A Lot of Opinions – Few Facts

SEMWealth.com
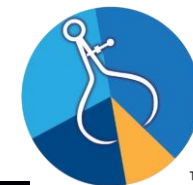
It's been a tough year

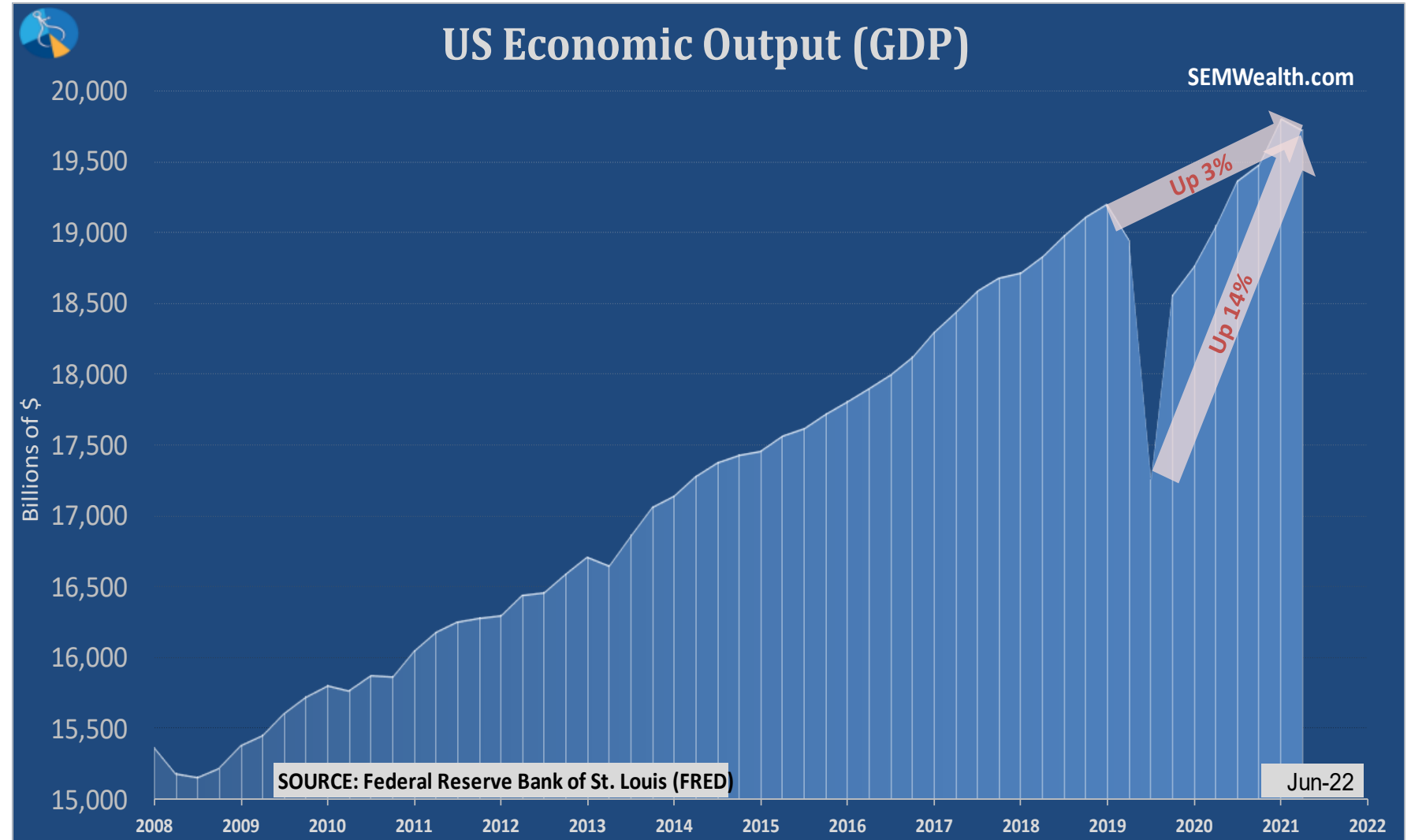SEMWealth.com

Getting back to "normal"

- Focus has been on recovering to 2019 levels.

- The depth of the losses & the strong recovery has disrupted "normal" functions.

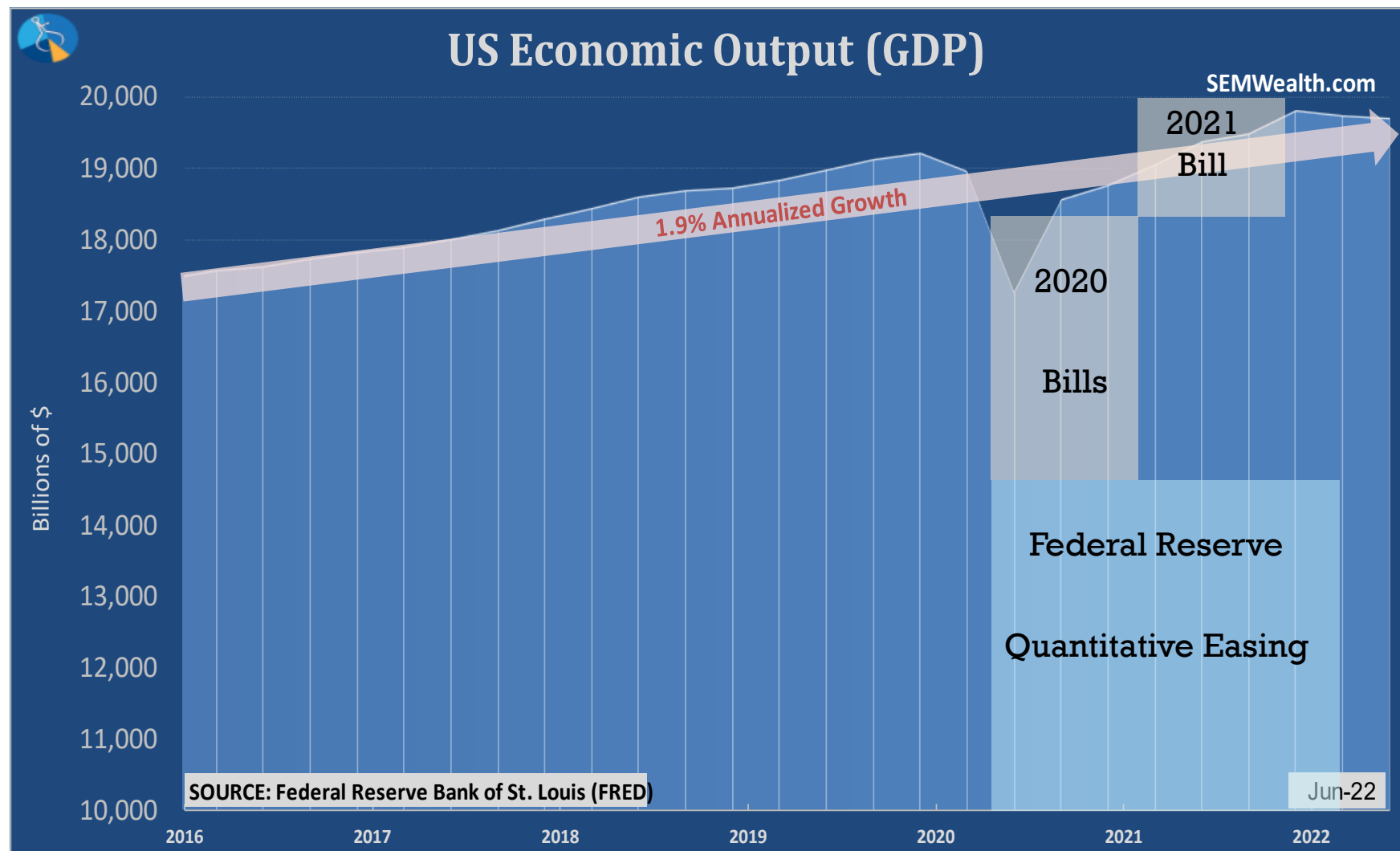- There are **structural** changes that happened during COVID which changes "normal"

US Economic Output (GDP)

SEMWealth.com

Up 3%

Up 14%

Billions of $

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

Jun-22

What is "normal?"

- 2020 Stimulus Bills = $3.5 Trillion

- 2021 Stimulus Bill = $1.9 Trillion

- Total Stimulus from Congress = $5.4 Trillion

- Fed has created an additional $5.2 Trillion

- Total Stimulus has been 50% of GDP output

US Economic Output (GDP)

SEMWealth.com

1.9% Annualized Growth

2021 Bill

2020 Bills

Federal Reserve

Quantitative Easing

Billions of $

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

Jun-22

20,000
19,000
18,000
17,000
16,000
15,000
14,000
13,000
12,000
11,000
10,000

2016   2017   2018   2019   2020   2021   2022

SEMWealth.com

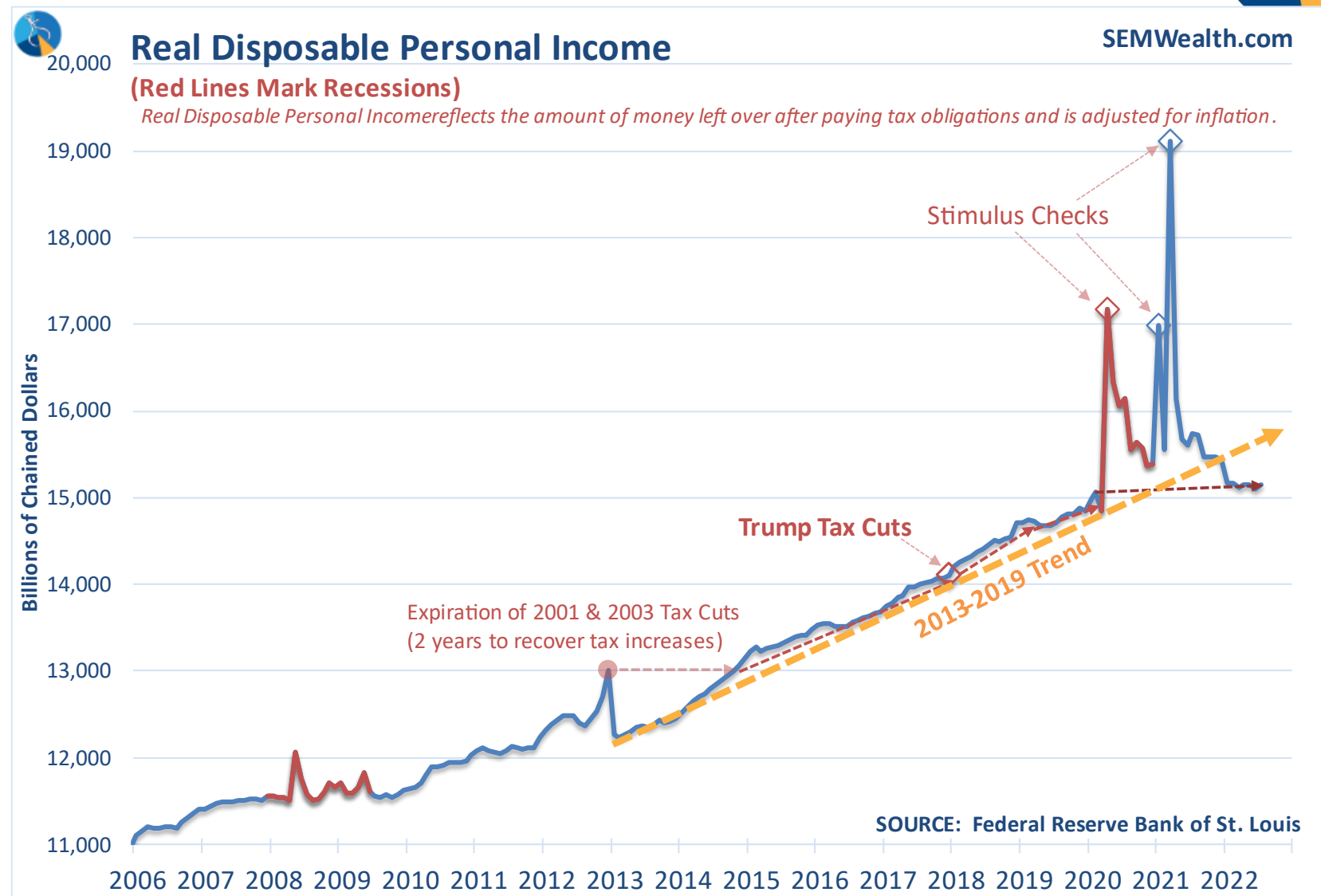# The impact of $5.4 Trillion+

- Consumer spending had slowed in 2019 as tax cuts wore off

- Current levels have **exceeded** the pre-COVID trend significantly

Consumer Spending

(Red Lines Mark Recessions) Dashed line is long-term trend

SEMWealth.com

Trump Tax Cuts

Stimulus Checks

Expiration of 2001 & 2003 Tax Cuts

SOURCE: Federal Reserve Bank of St. Louis

Jul-22

Billions of $

18,000
17,000
16,000
15,000
14,000
13,000
12,000
11,000
10,000
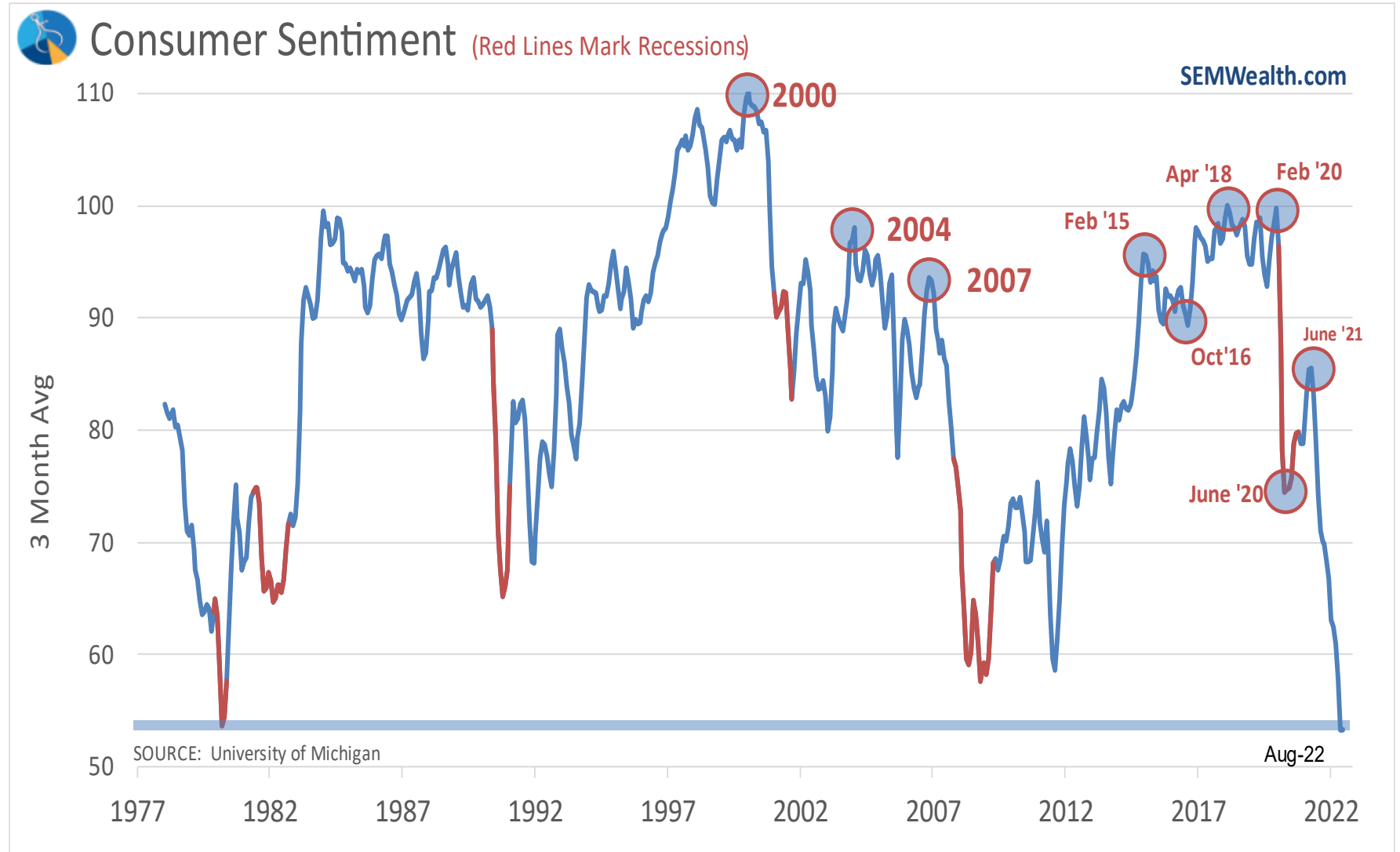9,000
8,000

2005   2010   2015   2020
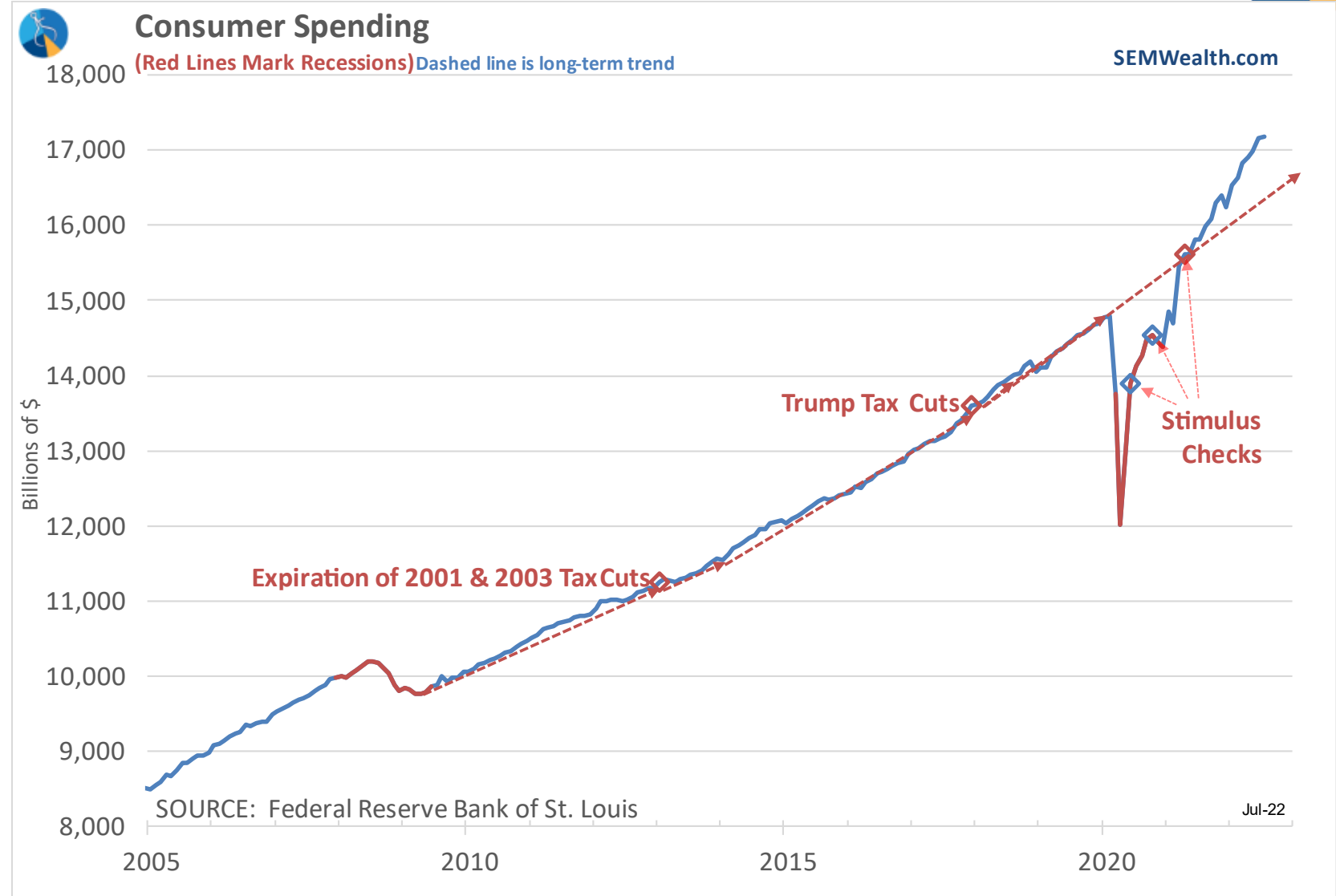
The impact of $5.4 Trillion+

- Income growth had slowed significantly prior to COVID

- Current income growth is now **running below** the 2013-2019 trend

Real Disposable Personal Income

(Red Lines Mark Recessions)
Real Disposable Personal Income reflects the amount of money left over after paying tax obligations and is adjusted for inflation.

SEMWealth.com

Stimulus Checks

Trump Tax Cuts

2013-2019 Trend

Expiration of 2001 & 2003 Tax Cuts
(2 years to recover tax increases)

SOURCE: Federal Reserve Bank of St. Louis

Billions of Chained Dollars

20,000
19,000
18,000
17,000
16,000
15,000
14,000
13,000
12,000
11,000

2006 2007 2008 2009 2010 2011 2012 2013 2014 2015 2016 2017 2018 2019 2020 2021 2022

SEMWealth.com
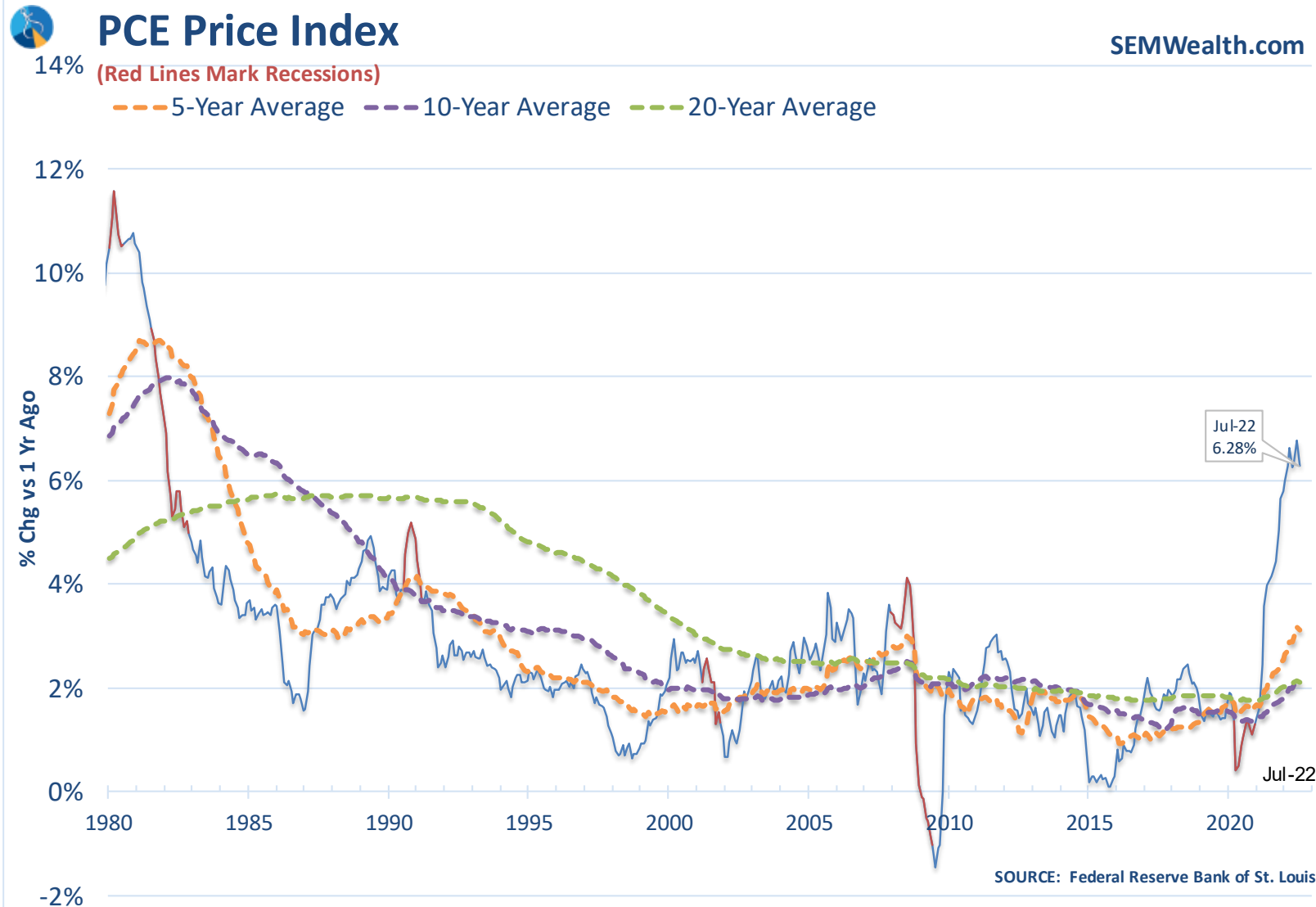
The impact of $5.4 Trillion+

- Consumer Sentiment had hit its highest level since 2004 just before COVID

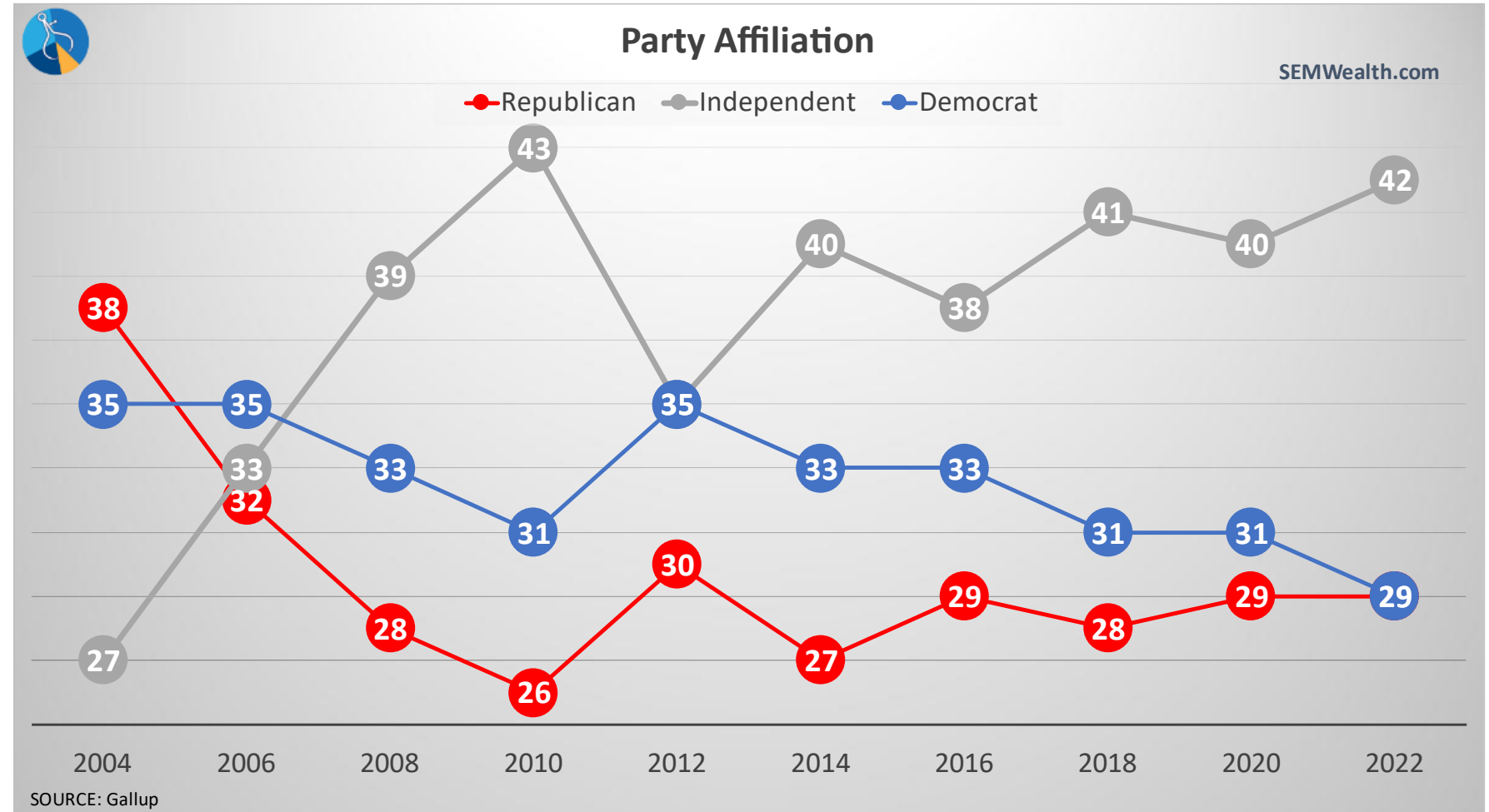- Sentiment has plummeted this summer despite most of the economy being reopened

Consumer Sentiment (Red Lines Mark Recessions)

SEMWealth.com

2000

Feb '15

Apr '18   Feb '20

Oct'16

June '21

June '20

2004

2007

3 Month Avg

110
100
90
80
70
60
50

SOURCE: University of Michigan

Aug-22

1977   1982   1987   1992   1997   2002   2007   2012   2017   2022

SEMWealth.com

What about inflation?

PCE Price Index

SEMWealth.com

(Red Lines Mark Recessions)

- - - 5-Year Average   - - - 10-Year Average   - - - 20-Year Average

% Chg vs 1 Yr Ago

Jul-22
6.28%

Jul-22

SOURCE: Federal Reserve Bank of St. Louis

(Y-axis labels: -2%, 0%, 2%, 4%, 6%, 8%, 10%, 12%, 14%)
(X-axis labels: 1980, 1985, 1990, 1995, 2000, 2005, 2010, 2015, 2020)

- Deficits are deflationary

- Too many retirees are deflationary

- Excess saving is deflationary

- Increased productivity is deflationary

- Inventory surpluses are deflationary
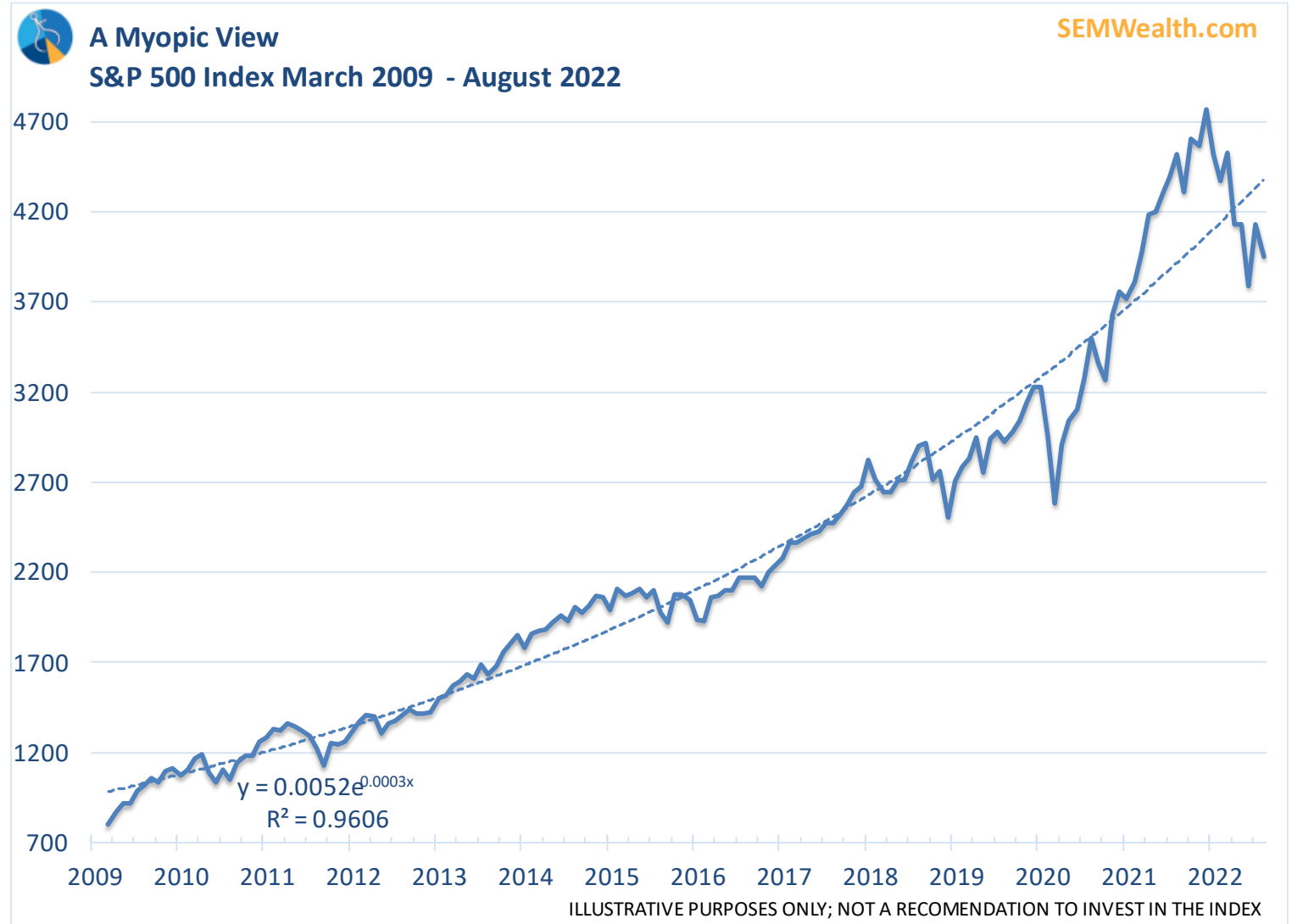
- Inflation is deflationary

SEMWealth.com

Politics will play a key role

- There was not a mandate for progressive politics

- Independents control the vote – they want progress

- Younger generations are least likely to be affiliated with a party

Party Affiliation

SEMWealth.com

●—Republican ●—Independent ●—Democrat

Republican: 38 (2004), 32 (2006), 28 (2008), 26 (2010), 30 (2012), 27 (2014), 29 (2016), 28 (2018), 29 (2020)

Independent: 27 (2004), 33 (2006), 39 (2008), 43 (2010), 40 (2014), 38 (2016), 41 (2018), 40 (2020), 42 (2022)

Democrat: 35 (2004), 35 (2006), 33 (2008), 31 (2010), 35 (2012), 33 (2014), 33 (2016), 31 (2018), 31 (2020), 29 (2022)

2004 2006 2008 2010 2012 2014 2016 2018 2020 2022

SOURCE: Gallup

Short-term Outlook

During bull markets, investors are conditioned to believe all dips are to be bought and fail to adapt to new information that could cause the bull market to end. The longer the bull market, the more likely they are to believe they will be able to see it coming and reduce their exposure to risky assets.
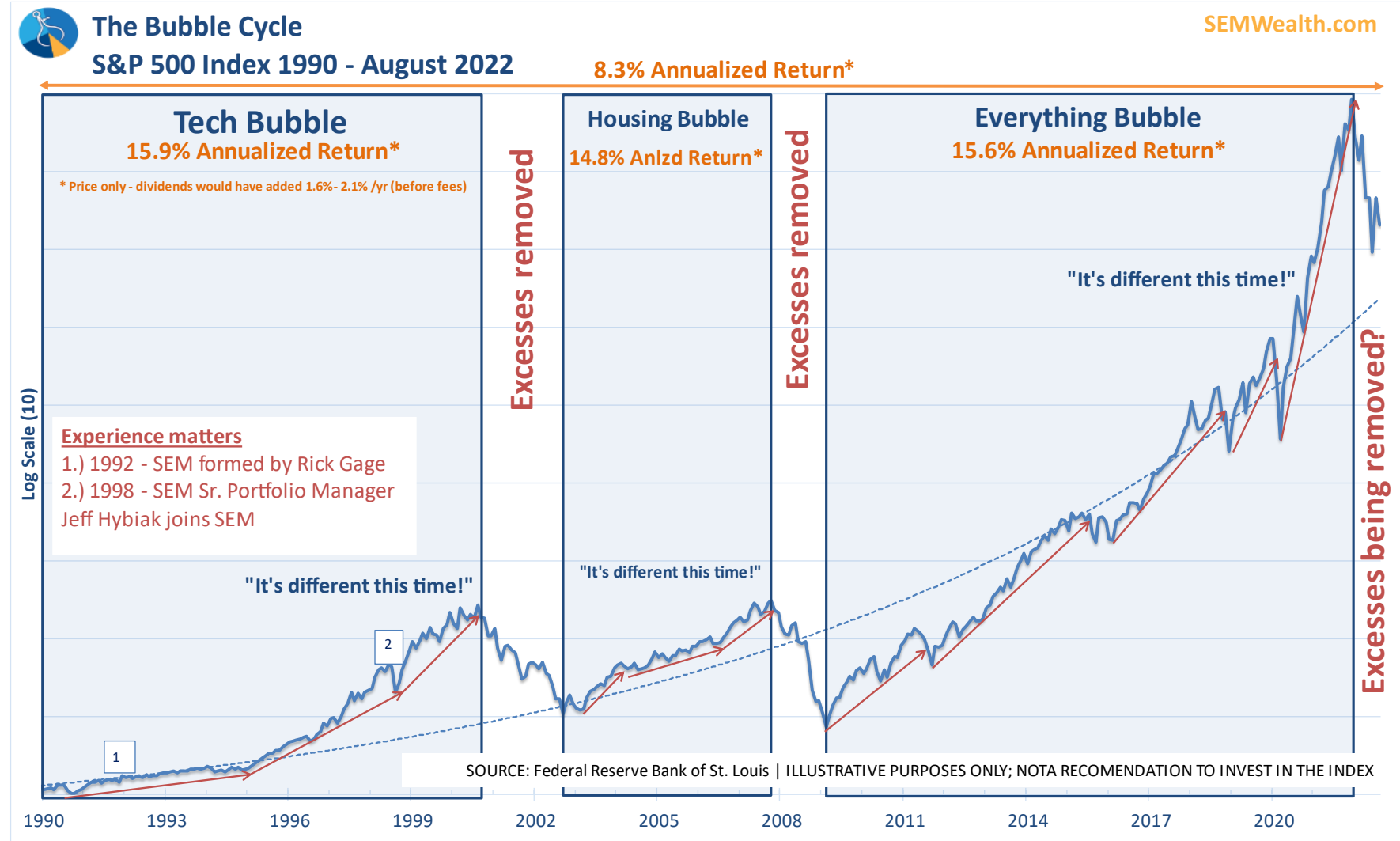

A Myopic View
S&P 500 Index March 2009 - August 2022

$y = 0.0052e^{0.0003x}$
$R^2 = 0.9606$

ILLUSTRATIVE PURPOSES ONLY; NOT A RECOMENDATION TO INVEST IN THE INDEX

SEMWealth.com

SEMWealth.com

Long-Term Outlook

Investors often look at the past bear markets and with hindsight believe they could have been avoided. 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 - August 2022

SEMWealth.com

8.3% Annualized Return*

Tech Bubble
15.9% Annualized Return*
* Price only - dividends would have added 1.6%- 2.1% /yr (before fees)

Housing Bubble
14.8% Anlzd Return*

Everything Bubble
15.6% Annualized Return*

Excesses removed

Excesses removed

Excesses being removed?

"It's different this time!"

Log Scale (10)

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

"It's different this time!"

"It's different this time!"

1

2

SOURCE: Federal Reserve Bank of St. Louis | ILLUSTRATIVE PURPOSES ONLY; NOTA RECOMENDATION TO INVEST IN THE INDEX

1990   1993   1996   1999   2002   2005   2008   2011   2014   2017   2020

SEMWealth.com

Valuations are still historically high

- Starting valuation levels are the number one determinant of long-term returns.

- High P/Es can be justified if interest rates are low and/or growth rates are high.

S&P 500 PE Ratio

Interest rates generally declined since the early 1980s, which supported rising P/E ratios.

SEMWealth.com
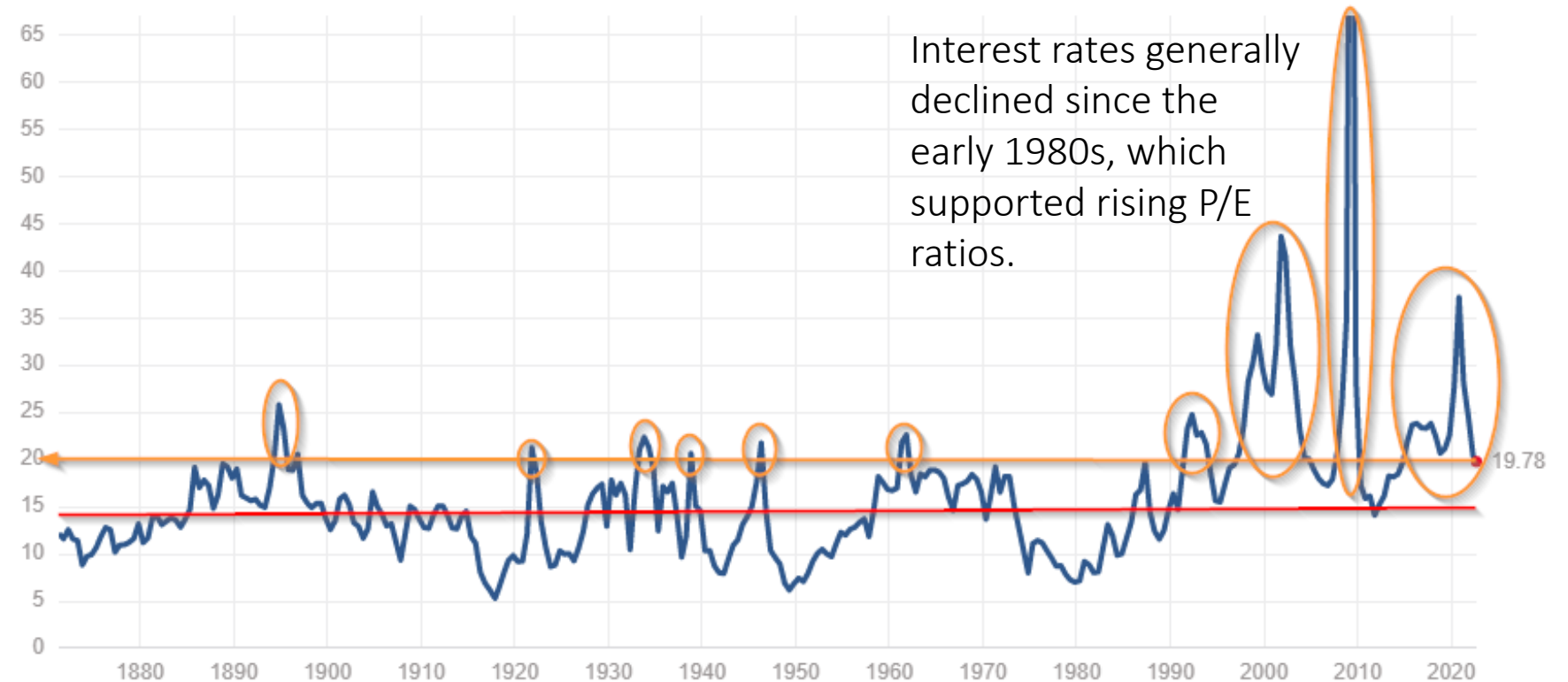
An "Unprecedented" Environment is a Real Possibility

- Since 1984, interest rates have generally been declining. This has given bonds an underlying uptrend to help support traditional stock/bond portfolios.

- The downtrend has been broken; if the Fed loses control of inflation, we could see a spike similar to the late 70s/early 80s

10-Year Treasury Yield

SEMWealth.com

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

Aug-22

We're used to the Fed saving stocks

"The Fed Put"

- -15.4%
- -17.5%
- -12.2%
- -10.3%
- -17.5%
- -31.3%

$SPX S&P 500 Large Cap Index INDX   @StockCharts.com
30-Sep-2020   **Open** 3333.90 **High** 3393.56 **Low** 3327.54 **Close** 3363.00 **Volume** 6.8B **Chg** +64.54 (+1.96%) ▲
— $SPX (Weekly) 3363.00 (2 Oct)

Since 2009 every correction has been met
with a shift in Fed policy.

Fed hikes rate 150 bp in 2018 / Announces
pause in Dec / starts cutting rates Aug 2019

-10.2%

-17.6%

-31.3%

Fed cuts rates to 0%
/ buys bond ETFs /
launches QE4

QE3 (Sep '12 - Oct'14)

-12.3%

Fed hints at rate hikes (June)
/ hikes rates once (Jan) and
then pauses

-17.6%

Debt ceiling circus (May-August)
/ Operation Twist Begins (Sept.)

-15.5%

QE1 Ended in March '10 / QE2 hinted
in August, runs Nov '10 - Jun '12

Bear Markets Include Strong Rallies

"The worst is over"

- 12.2%
- 7.7%
- 19.2%
- 21.6%
- 21.0%

$SPX S&P 500 Large Cap Index INDX
31-Dec-2002

Open 879.39 High 881.93 Low 869.45 Close 879.82 Volume 1.3B Chg +0.43 (+0.05%)

@StockCharts.com

2000 - 2002 Bear Market

Note: The Federal Reserve cut interest rates by a total of 6% from June 2000 through November 2002

12.2%
7.7%
19.2%
-49.0%
21.6%
21.0%
879.82

Bear Markets Include Strong Rallies

"The worst is over"

- 11.4%

- 8.0%

- 12.2%

- 7.4%

- 11.4%

- 24.3%

- 8.7%

$SPX S&P 500 Large Cap Index INDX
30-Jun-2009
Open 927.15 High 930.01 Low 912.86 Close 919.32 Volume 4.2B Chg -7.91 (-0.85%)
@StockCharts.com
— $SPX (Daily) 919.32 (30 Jun)

2008-2009 Bear Market

11.4%
8.0%
12.2%
7.4%
-56.7%
11.4%
24.3% 8.7%

Note: The Federal Reserve cut interest rates a total of 5.25% (down to 0%) from July 2007 through December 2008

919.32

2007 Feb Mar Apr May Jun Jul Aug Sep Oct Nov Dec 2008 Feb Mar Apr May Jun Jul Aug Sep Oct Nov Dec 2009 Feb Mar Apr May Jun

High Valuations – Low Future Returns

Forward 10-Year Return Expectations (Annualized)

MORNINGSTAR
- US Stocks: +1.6%
- US Bonds: +1.6%

60/40 Portfolio: +1.6%

(as of 12/31/2021)

Vanguard®
- US Stocks: +5.1%
- US Bonds: +3.6%

60/40 Portfolio: +4.5%

(as of 8/31/22)

BlackRock®
- US Stocks: +7.1%
- US Bonds: +3.0%

60/40 Portfolio: +5.5%

(as of 8/31/22)

Long-term Annualized Returns (1926-2020)
- US Stocks: +10.2%
- US Bonds: +5.5%

60/40 Portfolio: +8.3%

SOURCE: Ibbotson / CFA Institute

SEMWealth.com

Understanding Investor Behavior

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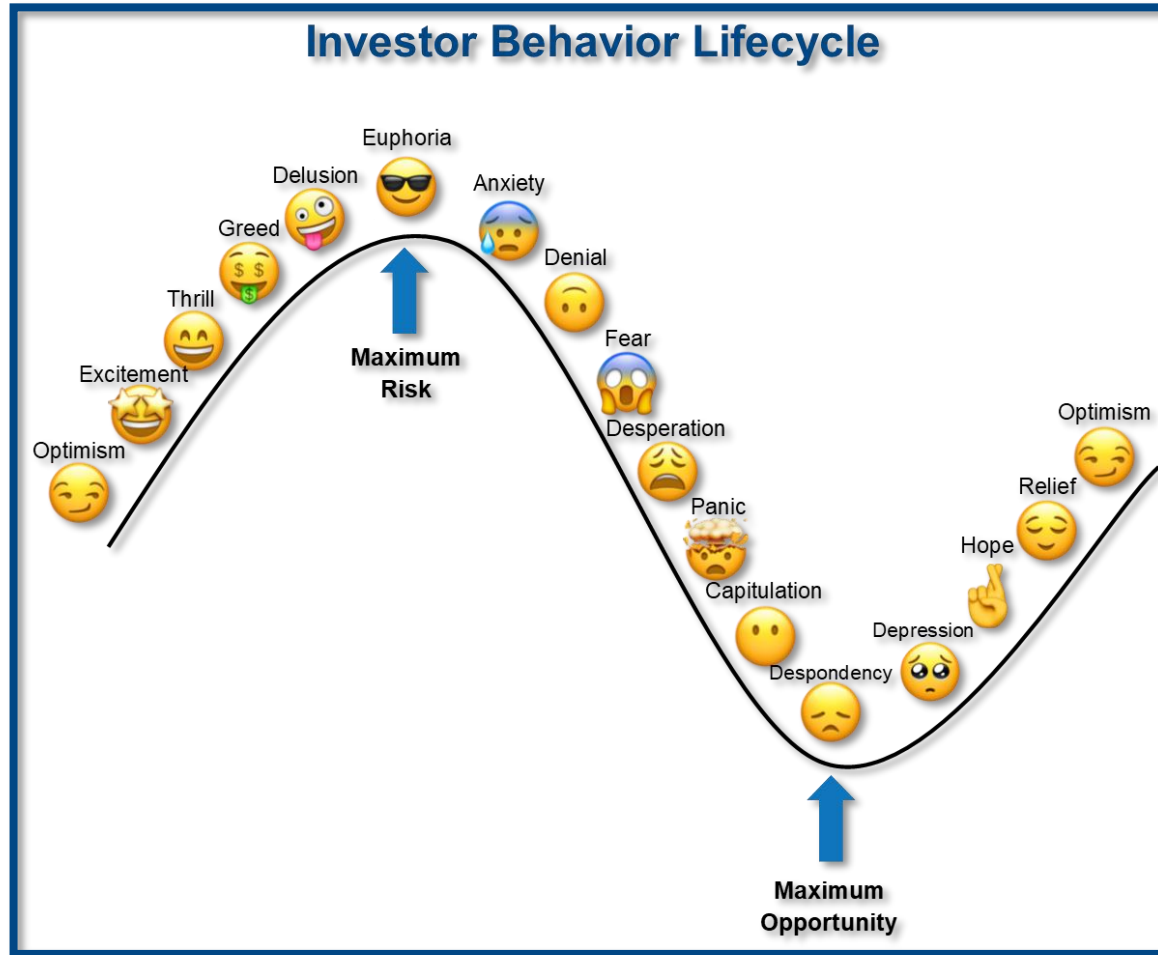
The stock market is a story of **cycles** & of the **human behavior** that is responsible for **overreactions** in both directions.

– Seth Klarman

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

SEMWealth.com

Combining diversified models
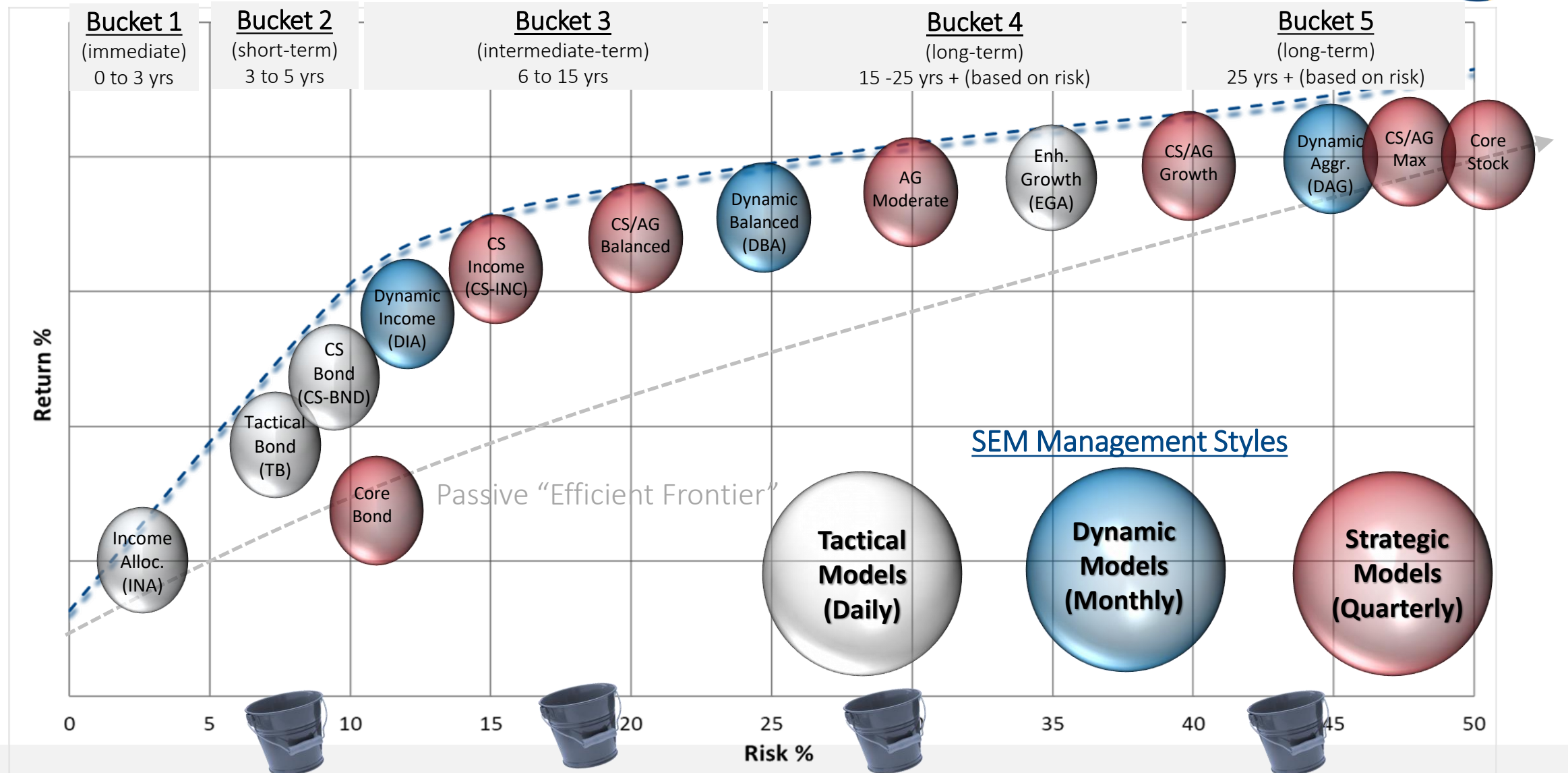
Tactical Models

- <u>Tactical Management</u>: Tactical programs are monitored DAILY.
  Tactical programs study the <u>trends in the market</u> with a primary
  <u>focus on moving to lower risk asset classes</u> when risks are high.
  Due to their focus on risk management, tactical programs <u>will not</u>
  <u>participate as much in rising markets</u>.

Tactical Trading System Example

Tactical trading systems use only data generated from the market --- price, volume, advancing versus declining issues, open price vs closing price, etc.

SEM tests a wide range of indicators back through time to develop rules of when to buy and sell various index funds.

Each system will generate an indication on intermediate-term market direction (1-6 months).

Since each system will have periods of time where it is out of favor, SEM utilizes 4-12 different trading systems in each investment model.

Source: S&P Dow Jones Indices

Index Price

Market-based price indicator such as up-down volume

Be Aggressive!

Be Careful!

Sit it Out!

Many of SEM's systems will generate conflicting signals so you do not often see a model move from fully invested to all the way out of the market in one or two days.

SEMWealth.com
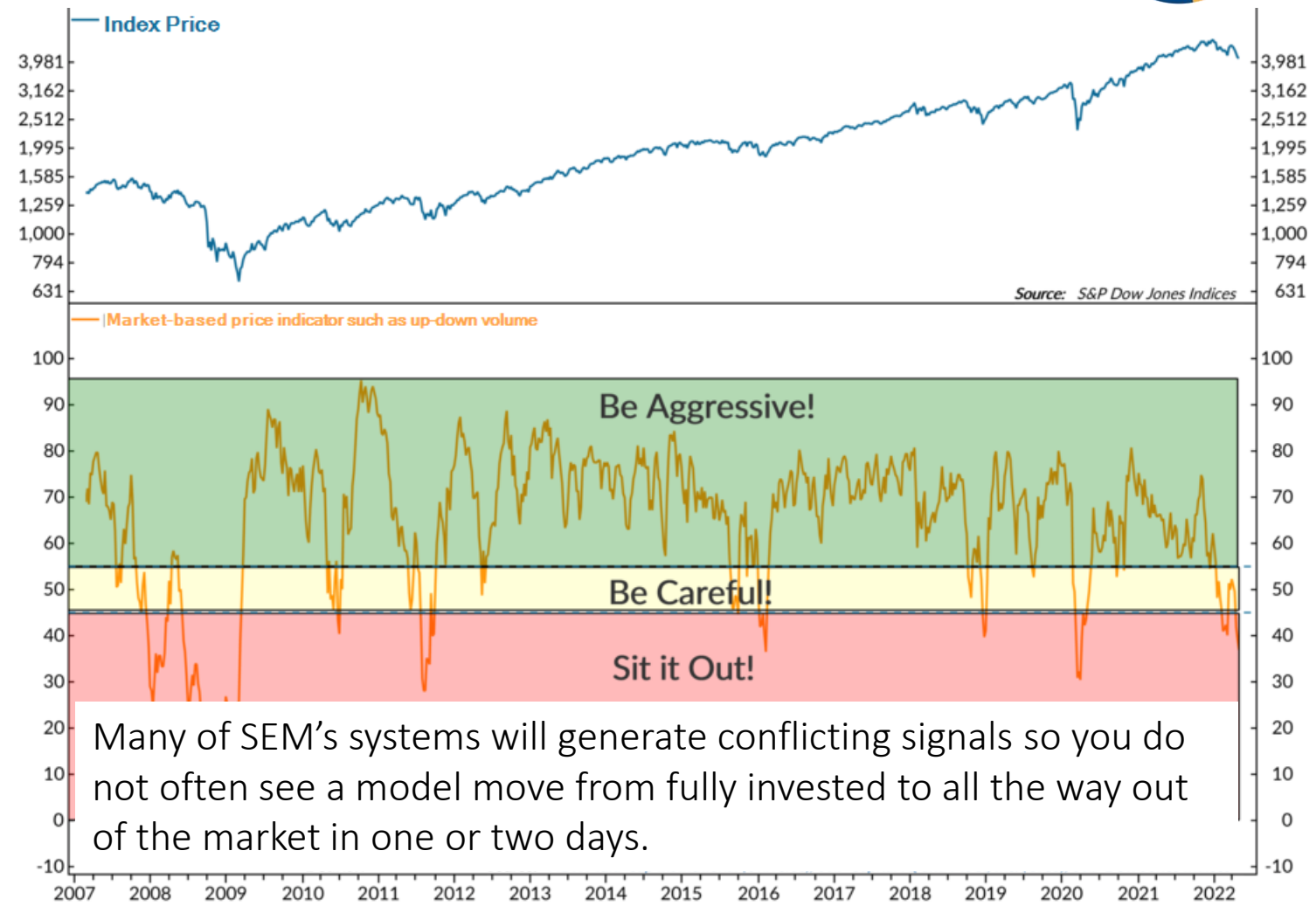
Tactical Bond (TB) / Cornerstone-Bond (CS-BND)

SEM's High Yield Bond trend following system has a real-time track record going back to 1992. This system has 3-5 different variations based on the market trends.

The chart to the right illustrates what Tactical Management is all about – follow a market index and invest in the index during rising trends & move to cash or other low-risk assets during falling trends.

The chart also shows the downside of Tactical Management – there will be many "bad" trades, but with proper discipline those are offset by the large winning trades that either generate strong returns or eliminate large losses.

SEM WEALTH MANAGEMENT
High Yield Bond Trading System: Capitalizing on Market Trends

—High Yield Bond Composite: 2007 - Sept 2022*

△ Buy Signals

● Sell Signals

Value

Indicates the actual BUY/SELL dates of a High Yield trading system. This chart was not used by SEM to generate buy or sell decisions. It should not be assumed that recommendations made in the future will be profitable or will equal the performance presented above. Please see our disclosure document for more information.

2007 2008 2009 2010 2011 2012 2013 2014 2015 2016 2017 2018 2019 2020 2021 2022

Tactical High Yield Bond System

The premise of Tactical Bond is simple:
-own high yield bonds when they are trending higher
-sell and move to lower risk investments when they are trending lower

While SEM's signals are proprietary, this chart illustrates the _concept_.
-The blue line is the signal
-Buy/Sell when the black/red line crosses the signal line

Open 7.80 High 7.80 Low 7.80 Close 7.80 Chg -0.10 (-1.27%)

© StockCharts.com
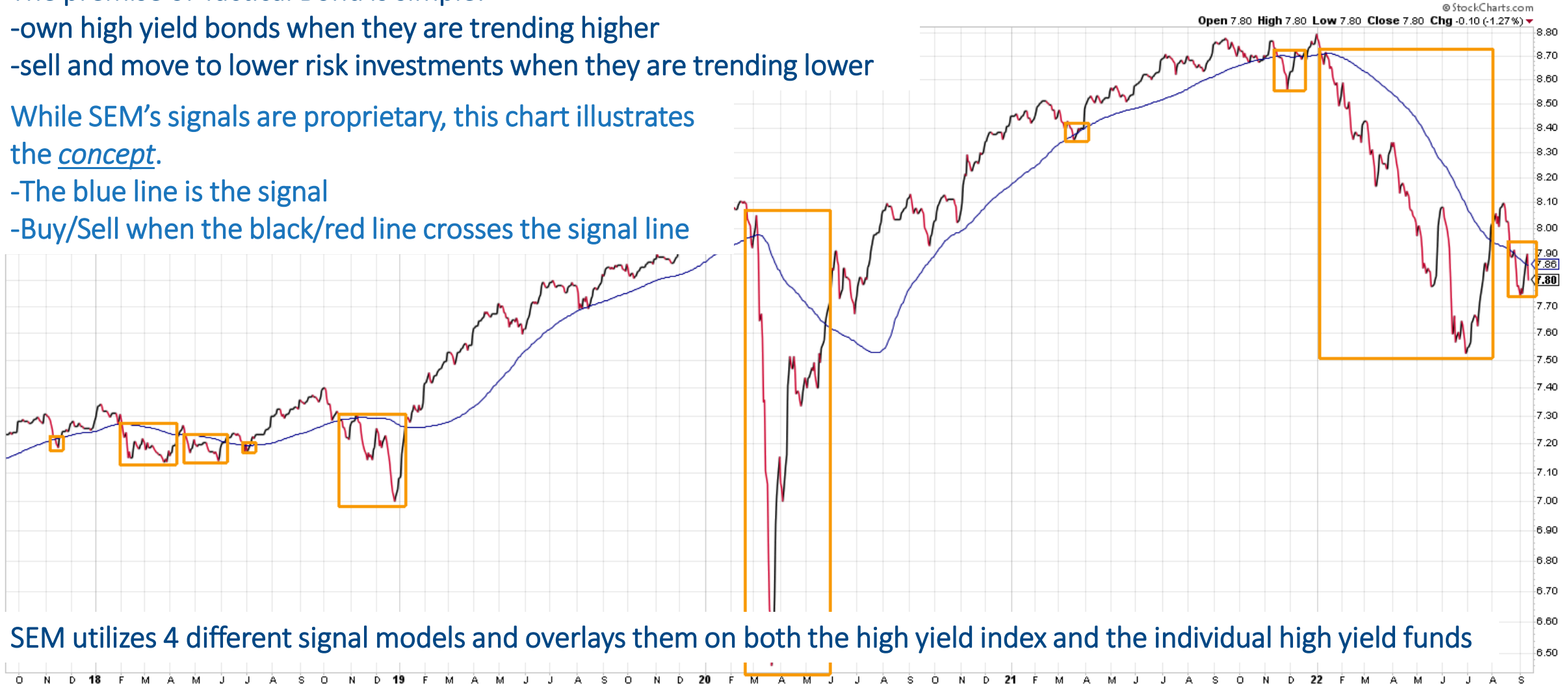
SEM utilizes 4 different signal models and overlays them on both the high yield index and the individual high yield funds

SEMWealth.com

Tactical Aggregate Bond System

Tactical trading of more efficient markets is more difficult, but the goal is the same:
-own/overweight bonds when they are trending higher
-sell/underweight bonds when they are trending lower

The goal of a tactical system is to participate in the bulk of the upside while missing the bulk of the downside. The downside is there will be false signals.

One alternative idea is to implement 50% of buy/sell signals across each moving average
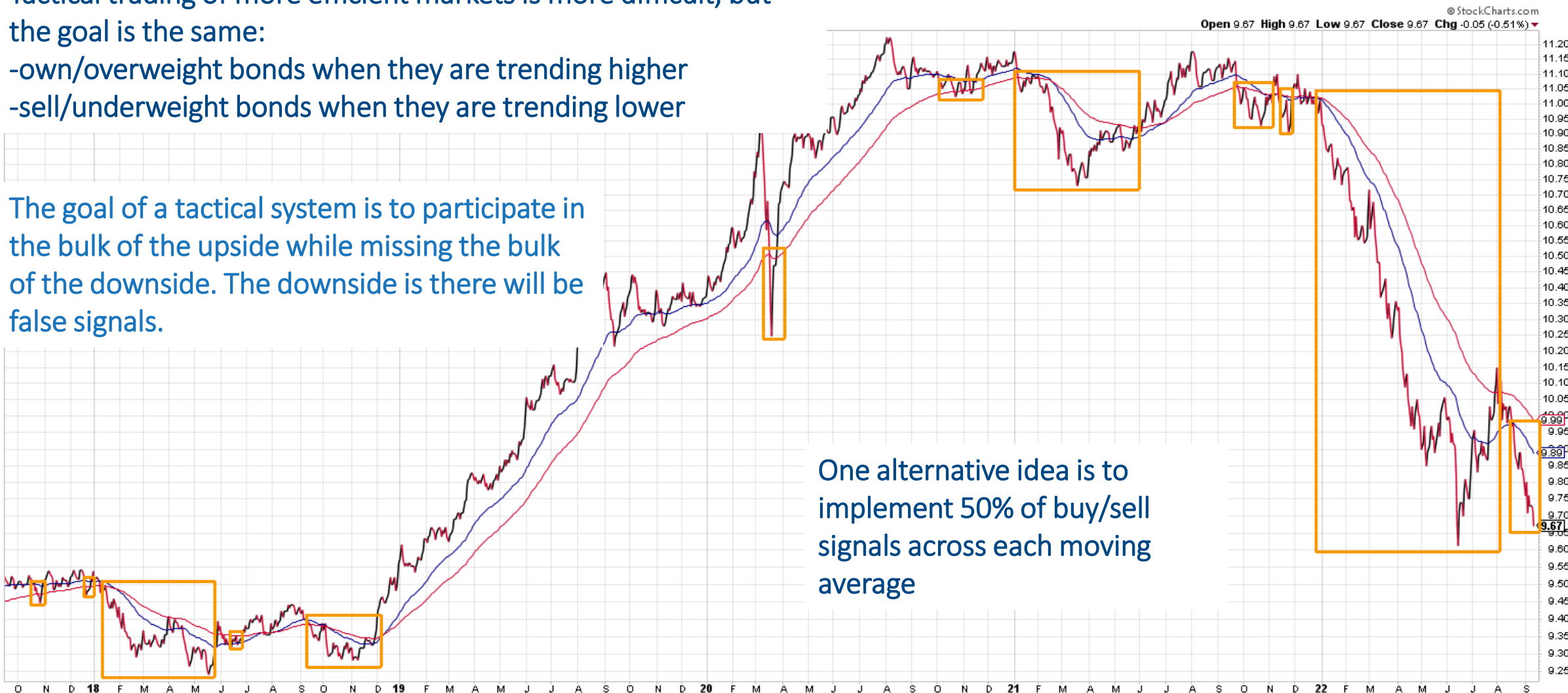
Tactical Stock Market System

Tactical trading of stocks is quite difficult; At best, most tactical stock market systems will help to avoid riding the market all the way down, which psychologically could help.

A moving average cross-over system tends to work better on broad stock markets, however most of the time these systems will miss the bottom, so multiple trading systems are recommended if attempting this.

Takeaway: These systems are better at identifying severe declines, but not at identifying the bottom.

Open 96.27 High 96.27 Low 96.27 Close 96.27 Chg -4.28 (-4.26%)

©StockCharts.com

SEMWealth.com

Dynamic Models

Dynamic Models: Adjusting to the economy

Leading Economic Indicator:	36 Month Trend:	GDP Indication:
Building Permits		↔
Consumer Confidence		↓
Consumer Goods Orders		↔
Business Activity		↔
Hours Worked		↑
Jobs		↑
Money Supply		↓
Stock Prices		↓
Vendor Performance		↑
Yield Curve		↓

Market Vs Economy Cycles And Sector Rotation

Finance / Technology / Cyclicals

Technology / Industrials / Basic Materials

Basic Materials / Energy / Staples

Energy / Staples / Healthcare

Healthcare / Utilities / Finance

Market Top

Full Recovery

Bull Market

Early Recession

Bear Market

Early Recovery

Late Bear Market

Market Bottom

Full Recession

STREETTALKLIVE.COM

■ Economy ■ Market

2022 Q2

Dynamic Models

Dynamic Allocation: Dynamic Allocation programs are monitored MONTHLY. These programs start with a core asset allocation and then increase/decrease exposure based on SEM's Economic Models.

"Strategic" Asset Allocation Models ✚ SEM's Leading Economic Indicator Index

Informational Purposes Only; SEM's model is based on a multiple regression of historical data of 10 leading economic indicators. The purpose is to give a guide to the direction economic growth tends to be moving. SEM's Dynamic Models then use this to adjust the asset allocation between growth & defensive assets.

2022 Q4
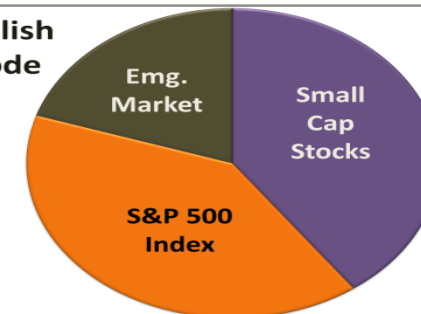
SEMWealth.com
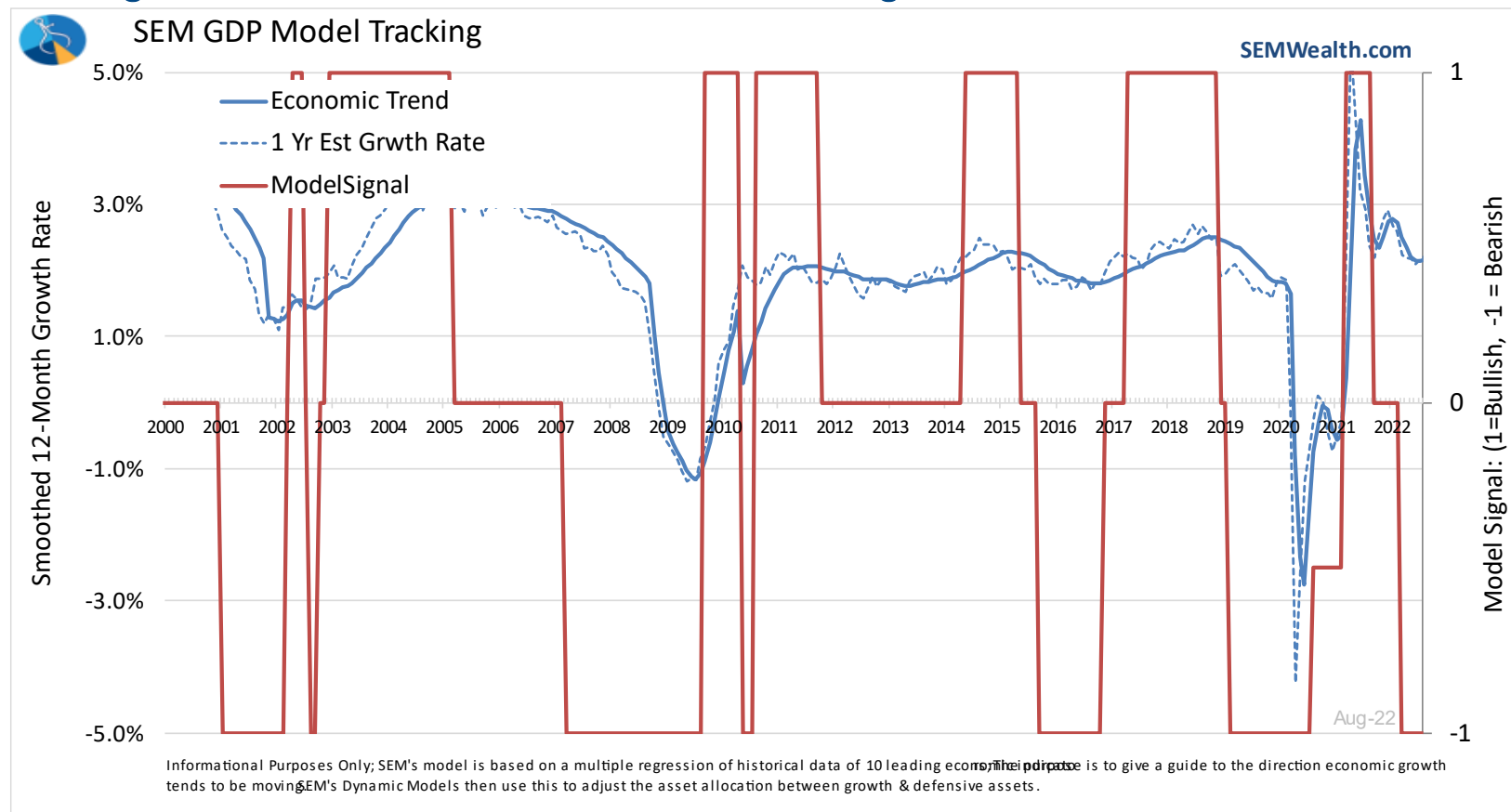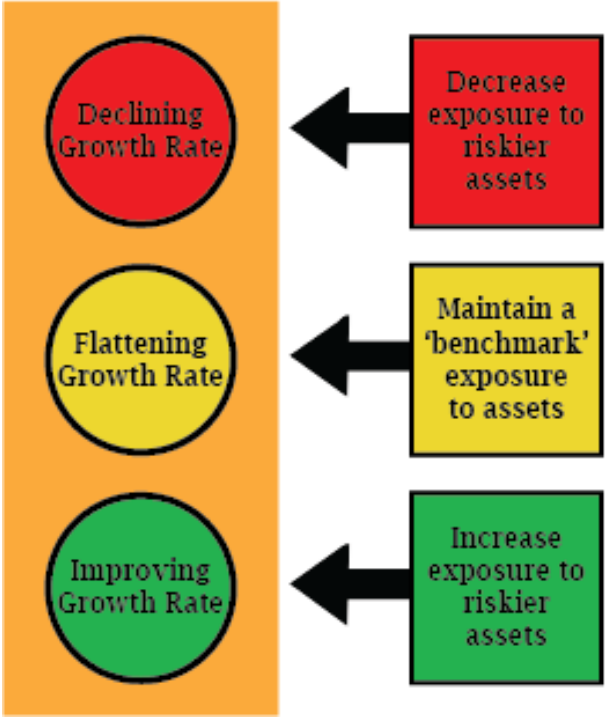
SEM's Dynamic Income Allocation (DIA)

GOAL: Manage exposure to duration via **_DYNAMIC_** asset allocation to asset classes based on business & economic cycle.


MS Pres. Alloc.

(Pie chart: CASH, Stocks, Bonds)

DIA Avg Alloc.

(Pie chart: Inverse Treas. Bond, Dividend Stocks, Bonds)
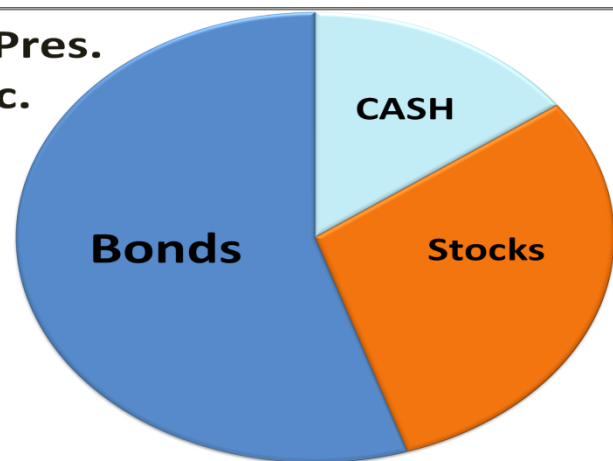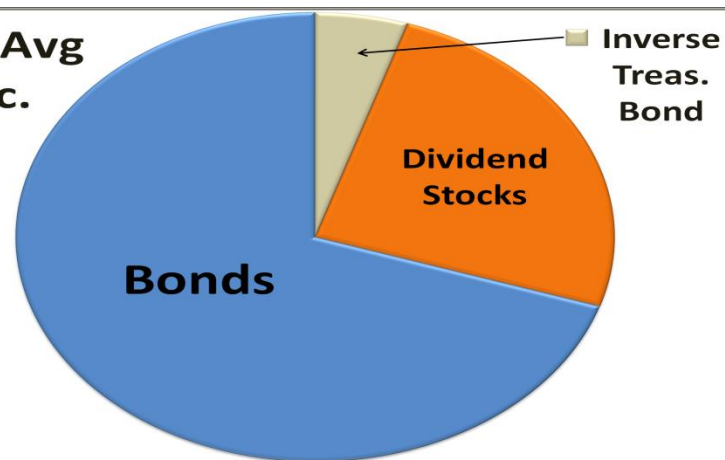
Economic Growth: Strong
Dividend Stocks: 40%
Tactical Fixed Inc: Higher Beta
Examples: Anchor, Counterpoint, Navigator, HCM

Economic Growth: Neutral
Dividend Stocks: 20%
Tactical Fixed Inc: Diversified Beta
Examples: Sierra, CMG, Toews, Wavelength, Navigator

Economic Growth: Weak
Dividend Stocks: 0%
Tactical Fixed Inc: Lowest Beta
Examples: Sierra, CMG, Toews, Anfield

Bullish Mode

(Pie chart: Tactical Fixed Inc., Dividend Stocks, Inverse Treas. Bond)

Transition Mode

(Pie chart: Tactical Fixed Inc., Dividend Stocks, Treas. Bonds)

Bearish Mode

(Pie chart: Tactical Fixed Inc., Treas. Bonds)
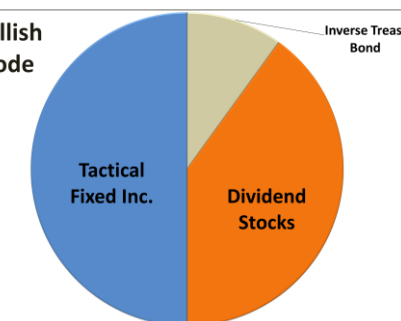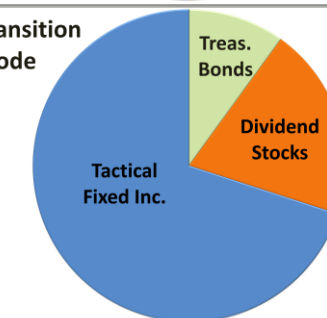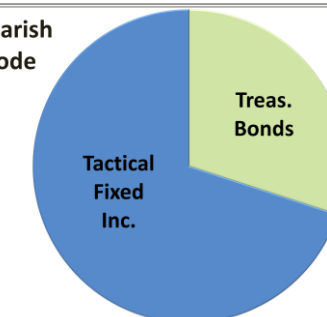
SEM's Dynamic Aggressive Growth (DAG)

GOAL: Manage exposure to market via *DYNAMIC* asset allocation to asset classes based on business & economic cycle.
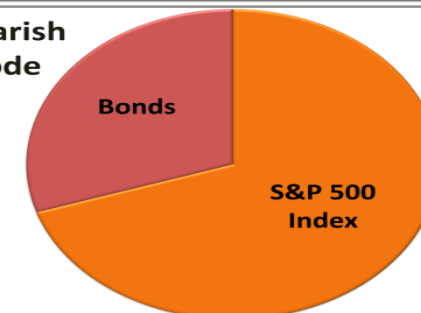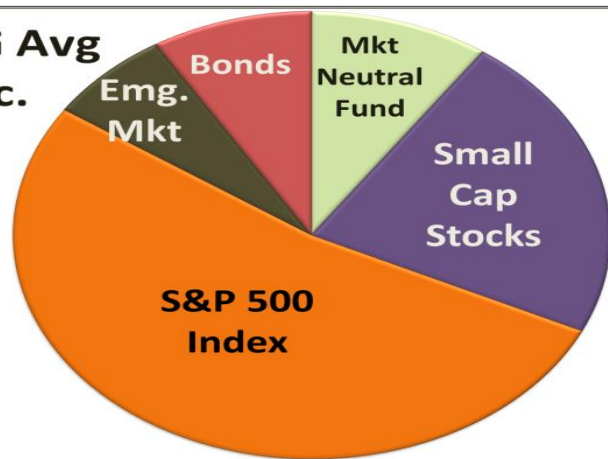

Economic Growth: Strong
Internal Indicators: Strong
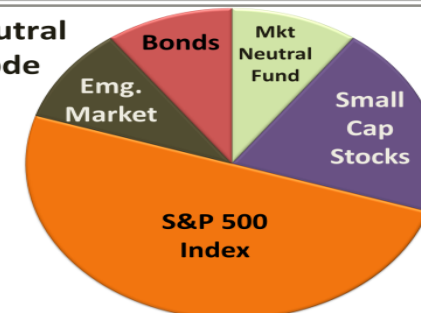
Economic Growth: Strong / Weak
Internal Indicators: Weak / Strong

Economic Growth: Weak
Internal Indicators: Weak

Strategic Models

Strategic / Factor Based Models

45 Funds

150+ Funds

AMERICAN FUNDS®

Vanguard
iShares by BlackRock

Price Performance
(30, 60, 90, 240 exponential averages)

Up vs. Down Performance

% from High

Volatility

AmeriGuard

SEM AmeriGuard & Cornerstone Models use a quantitative approach to select portfolio factor weights with a focus on:
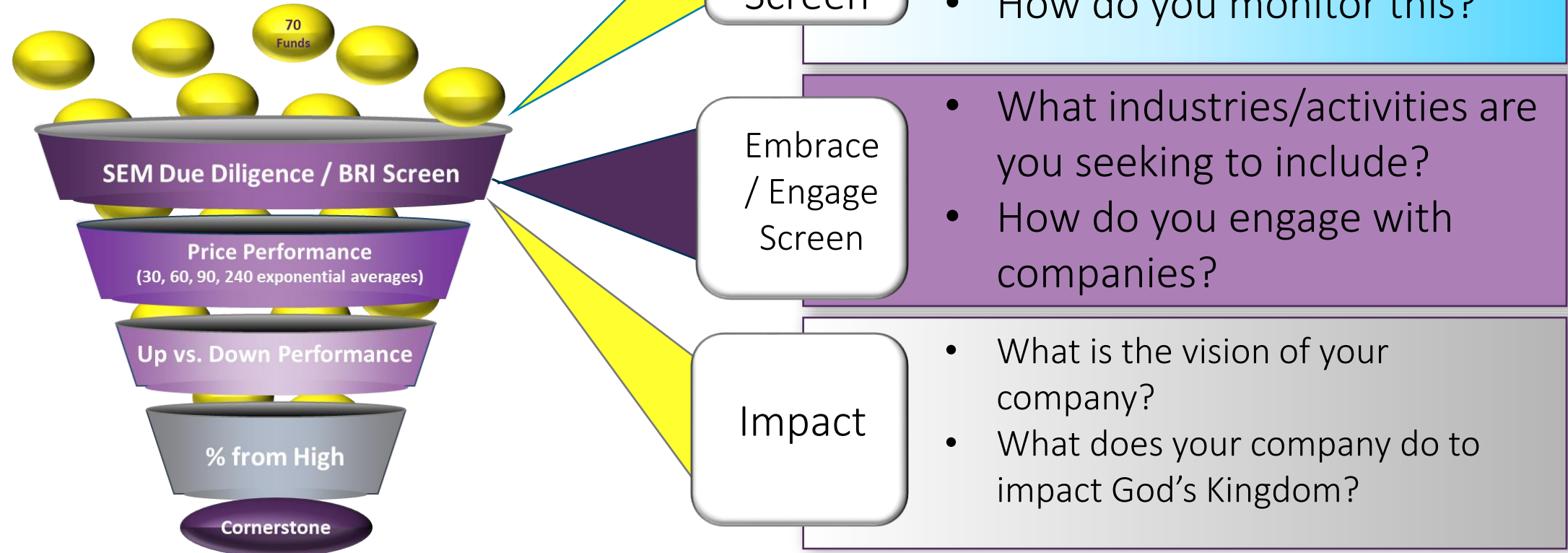
- Momentum
- Size (Large/Small)
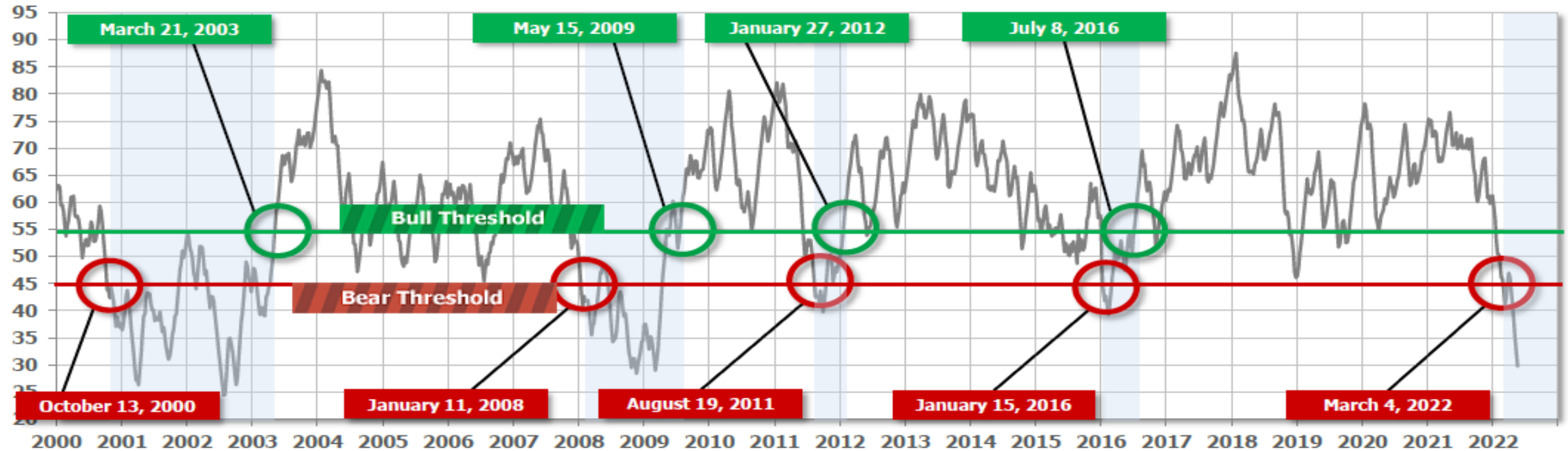- Value/Growth
- Volatility
- Location (US vs International)
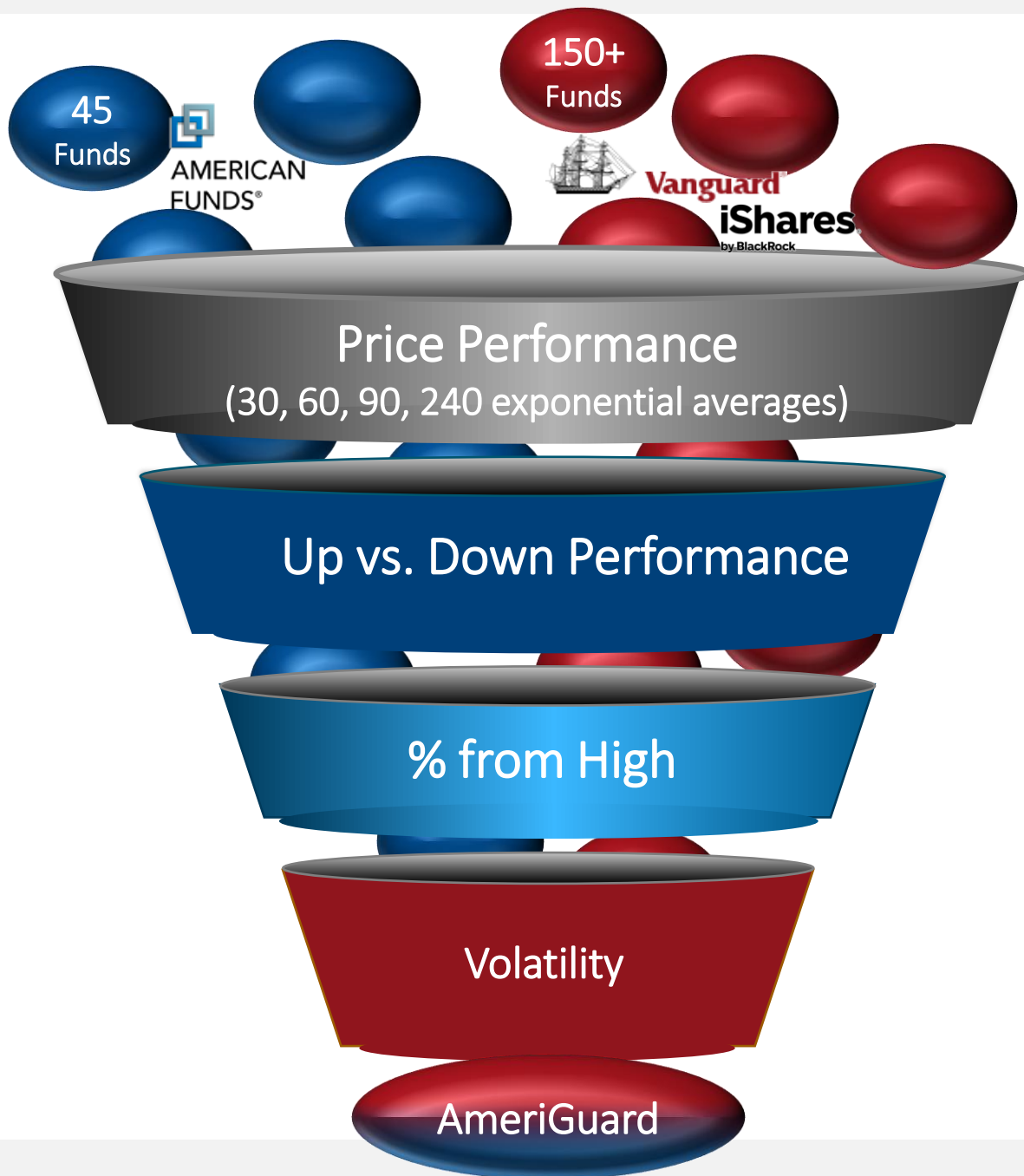
Biblically Responsible Strategic Models

The portfolio construction process follows a systematized process, starting with selecting the Biblically Responsible Investments eligible for placement in the Cornerstone Models.

70 Funds

SEM Due Diligence / BRI Screen

Price Performance
(30, 60, 90, 240 exponential averages)

Up vs. Down Performance

% from High

Cornerstone

Avoid Screen
- What industries/activities are you seeking to avoid?
- How do you monitor this?

Embrace / Engage Screen
- What industries/activities are you seeking to include?
- How do you engage with companies?

Impact
- What is the vision of your company?
- What does your company do to impact God's Kingdom?

Trends Still Matter

Source: NDR Multi-Cap Institutional (Universe), S&P Capital IQ and MSCI, Inc. (GICS), S&P Dow Jones Indices

SEMWealth.com

Dealing with Inflation

How we invest depends on the IMPACT of inflation

Above average growth

- Stocks will do well & help hedge inflation
  - AmeriGuard/Cornerstone
    - Growth outperforms value
    - Small outperforms large
- Treasury bonds struggle
  - Dynamic Income
    - Inverse Treasuries
- High yields & corporate bonds outperform
  - Tactical Bond / Dynamic Income
    - Overweight high yield

Average Growth

- Stocks may do "ok", but will be volatile
  - AmeriGuard/Cornerstone
    - Value outperforms growth
    - Large outperforms small
- Treasury bonds struggle
  - Dynamic Income
    - Inverse Treasuries
- High yields & corporate bonds slightly better than Treasuries
  - Tactical Bond / Dynamic Income
   - Overweight high yield

Declining Growth

- Stocks struggle
  - AmeriGuard/Cornerstone
    - Trend indicators reduce alloc.
    - Eliminate small cap
    - Invest in "materials" sectors
- Treasury bonds struggle
  - Dynamic Income
    - Stick to shorter-term bonds
- High yields & corporate bonds slightly better than Treasuries
  - Tactical Bond / Dynamic Income
    - Spend a lot of time in cash

SEM Signals Past 9 Months

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Process in motion – Sept 2022 allocations
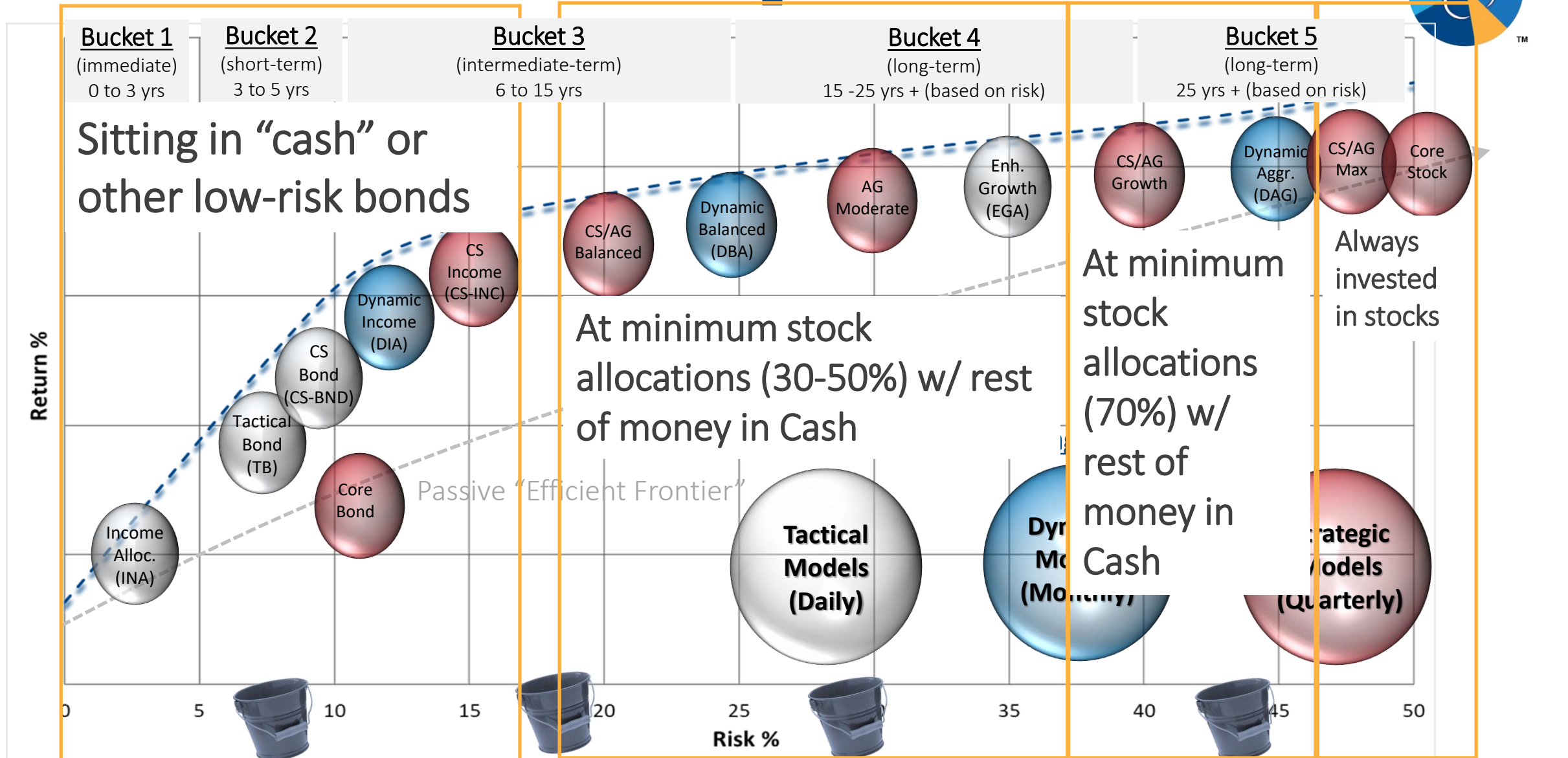
A Behavioral Portfolio Approach

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.

For more information go to
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