

GAUGES

- GDP – 2.5 ↓
- Interest Rates – 1.5 % ↑
- Unemployment – 4.1 ↓
- ISM – 60.8 ↑
- Inflation – 2.1 ↓
- Consumer Sentiment – 99.7 ↓

HIGHLIGHTS

- US economy is robust
- Global economy continues to show strength
- Corporate profits are increasing

SUMMARY OF THE ECONOMY

Robust-Robust-Robust. Finally, we are seeing job growth, a strong real estate market, a conducive business environment, good corporate earnings, inflation in check, employment is great, and upbeat consumer confidence. It's been a while since we have seen this, looks like we are hitting on all cylinders. All in a backdrop of tax cuts, trade restrictions, increased government spending, and a tense political environment with North Korea.

The economic outlook for the US continues to be robust for most of 2018. What could put a drag on the economy later this year is aggressive Fed rate hikes, increased inflationary pressures or any political turmoil.

The Global economy continues to show strength in each of the regions – Asia, Europe, and the Americas.

The Eurozone economy grew at its fastest pace in 10 years, with GDP at 2.5%. This is the result of an improved global economy, confidence, and monetary stimulus by the Central Bank.

For the Asia economy, Japan has joined the global economic growth after stagnating for so long. Japan's economy is showing eight quarters of growth as a result of increasing capital investments and corporate profits. China's economy continues to maintain growth above the target GDP of 6.5%.

Rising tides lifts all boats! Latin America is participating in the global growth.

GLOBAL ECONOMY

The global economy will continue its growth for 2018. Positive signs are coming from each region including Latin America.

China's GDP growth will stay around target of 6.5%. China is planning on tax cuts and reducing the deficit through reduced spending. ¹

The Manufacturing PMI from China for Jan 2018 came in at 51.5, maintaining the same level as the prior month. Over 50 indicates an expanding economy.²

China's exports is maintaining a steady growth since 2017.³





Contact Us

Allied Affiliated Funding

5151 Belt Line Rd., Suite 500

Dallas, Texas 75254

972-448-3583

David.lau@fundingbyallied.com

www.fundingbyallied.com

Japan's economy continues to grow from the negative growth rate they experienced in 2014.⁴ The economy looks like they are on a slow upward trajectory, which contributes to the global economic expansion. They have been slowly coming out of "The Lost Decade" back in the 1990's that started with a recession.



The Euro zone continues to show improved GDP growth in 2018 with a nice upward trajectory. As a reference, from 1995-2017, the average growth was around 1.6%. The EU is the 2nd largest economy in the world, but China may surpass this region in 2018-2019.⁵



Latin America's economy is expected to have a 2.2% GDP growth, with Peru, Chile, Brazil, Panama, and Columbia expected to have improving economies. Venezuela is the only country showing negative growth for 2018 as they will be entering their 5th year in a recession.

USA ECONOMY

The US economy is showing better growth than we have seen since the great recession. Employment is up, jobless claims continue to come down, the housing market is strong, consumer confidence is high, and the stock market is pushing all time highs.

Economic Data	Latest Date	Current	Prior Period	Year Ago	Trend: Yr -Yr% Chg	Note
GDP	4Q17	2.5	3.2	1.8	38.8 ↑	
Capacity Utilization (%)	Dec	77.7	76.1	76	2.2 ↑	1972-2015 average is 80.0
New Home Sales (1000's units)	Dec	643	639	548	17.3 ↑	Pre-Great Recession peak -1389
New Housing Starts (k)	Dec	1,209	1,159	1,268	-4.8 ↓	Pre-Great Recession peak -2273
Inventory to Sales Ratio Motor Vehicles	Dec	2.47	2.49	2.75	-10.1 ↓	Looks like car sales pushing inventory down
PMI	Dec	59.3	60.2	59.3	0	> 50 manufacturing expanding.
Consumer Price Index (CPI)	Dec	247.9	246.4	242.7	2.1 ↑	
Rate of Inflation (%)	Dec	2.1	2.2	2.1	0	Government target less than 2.0%
Consumer Sentiment	Dec	98.5	95.1	96.8	1.7 ↑	Non-recession periods, avg 87.8. Recession avg 69.3
Unemployment Rate	Dec	4.1	4.2	4.7	-12.7 ↓	
Jobless Claims (1000's)	Dec	250	269	258	3.1 ↓	Great recession peak 650k+

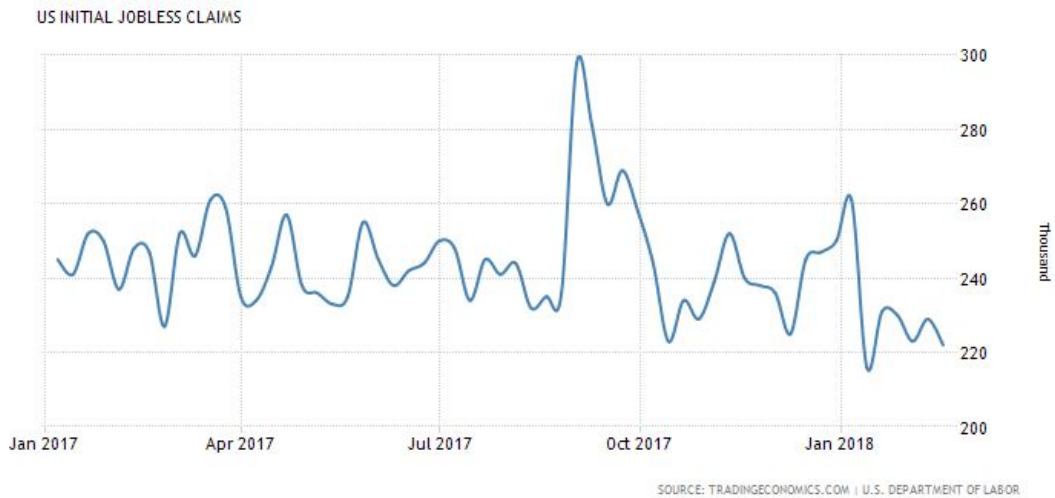
Job growth has been seen in all areas except for information technology. Strongest areas were in construction, retail trade, professional and business services, manufacturing, financial, government, and education.

Manufacturing PMI is at 59.3 in Dec 2017 showing the strongest growth since 2014. This can be attributable to greater domestic sales and exports. There are signs of rise in payroll, stretched delivery times and increase factory prices. All an indication of inflation to come.

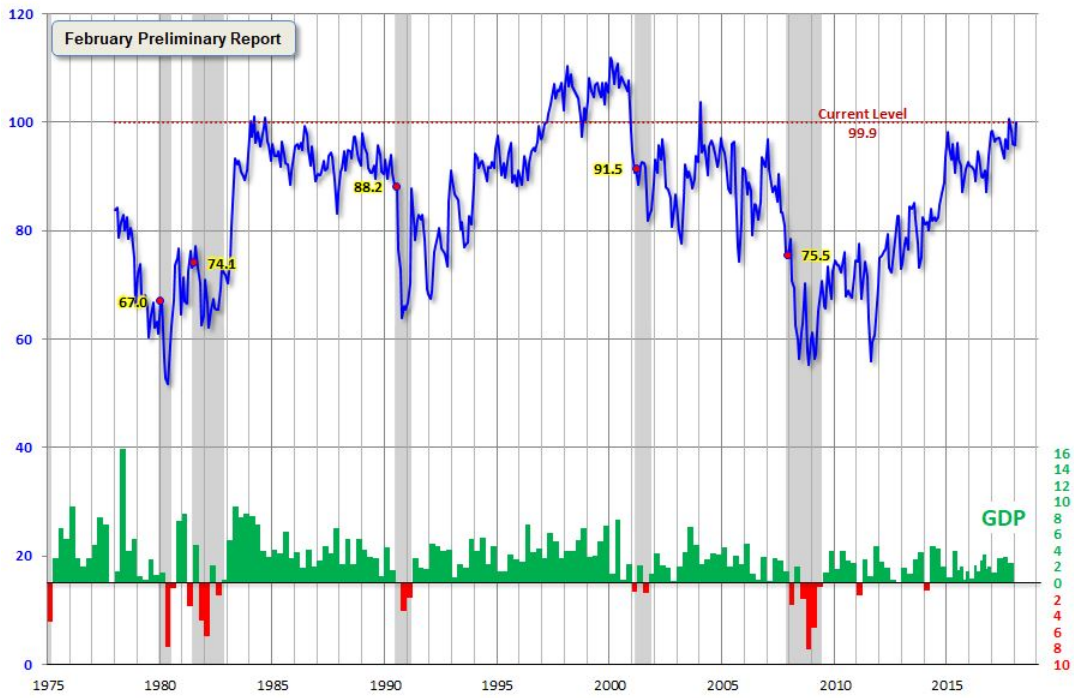
Retail sales shows a largest decline since February 2017. Looks like the holidays did not bring much cheer to Santa this past season. Sales were up for service stations, electronics and appliances, clothing, and misc store retailers. Sales were down for auto and parts dealers, gardening and building materials, furniture, sports and hobbies.⁶



Initial jobless claims is staying under 300,000 per week, at 222K, mid Feb 2018.⁷ Since January 2017, this is showing a downward trend, which is good for the economy and government tax receipts.

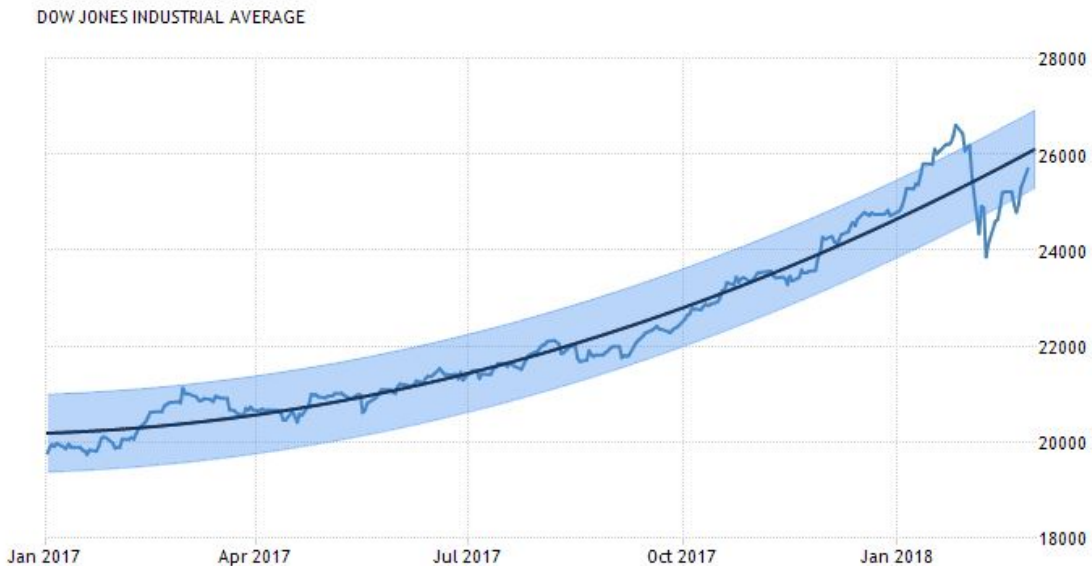


The University of Michigan Consumer Sentiment is a widely watched indicator of the overall health of the economy from the consumer's viewpoint. Preliminary sentiment for February 2018 is at 99.9, up from January 2018 by 4.2.⁹ From a historical perspective, non-recessionary years the average is 87.8 and during recessionary years is 69.3. The average has been 85.6.



MARKETS

The stock market continues to move higher since 4Q2017. The shaded area represents the forecast projections. So far the economy performance appears to justify the ever rising stock market – Tax cuts, corporate profits, promise for infrastructure spending. The rising interest rate environment may curb the stock market enthusiasm later this year and into 2019.



Corporate profits are trending on an upswing.¹⁰ Another reason for a strong stock market.



The US Government 10-year bond is at 2.85% as of end of February 2018, trending upward the past few months.¹¹ Shaded area is the projected forecast range. I would anticipate 3-4 more rate hikes this year, which will push the rates higher.



REAL ESTATE

Housing starts are trending upward since early 2017. As a reference, housing starts have averaged approximately 1440K over the past 40+ years. Housing typically increases economic activity – home improvements, update furniture and accessories, new appliances, etc. The S&P/Case Shilling index on home prices shows home values up 56.3% year to year in December 2017.¹²



The 30-year mortgage rates continue to trend higher. FED rate hikes will continue to make mortgages more expensive. It is expected the mortgage rates to stay under 5.0 for 2018.¹³ There looks like a push and pull coming with increased interest rates and the millennials ready to buy houses after starting a family.



COMMODITIES

Oil has been creeping up since this last report, now hovering in the \$55-65/barrel. Oil rig deployments have also steadily increased, a sign of confidence in the current market environment.

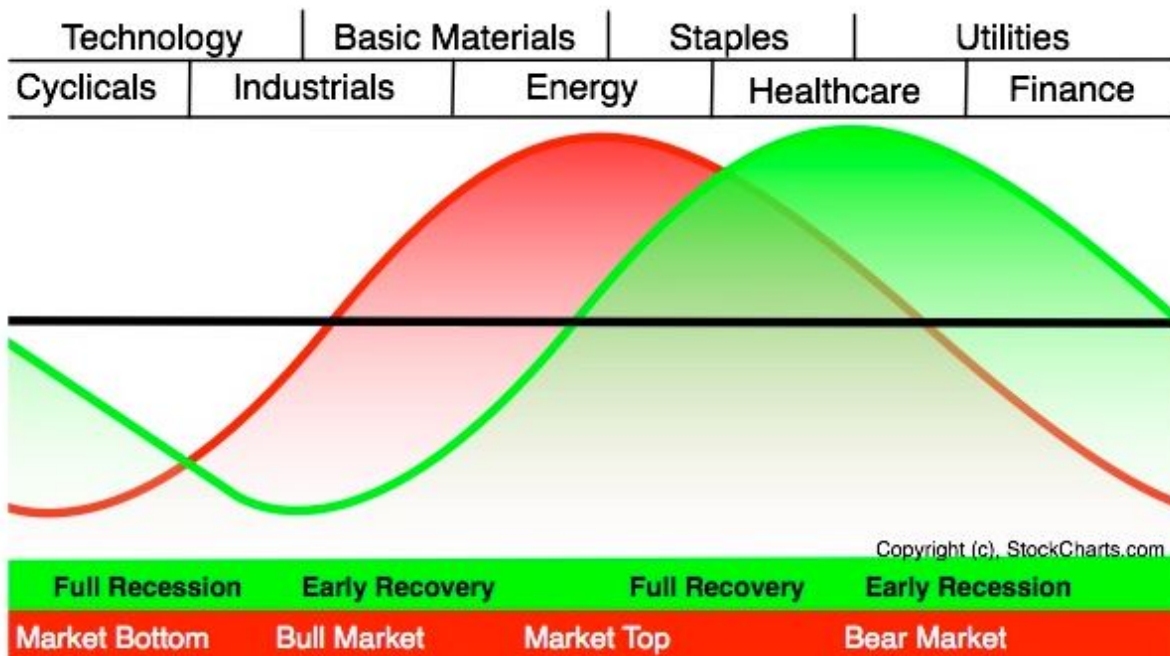
Gold continues on an upward trajectory since early 2017. It is currently around \$1300/oz. Gold is often used as a safe haven against other investment risk, hedge against inflation, or economic risk and uncertainty. As the stock market continues to rise in the backdrop of rising interest rates, demand for less risky assets such as gold may be driving the price higher.

Copper prices continues it's rise since early 2017, indicating a demand for the metal as construction boom continues throughout the US. Spending for infrastructure will place more pricing pressure on this metal.

SOME THOUGHTS FOR YOUR THOUGHTS – BUSINESS CYCLES

Ever wonder where we are at in the economic (business) cycle and what's next? Does this impact me and how? Who is driving this economic cycle?

The picture below depicts a general economic or business cycle in green and a stock market cycle in red. The black line is expansion (above the line) or contraction (below the line). The stock market cycle typical leads by about 6 to 12 months and is typically a proxy for things to come.



Just to keep it simple, here is an explanation of each phase. Early recovery has low but increasing inflation, low interest rates, low inventory and unused manufacturing capacity. Full recovery, considered expansion, has moderate inflation and capacity, rising interest rates, and rising commodity prices as expansion puts pressure on supply and demand. Early recession is characterized by lower consumer confidence, decrease interest rates, less pressure on prices thereby reducing inflation and decrease in inventory.

The answer to the questions above is yes, you are affected by this business cycle. As interest rates go up, home and auto loans get more expensive. As the expansion increases, there is more demand for good and services, hence pricing pressures are felt in the way of inflation, which reduces your purchasing power. Also with expansion comes lower unemployment, increasing wages, adding additional pricing pressures. The government drives the economic cycle. Legislators use fiscal policy (spending and taxation) and the central bank uses monetary policy (interest rates and money supply). Then either directly or indirectly businesses react to these policies which affects each of us.

So, where are we at in the diagram above? It looks like we are somewhere in Early Recovery to Full Recovery or expansion phase - inflation is moderate (government target is at 2.0%), we are in a rising interest rate environment, and not at full capacity yet. Companies that will benefit in this phase are chemicals, plastics, paper, metals, semiconductors, computers, software and services, energy, consumer staples (essentials such as food and beverage, tobacco, household items).

ABOUT THE AUTHOR

David Lau is Allied's Chief Technology Officer, "Rocket Scientist," Chef, Martial Arts extraordinaire, and In-House economist. David Lau joined Allied in April 2007 as Chief Technology Officer. He is responsible for all aspects of information technology, workflow processes and facilities management, including identifying technology solutions. He is always on the lookout for innovative and cutting edge strategies that will deliver Allied's services more efficiently. He is our resident "go to guy" for anything and everything technology related. David has a strong background in systems engineering, customer interfacing and product life cycle management with both small and large corporate process exposure. He has start-up, corporate and international experience, as well as expertise in the financial, defense, telecommunications and computer industries.

Prior to joining Allied, David was the Co-Founder and President of Dallas-based System Solutions Group, Inc., where he managed a staff placement, consulting and custom development company for the Internet and telecom industry. He built a start-up business that generated \$1 million revenue in the first 18 months, securing a major contract with Verizon. This company was successfully acquired by another telecom business he co-founded where he developed sales of over \$2 million and generated proposals of over \$60 million in new business opportunities. Prior to that, he worked as a Senior Systems Engineer for Texas Instruments for over 18 years, where he also worked on drones. David has a Bachelor of Science degree in Electrical Engineering from Virginia Polytechnic Institute and graduate work in Computer Science at Southern Methodist University. He also holds various patents. David enjoys cycling, traveling, photography, reading, cooking, and trying out new restaurants and cuisines. David also teaches martial arts and is a car enthusiast.

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