Tarheel Advisors Newsletter

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2018 Predictions

We'd like to wish a very happy New Year to all our valued clients. 2018 is special for us as it is our 10th year in business, and without our clients we'd look silly writing these newsletters every quarter.

Year in Review—The success of our 2017 predictions is a bit mixed, but we were spot on where it mattered. Our core prediction was for the market momentum that started with the Trump election to continue for the entirety of 2017. Returns for the year were stellar for equities of all types, and the manner that they were achieved was quite interesting as well. Despite the volatility that is perceived by many in politics, the markets had one of their least volatile years on record without recording a single negative monthly return.

We also predicted the Federal Reserve would increase rates twice during 2017, and we weren't far off. Rates changed three times for a total increase of 0.75% for the year. We also predicted that these increases would cause the dollar to appreciate, however, we got that trend incorrect as the dollar depreciated around 10% against many major currencies during 2017.

Our biggest miss for the year was a prediction that we'd see the first major overhaul in Social Security since the Reagan years. While we did manage to close out the year with a historic tax reform bill, Congress was especially careful to not touch anything Social Security related. This proves that the topic is so cancerous in the political realm that we will most likely not see a voluntary overhaul to the system for decades to come.

2017 Score Card

Return to 3% GDP Growth	A
Market Returns of 15%	A
Two Interest Rate Changes	B
Social Security Ovehaul	F
Dollar Appreciates	D

2018 Predictions—The big question for market prognosticators is how much gas is left in the tank of this nearly decade long bull market? The answer to this question is predicated on a debate that has raged in economic and political circles for nearly 40 years. The Reagan administration coined the term of "trickle down economics" based on the idea that individuals are better stewards of their money than the government, and if given a lower taxation rate we will see stronger economic expansion for all.

If trickle down economics works, then our current bull market may have been refueled with enough gas to go another 2-3 years. 2013 was the last time we saw a 20+% increase in equity prices, and the following year we saw another increase of 10%. For 2018 we're looking for a similar story with expectations of low double digit returns for US stocks. However, it's unlikely we go a second straight year with ultra low volatility, so it would be reasonable to expect a 5-10% correction sometime during the year.

For a second straight year, our baseline expectation is for two more Fed interest rates hikes for an annual increase of 0.5%. The reason for these increases will be continued domestic economic expansion and GDP growth of between 3-3.5% for 2018. The wild card may be the new leadership beginning in February when current Chairmen Yellen steps down and is replaced by Trump nominee, Jerome Powell. Mr. Powell according to most pundits is expected to maintain a similar style of operation and interest rate trajectory to his predecessor, but we really don't have any historical data to base that on.

Finally, it wouldn't be fun unless we made an outlandish prediction on the value of Bitcoin. We've seen others make predictions from $0 all the way up to $1 million. About 0.1% of the world population has a meaningful holding in Bitcoin, but the way it has been covered in 2017 you'd think that number was 25% or higher.

While we are not bearish on the future of the block chain technology that Bitcoin was built on, we are

2017 Market Wrap

S&P 500	**+21.83%**
DOW	**+28.11%**
RUSS 2000	**+14.65%**
MSCI World	**+24.21%**
BONDS	**+3.54%**
GOLD	**+11.3%**

Mortgage Rates

15-Year	**3.25%**
30-Year	**3.90%**
5/1 ARM	**3.79%**

Did You Know?

* GE was the worst market performer in the DOW last year losing 42%.

* Boeing was the best performer in the DOW last year gaining 93%.

* Less than 10% of the world's money is physically held. It turns out the Dollar (and other currencies) went cyber long before Bitcoin was ever thought of.

* The 401(k) contribution limit has been raised slightly for 2018, up to $18,500. Those over 50 can continue to make a catch-up contribution of an additional $6,000.

2018 Predictions (Continued)

less bullish on the forward case of Bitcoin and other non-governmental issued cyber currencies. Followers of Bitcoin may remember the collapse of one of their major exchanges in 2014, Mt. Gox. Our 2018 outlook for Bitcoin is negative, and we are expecting to see another major exchange failure commensurate with what was seen in 2014. If any newly minted Bitcoin millionaires are out there reading this, don't quit your day job just yet.

-Ryan Glover, CFP®

Byrd is the Word

INDIVIDUAL TAXES					
Current Law (2017)			"The Act" (Expire in 2026)		
	Single	Married/Joint		Single	Married/Joint
10%	$0-$9,525	$0-$18,650	10%	$0-$9,525	$0-$19,050
15%	$9,525- $38,700	$18,650-$75,900	12%	$9,525-$38,700	$19,050-$77,400
25%	$38,700-$93,700	$75,900-$153,100	22%	$38,700-$82,500	$77,400-$165,000
28%	$93,700-$195,450	$153,100-$233,350	24%	$82,500-$157,500	$165,000-$315,000
33%	$195,450- $424,950	$233,350-$416,700	32%	$157,500-$200,000	$315,000-$400,000
35%	$424,950- $426,700	$416,700-$470,700	35%	$200,000-$500,000	$400,000-$600,000
39.6 %	$426,700 and over	$470,700 and over	37%	$500,000+	$600,000+

As many of you probably know, the House and Senate approved the final version of the tax reform legislation in the last week of 2017, and President Trump signed into law the Tax Cut & Jobs Act ("The Act"). This new legislation will have a profound impact on many aspects of the tax system in the United States and is likely to impact both individuals and businesses significantly over the next decade. Due to procedural nuances of how the bill was passed as part of a budget resolution (known as the Byrd Rule), the new tax provisions expire in 10 years concurrent with the budget window.

Although this new law was touted as a major tax cut, we think it is better labeled as a tax reform. The Act eliminates or modifies a number of well-known business and individual deductions, credits, and incentives. Depending on where you fall in the various brackets and whether you itemize will make a big difference on whether you can expect a beneficial move in your future tax bill.

Corporations appear to be the big winners. With a rate drop from 35% to 21%, Many C corporations will see a decrease in their impending tax liabilities. To put small business owners on a similar playing field, The Act provides a deduction for 20% of qualified business income. However, the rules for this deduction are complicated and many will receive a smaller than expected benefit.

On the individual side, the biggest changes are in the modified marginal tax brackets and the increased standard deduction. I've pasted a comparison of the 2017 and 2018 table above, and as you can probably tell, the new law kept the 7 different brackets, but modified the rates and thresholds. On top of the bracket changes, the standard deduction for both single and married filers has been doubled (12K for single and 24K for married filers). Given that nearly 70% of tax filers claim the standard deduction, this will undoubtedly help the masses, but may not be to your benefit if you have a lot of mortgage interest, charitable contributions, etc. that would put you above the threshold.

Some other notable provisions in the tax bill include:

- 529 contributions can now be used for K-12 education as well as post-graduate expenses
- The estate tax exemption is doubled to 11.2M per person (indexed for inflation).
- The Obamacare coverage penalty provision is eliminated as of 2019.
- Mortgage interest deduction is decreased to the first 750K of indebtedness versus 1MM.
- State, local, and property taxes are only deductible on your Federal tax return to the extent of $10K
- The child tax credit has been increased to $2K
- Qualified dividend and long-term capital gains rates remain unchanged.

-Walter Hinson, CFP®