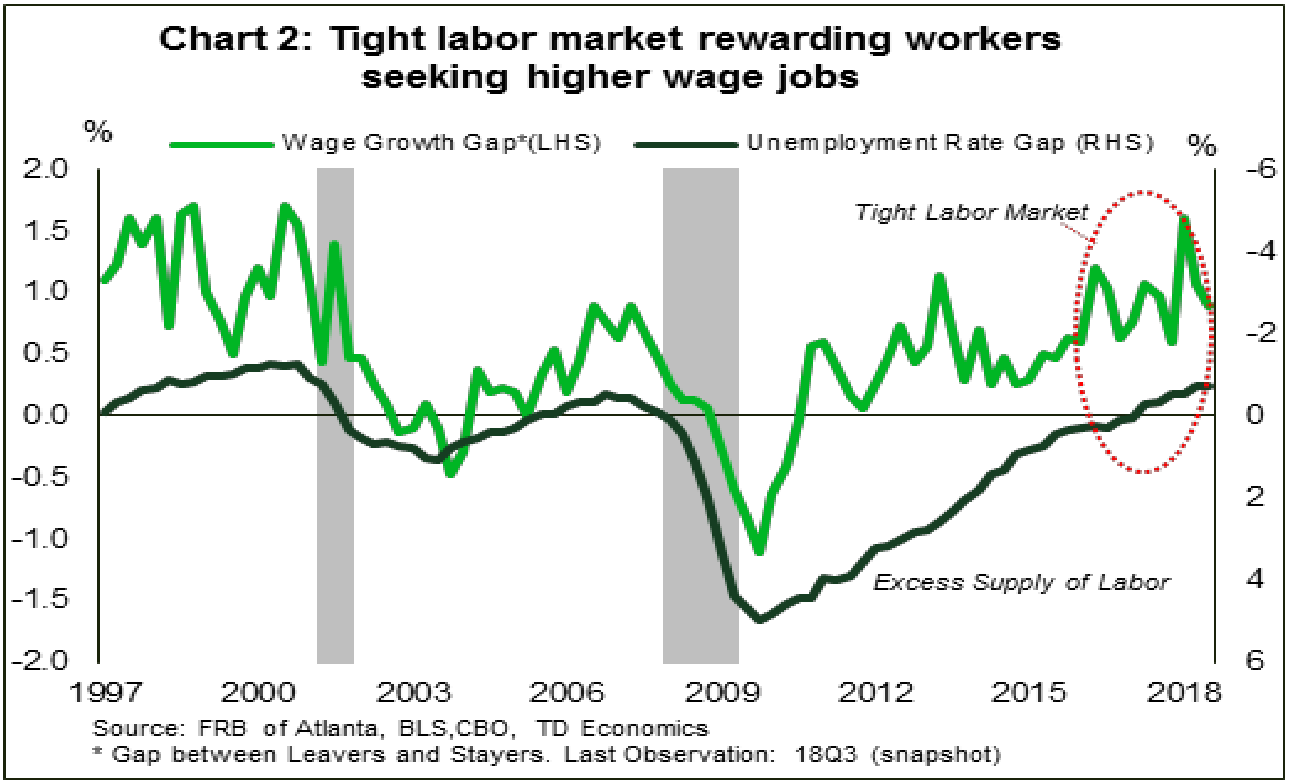
Market Update

September 18, 2018

Labor Market Signs are Beneficial to Workers

Recent data has confirmed that a robust economic expansion is still underway. Small businesses continue to impress as labor shortages and tariffs take effect. Tightness in the labor market was underscored by the July JOLTs data that recorded an uptick in the quits rate. Workers are being rewarded for quitting their current jobs for higher paying jobs. The chart below from TD Economics shows this relationship.



Information in the chart above was taken from sources we believe to be reliable; however; we do not guarantee its accuracy or completeness.

If wages continue to rise this could lead to increases in inflation in the future. The reason is that as wages increase, there is often a corresponding increase in consumer spending, which leads to more demand for goods and services. This typically drives prices up. August inflation came in at 2.7% year over year. The chart below continues to show equities to be the choice of investors as gold retreats. Bond prices especially long dated bonds continue to see price pressure, as the interest rate environment continues to point to future higher rates, due to strong economic conditions.

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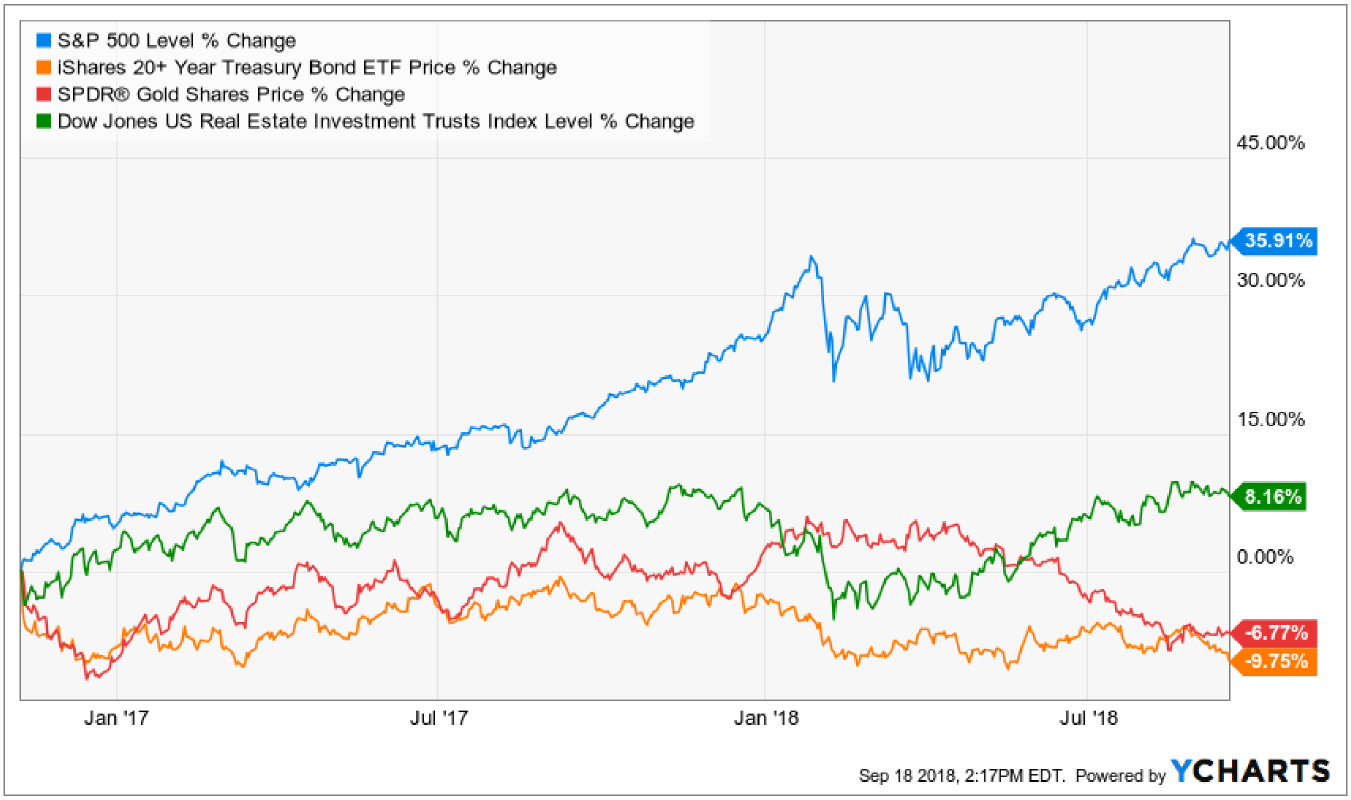

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The US Treasury yield curve, chart below, has shifted up and has maintained its relative steepness from the prior month. We anticipate that this pattern will remain for a while, as the economy remains robust and inflation and Federal Reserve interest rate policy are poised to continue supporting this. One area that could eventually cause some concern is the relative under performance of emerging market economies due to some pressure from countries' (such as Turkey) economic issues. However, if the labor market can continue to remain strong and consumer spending can continue to remain strong the US economy should be able to weather these issues for some time. The trade war with China has yet to drastically impact the American consumer and worker. If China and the US can resolve their issues, this would be a further positive for the economy and the markets.

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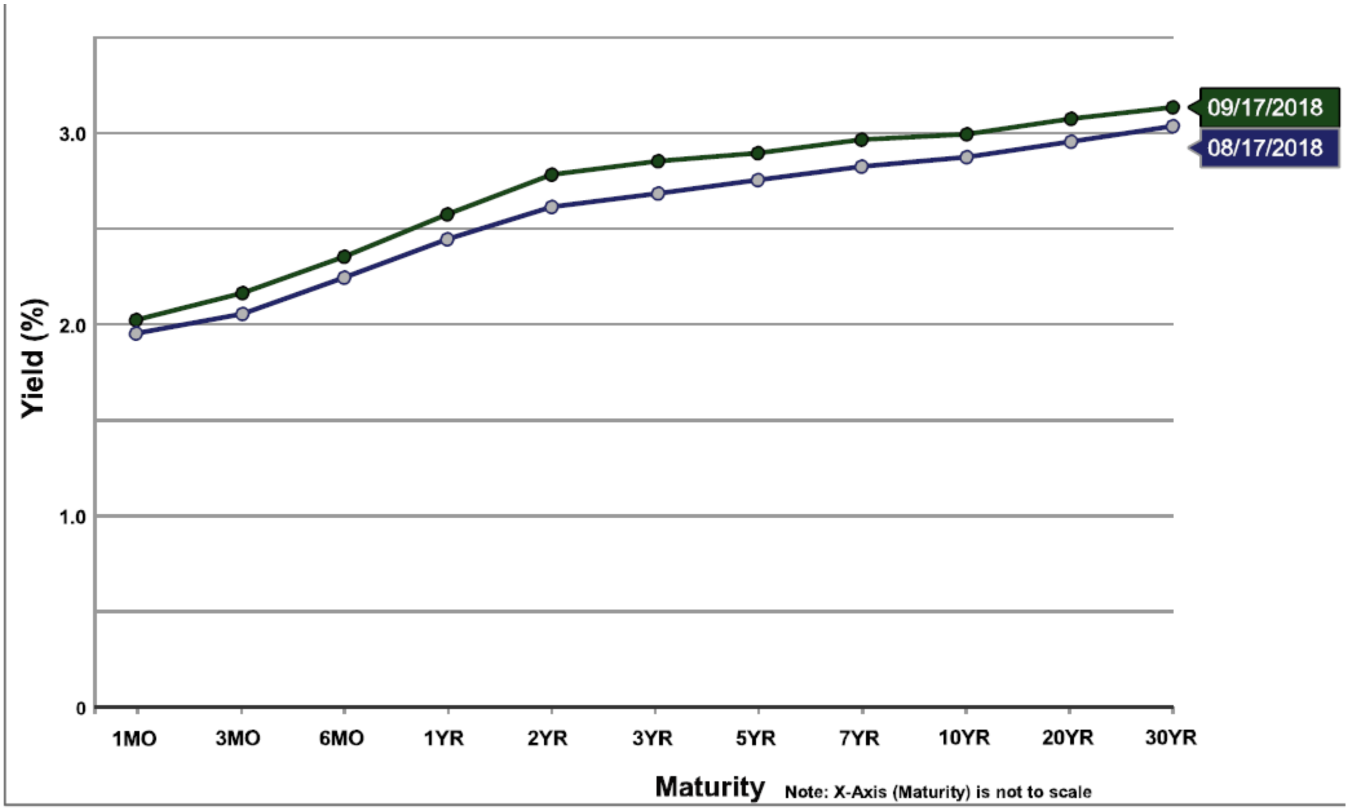

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https://www.treasury.gov/resource-center/data-chart-center/interest-rates/Pages/Historic-Yield-Data-Visualization.aspx

As mentioned in my previous update, we still feel that there are signs of a later stage economic environment, as evidenced by wage increases, inflation and rising interest rates. The US could stay in this economic phase for an extended period. The biggest concern for the economy in the next 12 months is still the Federal Reserve increasing rates too quickly to combat inflation, which can often stifle growth. Our outlook is more cautious for the remainder of this year, although we do feel there is more opportunity for growth.

Overall, we prefer domestic equities over international equites although some international markets may become more attractive as the U.S. economic cycle continues to mature. We are currently bearish on fixed income and interest rates and believe that the future will bring a higher rate environment. As mentioned in the past, we are looking at combating the decline in fixed income prices by shifting some of our fixed income holdings to floating rate securities. These tend to hold value better in rising rate environments. Also, we are looking at ways to directly combat inflation such as investing in Treasury Inflation Protected Securities (TIPS). These securities have important tax ramifications, and are typically most appropriately used in retirement accounts, where the current tax effects are reduced and often eliminated. It is important to maintain discipline regarding strategic asset allocation. Tactically, the shift to holding some floating rate bonds or bond funds and TIPS should help reduce some of the pressure on the bond allocations in our portfolios.

If you have questions or would like to discuss this further with regard to your personal portfolio, please contact me at 310-433-5378.

James M. Liotta, CFP®, CPWA®, AIF®, NSSA®, MBA
President
Prominence Capital GP, LLC.
jliotta@prominencecapital.com
www.prominencecapital.com