WALKER FINANCIAL ADVISORS, INC.
Registered Investment Advisor

Private Client Update   April 10, 2018

By: Scott Walker, CFP®

Happy Anniversary! – It was twenty years ago this February that I received a resume in the mail from a newly minted CFP® named Warren Isenberg. He was with American Express Financial Advisors and did not care for their commission driven approach to the business offered under the guise of financial planning. He preferred to be a fiduciary advisor and sought out an independent Registered Investment Advisory firm that worked with clients on a fee-only basis. I took a chance, and twenty years later could not be happier with the way it's all turned out. Warren handles 50 individual private client relationships, does investment research, and has serviced the City of Costa Mesa account since 1998. Warren and his wife Michelle have two boys, Owen and Everett, ages 14 and 11, and own a home in Encinitas. Thank you, Warren, for a job well done and congratulations! Your efforts are much appreciated!

The Economy – The January pop from the tax bill has faded and the calm steady climb in financial markets came to a halt in late January when higher interest rates triggered a spike down in prices. The economy has been strong, and the Federal Reserve does not want inflation to get out of control, so they are continuing a path of normalizing monetary policy by bumping up short-term interest rates. Two more 0.25% increases are planned for 2018, with more to follow next year. President Trump has instituted tariffs on imported steel and aluminum, and additional levies on other goods announced. China's President Xi has offered a conciliatory gesture by promising greater intellectual property protection. More negotiation is expected and hopefully Mr. Trump's tough tactics will help to level the playing field and begin to reverse the chronic trade deficits we've had with many foreign countries.

Portfolio Recap & Strategy – Across all client accounts, we had a net average gain of 0.15% for the first quarter, and 8.24% for the past twelve months. Our conservative accounts were hurt by higher interest rates which depressed the value of existing bonds and high dividend stocks last quarter. The top performers for the past three months included **Amazon.com, Intel, Intuit, and Square**. **Primecap Odyssey Growth** was our best fund, up 8.1%. Performance detractors included Qualcomm, which was sold following the announcement that the U.S. government would block Broadcom's acquisition attempt. The energy complex was weak, but we capitalized on the price decline by increasing our exposure with the purchase of **ExxonMobil**. Higher interest rates led to softness in bonds which resulted in us selling most of our funds, with the sale proceeds repositioned into super safe T-Bills. The security and comfort of U.S. Treasury Bills & short-term Notes feels like an electric blanket on a cold snowy night in Nebraska. Yields have been moving up and we are now able to get a 2% yield to maturity in December of this year. There is a bonus for taxable accounts as the interest is exempt from CA state income tax.

Having a cushion and knowing you have plenty of safe money to cover your cash flow requirements for the next 3-5 years helps to ride out any short-term downdrafts in the equity portion of the portfolio. If you need reassurance about the durability of your future cash flow, our E-Money Advisor platform can project your net worth given your current resources and spending assumptions. You can email our assistant for login instructions or further help with this at: olivia@walkerfinancial.com

Common Stocks – We continue to be overweight financial and technology stocks. Banks stand to benefit from a favorable regulatory backdrop from the current administration, and higher interest rates which will help profit margins. We own Bank of America to ride the wave. Technology stocks have led this market and we see long-term secular trends continuing to favor the companies we own. **Microsoft, Apple, Intel, Intuit**, and **Alphabet** continue to innovate with cutting edge products. **Amazon's** web services division provides secure data storage to governments and business organizations worldwide.

New holding **ExxonMobil** sold off last quarter giving us the opportunity to pick up shares at a bargain level. This stalwart has a strong balance sheet with low debt and has increased the dividend for the past 35 consecutive years and offers a current yield of 4.1%. We also own fellow Dow 30-member **Chevron**, which has a similar growth and dividend profile.

Defense contractor **Raytheon Company** was added last quarter as global tensions and a beefed up domestic defense budget provide a steady source of demand for their missiles and integrated air/missile defense system. The company is also a big player in gallium nitride chips. The military was an early adopter of this material in semiconductors which are faster, lighter, and more efficient than their silicon peers.

Your holdings may not include all securities discussed due to client inception date and manager discretion.

Heading to Omaha – Keeping current on our investments is important, so I'm headed to Omaha in May to attend the Berkshire Hathaway annual meeting while Mr. Buffet is still at the helm. Only current stockholders may obtain credentials for entry into the "Woodstock for Capitalists" meeting. Berkshire is our oldest and largest individual issue, so not only will I get an update on all their subsidiary businesses and stock holdings but will also get to hear an informed perspective on the markets from the master himself during an extensive Q&A session with the shareholders.

International Stock Funds – Given the recent weakness in global equity markets, we chose to bank our gain with the Matthews India Fund and the Oakmark International Fund. India was a big winner for us last year and with the inherent volatility of emerging market stocks, I did not want to see our hard-earned gains from last year evaporate. Oakmark was lagging, so we upgraded the position into our two remaining funds in this space. **Grandeur Peak Global Reach**, with their expertise in the small – mid cap space; and the **EuroPacific Growth Fund**, for large company exposure, managed by the American Funds out of L.A. As a risk control measure, we limit international equity exposure to no more than 15% of a total portfolio.

Fixed-Income Investments – With interest rates moving higher, our downside price threshold was breached for several of our taxable bond funds and ETF's last quarter, so we chose to preserve capital and sold to lock in our gains with the **Pimco Income Fund** and the **Vanguard bond ETF's**. Given the high probability of interest rates continuing to move higher, we are emphasizing short-term U.S. Treasury Bills with maturities up to one year. These instruments trade at a discount to par, or maturity value, and accrue interest daily. We have also purchased short-term coupon-bearing Treasury Notes. These pay interest semi-annually. Minimizing interest rate risk is important when the Fed is in a tightening mode and raising interest rates. Long-term interest rates do not always shoot higher when the Fed is raising short-term rates, but they have this year. Remember, when interest rates go up, the price of existing bonds goes down prior to maturity, and those reaching for yield in long-maturity funds can get hurt. We continue to like and hold one bond fund that specializes in floating rate bank loans and carries a low duration of 0.40 years. The **T. Rowe Price Institutional Floating Rate Fund** has a seasoned management team, good share price stability, and pays a monthly dividend with a trailing 12-month yield of 4.35%.

California Municipal Bonds – For our higher tax bracket clients we own individual issues of municipal bonds that pay tax-exempt interest. Using a ladder strategy, we own bonds with staggered maturity dates. Recent purchases have been in the 1-2-year maturity range to minimize interest rate risk. We are willing to sacrifice some yield in exchange for greater principal stability at this point in the Fed cycle.

Itemized Deductions – For those clients who itemize deductions, the new tax law has brought about some changes that become effective for the 2018 tax year. Mortgage interest will now be deductible for first mortgage debt up to $750,000. Interest on a second mortgage or home equity loan is no longer deductible. The deduction for State income tax and property tax is now capped at $10,000 per year. Miscellaneous itemized deductions such as tax preparer fees and investment advisory fees are no longer deductible. Because of this change, for the current billing cycle we debited each client account for its respective fee. We work with many client's CPA's throughout the year to maximize tax planning opportunities. If you are over age 70 ½ and taking required minimum distributions from your IRA, one strategy to consider is to have your IRA pay a portion of the distribution directly to a charity, thus excluding that amount from your taxable income.

Always remember that Warren and I eat our own cooking, as we hold many of the same securities in our own personal accounts that are found in our client accounts. Please let us know if there is anything else we can do to be of further service to you.