (based on risk)

Bucket 5
(long-term)
25 yrs + (based on risk)

- Current Stock Allocation %
- Current High Yield Bond Alloc %
- Current Floating Rate Bond Alloc %
- Current Cash/MMKT Alloc %

*Strategic (Low Cost) Portfolios:
Bonds: Core-Bond, Core-Muni, ESG-CB, MF-INC
Stocks: Core-Stock, ESG-CS, MF-EQT

SEM Management Styles

- Tactical Models (Daily)
- Dynamic Models (Monthly)
- Strategic Models (Quarterly)
- Index Fund Allocations [STOCK % / BOND %]

For more information go to

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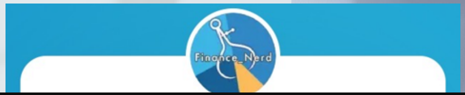
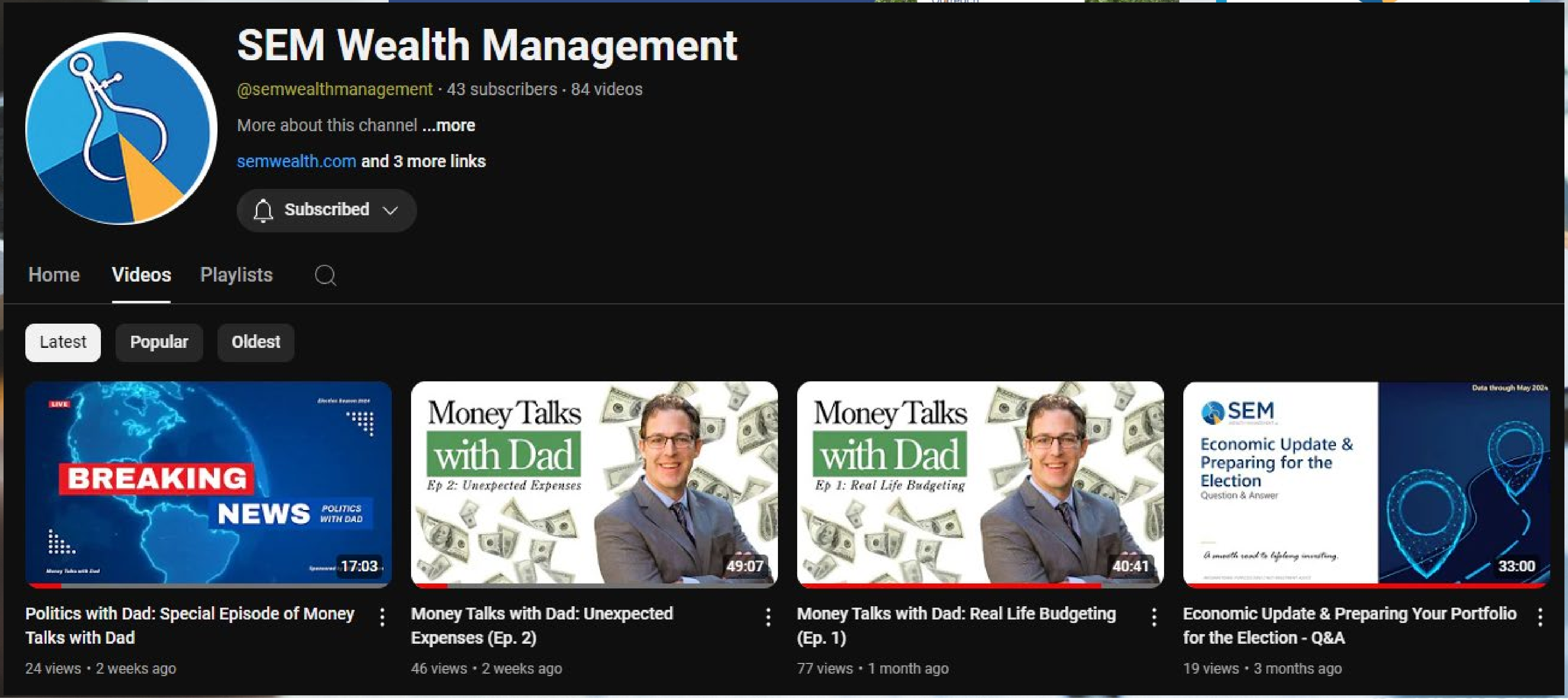

Finance Nerd



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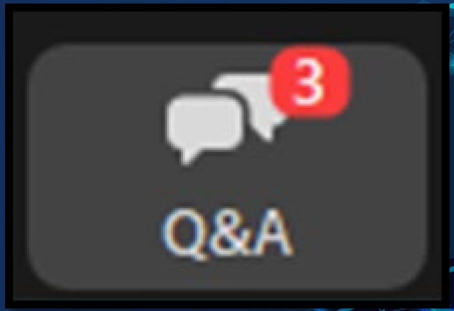
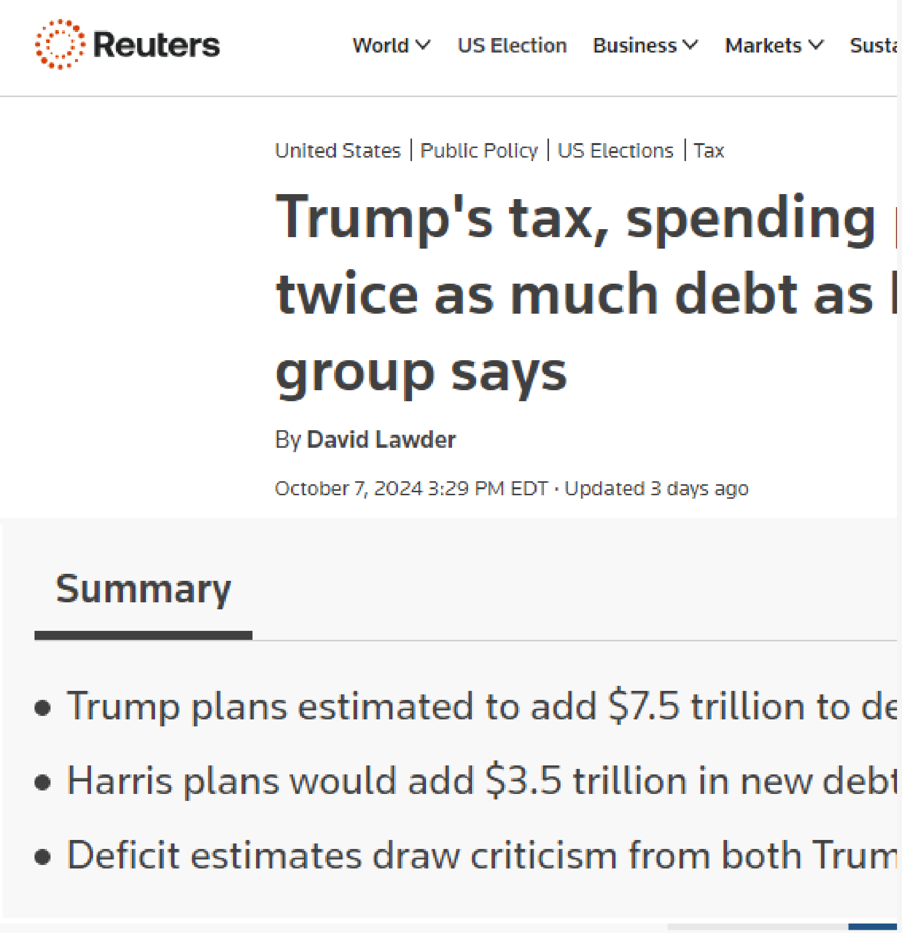
17:03
Money Talks with Dad
Ep 2: Unexpected Expenses
49:07
Money Talks with Dad
Ep 1: Real Life Budgeting
40:41
SEM
Economic Update & Preparing for the Election
Question & Answer
Data through May 2024
33:00

QUESTIONS?



> *“The biggest difference I see in the candidates is the tax consequences for investors and businesses. Can you address this please?”*
>
> -Mark M.

Tax Proposals



United States | Public Policy | US Elections | Tax

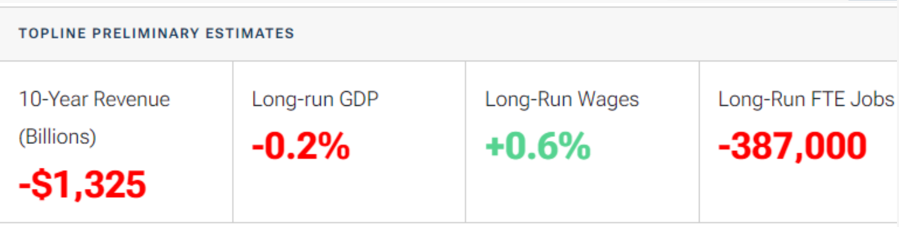
Trump's tax, spending
twice as much debt as
group says

By **David Lawder**

October 7, 2024 3:29 PM EDT · Updated 3 days ago

Summary

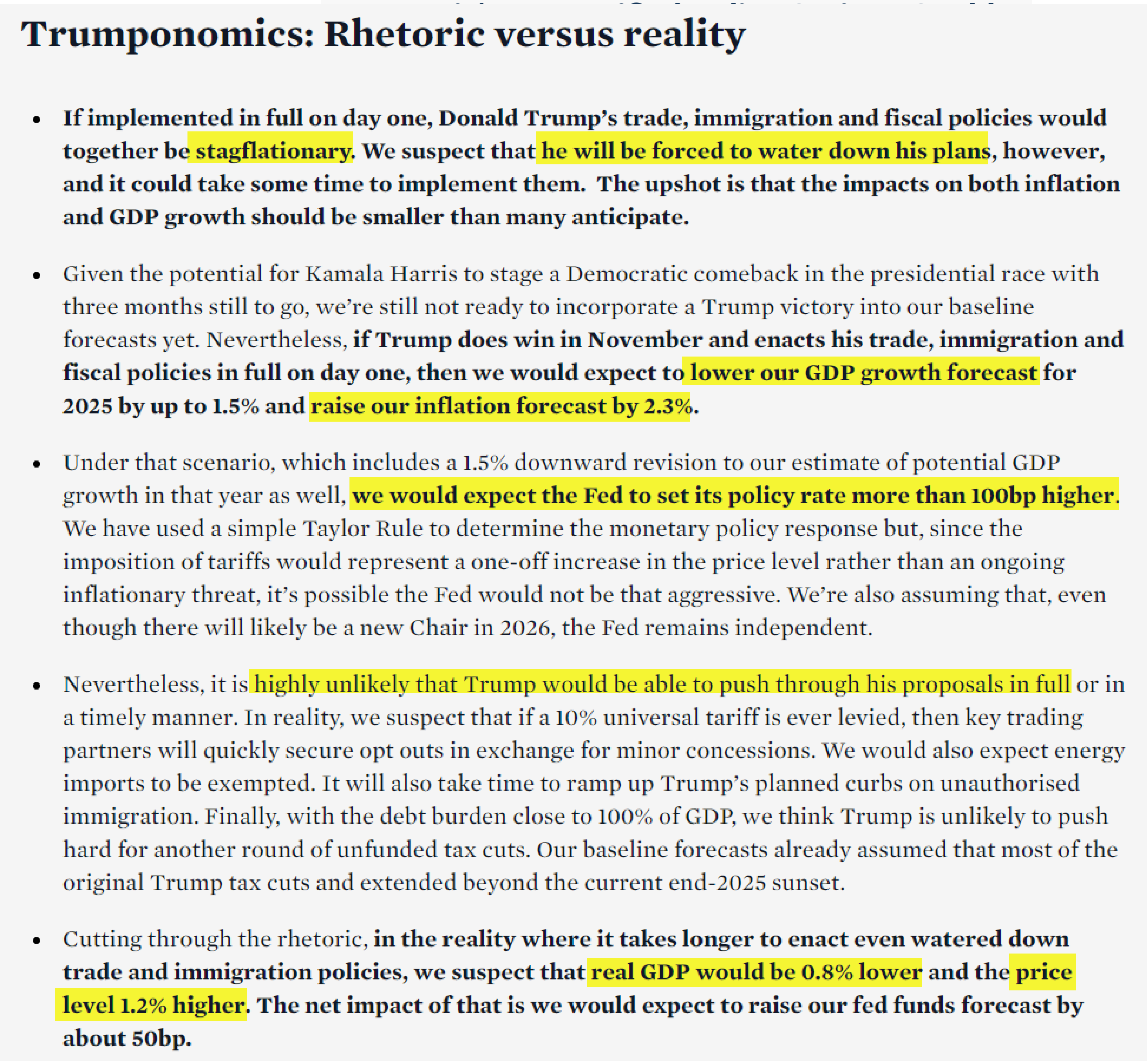
- Trump plans estimated to add $7.5 trillion to de
- Harris plans would add $3.5 trillion in new debt
- Deficit estimates draw criticism from both Trum



TOPLINE PRELIMINARY ESTIMATES

10-Year Revenue (Billions)	Long-run GDP	Long-Run Wages	Long-Run FTE Jobs
-$1,325	-0.2%	+0.6%	-387,000

Tax Foundation General Equilibrium Model, September 2024

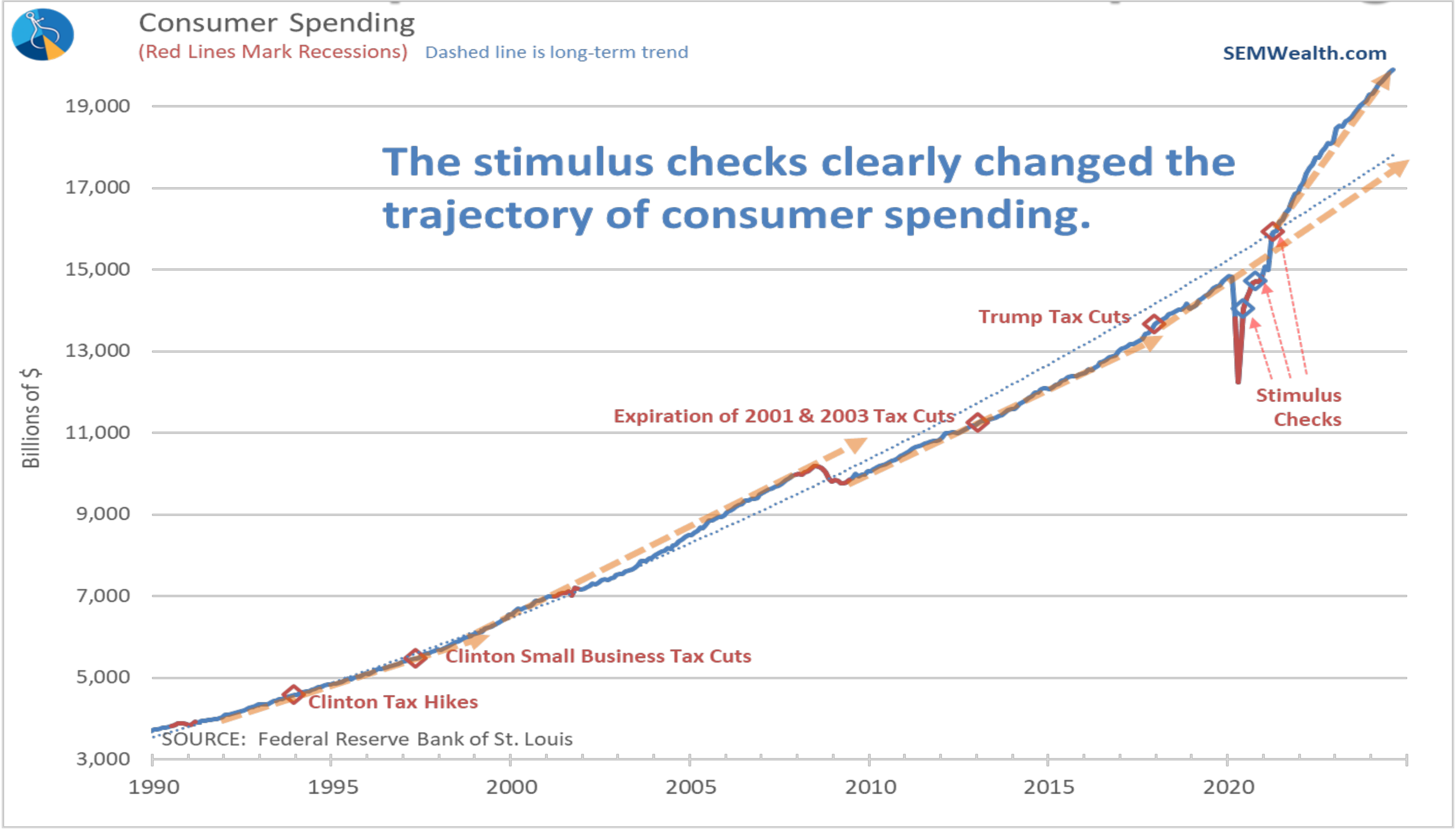


Trumponomics: Rhetoric versus reality

- **If implemented in full on day one, Donald Trump's trade, immigration and fiscal policies would together be stagflationary. We suspect that he will be forced to water down his plans, however, and it could take some time to implement them. The upshot is that the impacts on both inflation and GDP growth should be smaller than many anticipate.**
- Given the potential for Kamala Harris to stage a Democratic comeback in the presidential race with three months still to go, we're still not ready to incorporate a Trump victory into our baseline forecasts yet. Nevertheless, **if Trump does win in November and enacts his trade, immigration and fiscal policies in full on day one, then we would expect to lower our GDP growth forecast for 2025 by up to 1.5% and raise our inflation forecast by 2.3%.**
- Under that scenario, which includes a 1.5% downward revision to our estimate of potential GDP growth in that year as well, **we would expect the Fed to set its policy rate more than 100bp higher**. We have used a simple Taylor Rule to determine the monetary policy response but, since the imposition of tariffs would represent a one-off increase in the price level rather than an ongoing inflationary threat, it's possible the Fed would not be that aggressive. We're also assuming that, even though there will likely be a new Chair in 2026, the Fed remains independent.
- Nevertheless, it is highly unlikely that Trump would be able to push through his proposals in full or in a timely manner. In reality, we suspect that if a 10% universal tariff is ever levied, then key trading partners will quickly secure opt outs in exchange for minor concessions. We would also expect energy imports to be exempted. It will also take time to ramp up Trump's planned curbs on unauthorised immigration. Finally, with the debt burden close to 100% of GDP, we think Trump is unlikely to push hard for another round of unfunded tax cuts. Our baseline forecasts already assumed that most of the original Trump tax cuts and extended beyond the current end-2025 sunset.
- Cutting through the rhetoric, **in the reality where it takes longer to enact even watered down trade and immigration policies, we suspect that real GDP would be 0.8% lower and the price level 1.2% higher. The net impact of that is we would expect to raise our fed funds forecast by about 50bp.**

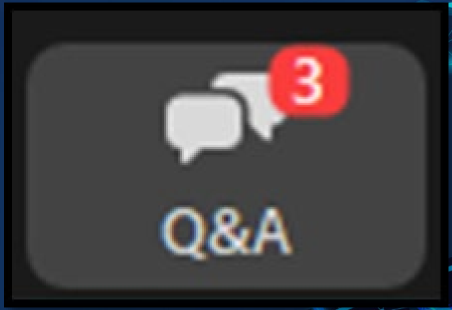
TAX FOUNDATION

Taxes & Impact on Consumer Spending



SOURCE: Federal Reserve Bank of St. Louis

QUESTIONS?



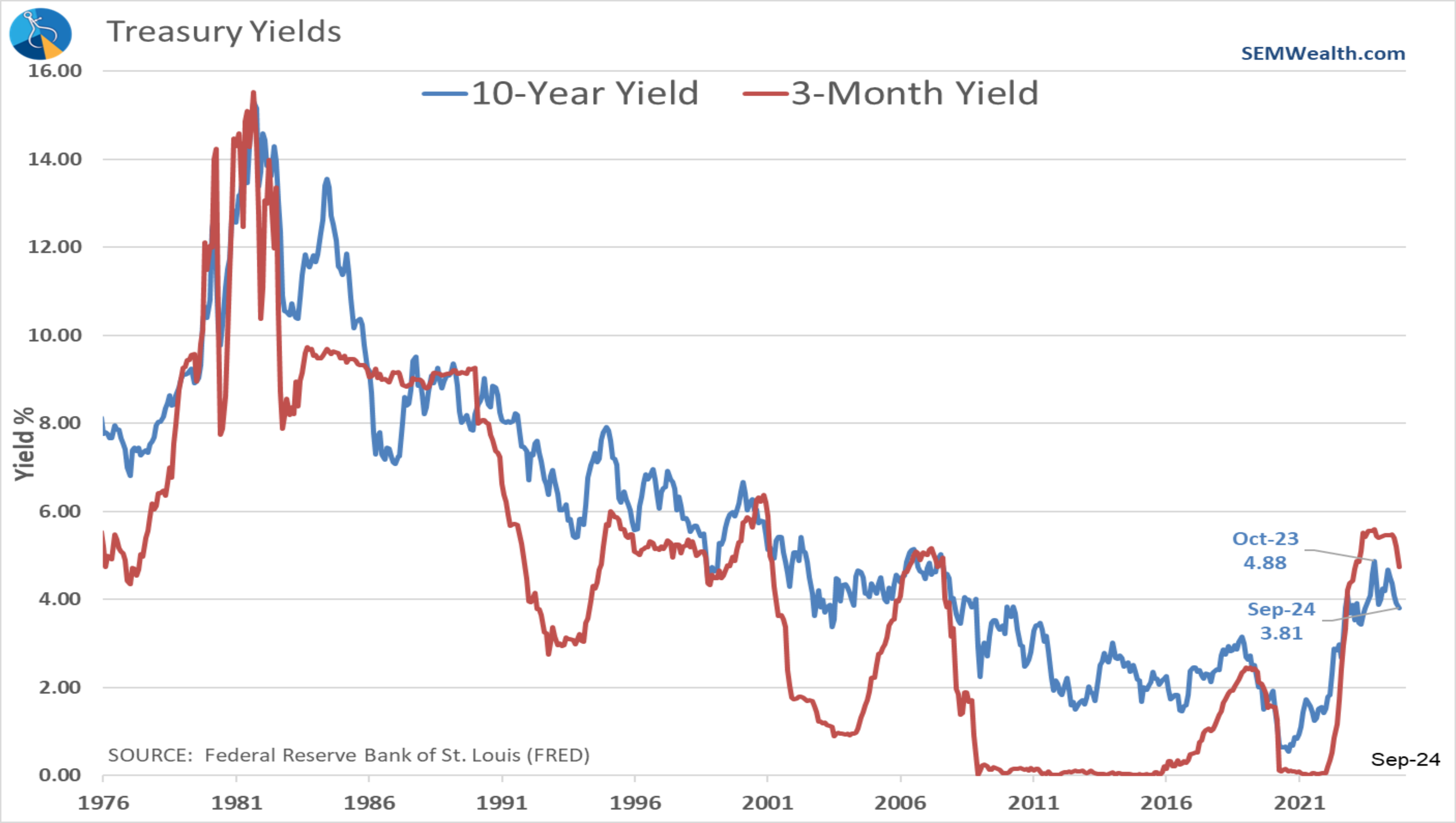
“Why are mortgage rates going up even though the Fed cut rates?”

-Steve F.

“It seems fishy the Fed would cut rates so much just before the election. Thoughts?”

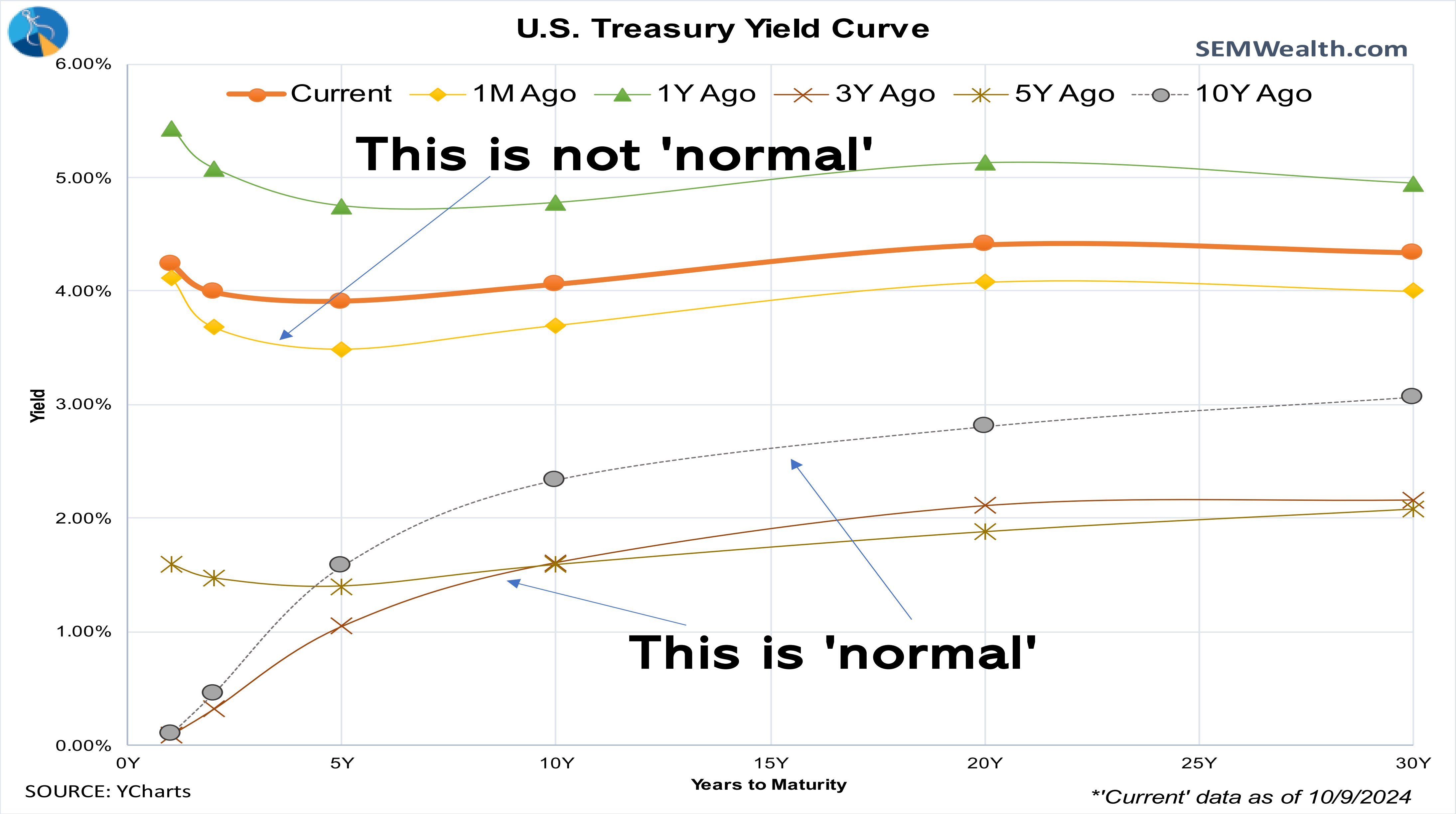
-Jonathan S.

Short & Long-Term Interest Rates



SOURCE: Federal Reserve Bank of St. Louis (FRED)

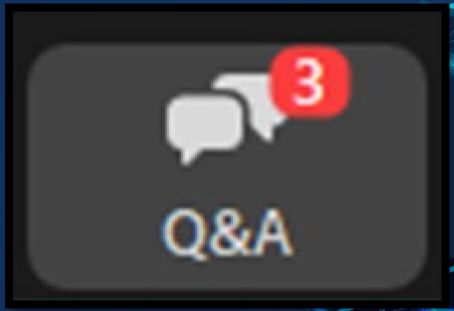
Short & Long-Term Interest Rates



SOURCE: YCharts

*'Current' data as of 10/9/2024

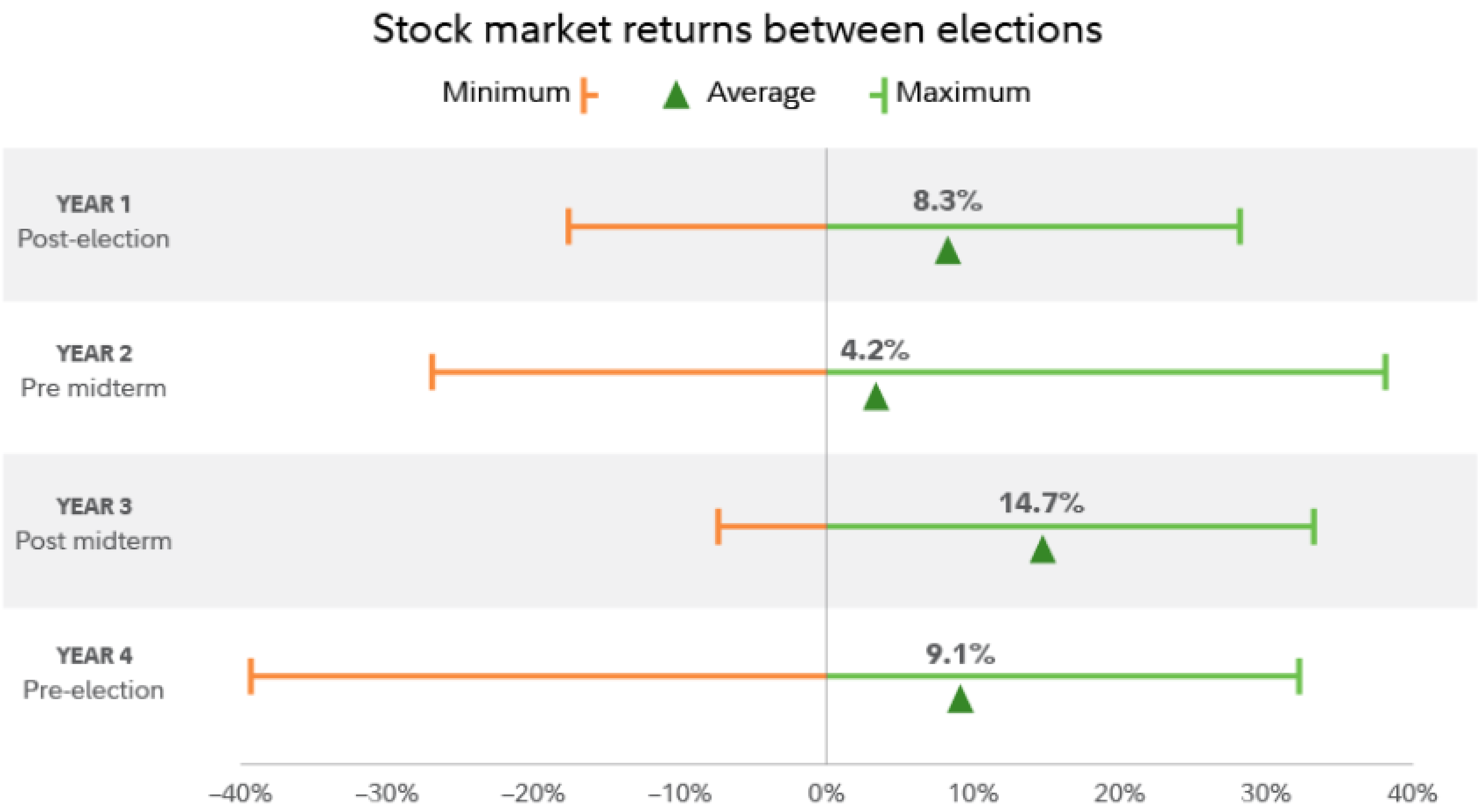
QUESTIONS?



“Would you expect the trend of strong post-presidential election years to continue? (2009, 2013, 2017, 2021)”

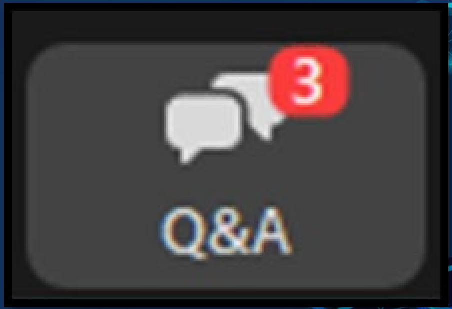
-Cody H.

Short & Long-Term Interest Rates



Past performance is no guarantee of future results. Data spans from November 30, 1950, to November 14, 2023. Years represent the 12-month period from November 30 to November 30 following a US presidential or midterm election. The chart depicts the average, minimum, and maximum price return achieved during this period. Stocks are represented by the S&P 500®. Indexes are unmanaged. It is not possible to invest in an index. Source: Haver, FactSet, FMR. As of November 14, 2023.

QUESTIONS?



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- Founded in 1992 by Richard Gage a metallurgical engineer
- Co-owner and Chief Investment Officer, Jeff Hybiak, CFA joined in 1998
  - Background in accounting and traditional portfolio management (MPT)
- Outsourced Chief Investment Officer (OCIO) for Financial Planners throughout the country (~2700 accounts)
- Total AUM = $850M as of 9/30/2024
- Primary Custodian is Axos Advisor Services
  - Select models also available on
    - Adhesion/FlexUMA
    - Axiom (Geneos Wealth Management)
    - Via subscription services
- Systematic, data-driven process designed to remove behavioral biases from all areas of the investment process
- 3 Distinct Management Styles – Tactical, Dynamic, and Strategic

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