Private Wealth Management

InSight

Summertime marks the mid-point of the year, so now is a good time to take a moment to check on your full financial picture, including a review of your goals and progress you've made toward milestones. Statistics show almost four million Americans anticipate retiring in the next 15 years, and there are key considerations that can help anyone prepare, whether retirement is right around the corner or 20 years away. We encourage everyone to have a solid plan for retirement, which begins with understanding your core numbers: anticipated age of retirement, how much income you'll need to maintain your current lifestyle after retirement, and the value of your assets and cash savings. Having a clear picture of your current and future states makes establishing priorities simpler. Keeping these numbers in mind as you make other financial decisions ensures your goals and choices remain in alignment.

While retirement planning is critical for your future, there will always be plenty of present-day matters to attend to. This issue of InSight covers several topics related to life events and the economy. Beth Brown, senior vice president and senior wealth advisor, discusses steps to consider when you are faced with an unexpected financial windfall to help ensure your plan supports your objectives. Shelly Addington, vice president and private banking client manager, provides an educational construction loan overview, including what you can expect from the process from start to finish. And KC Mathews, UMB Bank executive vice president and chief investment officer, delivers an economic analysis that covers the impacts of political and policy shifts.

As you navigate your day-to-day decisions, be sure to connect with your UMB team often. We're committed to partnering with our clients through every stage of your financial story as it changes over time.

We hope you find value in the summer edition of InSight, and we thank you for being part of the UMB family.

Sincerely,

Dana Abraham
President, UMB Private Wealth Management

Reality TV Versus Reality—America is Watching

Reality TV has become very popular. Apparently we enjoy watching people be voted off the island, search for love and get fired on national television. Included in this group is our new president, who was the host of The Apprentice for a number of years. However, since the January inauguration, President Donald Trump is now faced with reality, which does not include retakes, professional editing and an audience who enjoys both failure and success.

But, his new job does include balancing an active audience's perceptions and actual reality, particularly as it relates to the economy and some of his key initiatives.

Paradigm Shift

Trump has suggested a paradigm shift by stimulating economic growth through fiscal policy and government spending, rather than relying on monetary policy and lower interest rates. While the economic fundamentals have been improving for several quarters, which contributes to positive public perception, Trump's proposed fiscal policy stimulus will have a relatively minor impact on long-term economic growth.

The empirical evidence suggests that when the economy is at full employment, any fiscal policy stimulus will have a temporary impact on growth, four to six quarters at best. In reality, fiscal policy stimulus does one thing on a long-term basis—it increases the national debt.

Tax Cuts

The president, along with others such as Treasury Secretary Steven Mnunchin, has suggested tax cuts will pay for themselves by boosting economic growth. There is no evidence to support this idea. Rather, historical reality suggests cutting taxes will increase the federal debt burden.

Former President Ronald Reagan in the early 1980s and former President George W. Bush in the early 2000s both cut taxes, yet there is little evidence that economic activity improved. However, we do know the national debt mushroomed in both cases.

Repatriation of Foreign Profits

Believe it or not, we have been here before. In 2004, the American Jobs Creation Act was passed. Part of the plan covered the repatriation of overseas profits at a reduced rate of 5.25 percent. In 2004, five companies, primarily pharmaceutical, dominated the almost $1 trillion foreign profit stockpile.

Only one-third of the total cash came back to the U.S. Most of the money went to repairing corporate balance sheets and rewarding shareholders with

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share repurchases. $18 billion did go into the U.S. Treasury's coffer. The Congressional Research Service, a nonpartisan think tank, said the program was an ineffective means of increasing economic growth.

Today, the reality is that a small number of technology companies dominate the $2.5 trillion cash balances overseas. If offered a tax reprieve on repatriating foreign profits, history tells us the same behaviors will result—higher dividends and more share repurchases, which, I believe, will not materially impact the economy.

Multiplier Effect

The multiplier effect is a phenomenon where given a change in a particular input, such as government spending, a larger change in an output occurs, such as gross domestic product (GDP).

We are about to see a paradigm shift in the U.S.—moving from monetary policy stimulus (interest rates) to fiscal policy stimulus (government spending).

The million dollar question is, "Will it promote economic growth?" The Congressional Budget Office provides historical analysis on the efficacy of fiscal spending. The multipliers show that any form of increased government spending would have a higher multiplier effect than any form of tax cuts.

Economic Reality

There are two primary drivers of long-term economic growth, labor force growth rate and productive gains. Labor force growth rate in the U.S. is approximately 1.2 percent. Non-farm productivity year-over-year growth is 1.1 percent. Add them together, and you have a 2.3 percent trend GDP over the next few years. We could realize one or two quarters of 3.0 percent or greater GDP, but it's not sustainable.

However, this is not a doomsday conclusion. If we do experience trend GDP between 2.0 and 2.5 percent, it will allow companies to grow revenues and earnings. This in turn will support higher stock prices.

Political Process Reality

Trump's term has really just begun. And what many reality television enthusiasts, and the president himself, may be finding out is that reality TV can be fun to watch, but the reality of the political process may not be.

KC Mathews, CFA
EVP, Chief Investment Officer, UMB Bank

As executive vice president and chief investment officer, KC Mathews is responsible for the development, execution and oversight of UMB's investment strategy. Mathews has more than 20 years of diverse experience in the investment industry. He earned a bachelor's degree from the University of Minnesota and a master's degree in business administration from the University of Notre Dame. He also attended the ABA National Trust School at Northwestern University and is a Chartered Financial Analyst (CFA) and member of the CFA Institute.

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Build Your Dream Home: Construction Loans Explained

Recent shifts in the economy have positive implications for new home construction in the U.S. In fact, MarketWatch reported in May that low home inventory, growth in single-family home construction, and high builder sentiment have come together to create a bright outlook for new home builds. If you have been dreaming of building a custom home for you and your family, now may be a good time to start your research.

Considering construction

The home buying process comes with many factors to consider, and for those who dream of crafting their home from the ground up, the road ahead can seem even more complicated. One of the most important aspects of a home build project is financing, and construction loans are specifically designed to meet those needs. Construction loans are short-term loans that can be used to build a primary or secondary home. Typically, a construction loan is a temporary financing option—anywhere from six months to a year—that helps cover the cost of ground-up construction before the home is eligible for long-term financing, like a mortgage.

Finding financing

If you're ready to take the plunge and begin building your home, start by researching lenders who offer products like standalone construction loans, or construction-to-permanent loans that transition to mortgages when the project is complete. Loans that transition to long-term financing can potentially save you money because there is only a single closing cost associated with the end of the loan term. However, some may opt to keep the construction and mortgage loans separate so they are free to search for the best rates and terms for each type of loan—especially in the current rate environment.

Financing begins with an application process similar to that of purchasing a home. The major difference is that the project scope—comprehensive building plans, estimates, proof of a purchased lot—is required almost right away. Many lenders may require a signed contract with a builder before considering the loan application. This a good time to set up builder and/or risk insurance due to the unpredictability of build projects, which can be delayed or adjusted for a variety of reasons.

Appraisals

Once construction loan approval is granted, the project will be appraised. This is the most critical step of the construction loan process because it determines the final loan amount. Each lender is different, but in most cases, financing will be given for the lesser of either the cost of building the home or the appraised value of the final product. The appraised value is largely determined by reviewing all of the home's components and then comparing it to recently-sold, similar homes in the area.

For example, consider the cost of building a home as $500,000 and the appraised value as $550,000. If the lender is willing to finance at least 80 percent, it would choose the lesser of the two prices — $500,000 — to reach the total loan amount of $400,000.

Down payment and draws

Another critical component of home construction financing is the equity contribution, or down payment. The equity contribution is usually a percentage of the project's cost or value, whichever is less, which the homeowner pays toward the project in cash. It's important to note that the equity contribution amount is used to pay for project costs first, with the loan money being disbursed only after the equity contribution is spent. Having additional cash reserves available outside of the equity contribution can help offset any unforeseen expenses or additions during the build.

Once financing is in order and the project is underway, the next step is to become familiar with the draw process, which normally follows this system:

- The general contractor and other project vendors submit invoices to homeowner.
- The homeowner submits the draw requests to the lender.
- The lender reviews the requests and ensures that the costs align with the project budget.
- The lender's inspector is sent to the project site to check that the goods or services invoiced are either on site as promised or completed as described.
- If all inspections and reviews are passed, the draw requests are approved and the homeowner can draw those funds to pay the invoices.

Building the perfect home

Building the perfect, one-of-a-kind home can be an exhilarating experience—as long as you have patience and a good sense of the process. Construction loans feature several benefits that can help keep the project moving, including regular inspections, flexible financing, appraisals and budget management. While complex, crafting a house from scratch can be rewarding in the long term. ■

Shelly Addington is vice president and private banking client manager at UMB Bank.

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First Steps for Handling an Unexpected Financial Windfall

It may seem far-fetched to imagine yourself on the receiving end of an unexpected financial windfall, but many people will experience a sudden influx of cash at least once in their lifetime. Windfalls don't always come from winning the lottery; they can be legal settlements, inheritances, proceeds from the sale of a business, unplanned investment gains, or even a startup that becomes an overnight success. CSNBC reported that in the next few decades, more than $30 trillion in intergenerational wealth transfers will change hands, which means managing these financial transitions will become increasingly important.

In the event you are faced with an unanticipated cash infusion, it's important to have steps in place to help you adjust to having additional funds and take advantage of the opportunity.

Gather your team

Whether you know months in advance or just found out about your financial windfall, your first step should be to gather your team of professionals. Handling significant changes in wealth requires an in-depth look at your full financial picture and knowledge of available strategies, from savings and investing to taxes and protection—because the addition of unexpected funds will almost certainly impact your current financial plans. Advisors to connect with include:

- Tax professional
- Wealth advisors
- Estate planners
- Attorneys

These individuals can inform you of your options around saving, investing, and spending in the context of your personal situation, and alert you to areas that may become more complicated—such as income tax and your personal estate. Tax planning, at the time you receive the funds and beyond, is an especially critical component to consider in regard to a windfall.

Understand the fine print

Sudden windfalls can be exciting, but they can also be brought on by stressful events like the death of a loved one. In times like these, details tend to fall to the wayside—exactly when they are most important. To help navigate your financial decisions in complex and emotionally heightened situations, understanding the fine print should be top of mind. Your financial team can help you process these details, but don't forget to ask questions and take notes. Some questions to consider include:

- Where exactly is this money coming from?
- What is the timing for receiving this money?
- What are my tax obligations?
- Is there paperwork or are processes required before I can receive the money?

Develop a short- and long-term plan

With your team and the fine print taken care of, your next step is figure out how you plan to use the windfall. Until you have a plan in place, avoid making large purchases or any significant financial decisions. Planning for the long-term first can help place you in a better financial story at or during retirement. For instance, establish your priorities for retirement, charitable giving, investments and family support.

Where will your windfall provide the most benefit? Your advisors can help you analyze where you are, what is most important to you, and where you want to be financially.

After reviewing your long-term financial goals, identify your short-term financial concerns or issues, such as outstanding debt, upcoming expenses, healthcare, and family-related expenses. Make a plan to tackle those after setting aside funds for your longer-term objectives.

Implement the plan

Obtaining an unexpected cash influx can be a boon, but only if you understand how to react before the funds reach your account. Be deliberate with your choices and make sure you have a complete picture of your financial obligations and opportunities so the windfall works to your financial advantage. ■

Beth Brown is senior vice president and senior wealth advisor.

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2017 Outlook by the Numbers

		2013 (year end)	2014 (year end)	2015 (year end)	2016 (year end)	Most Recent	2017E[1]	Trend
ECONOMY	**Real GDP Growth SAAR**	1.50%	2.40%	2.60%	1.60%	1.20%*	2.20%	
	As has been typical over the last few years, first quarter real GDP rose 1.2% - less than expected. Consumer spending only increased 0.6% after increasing 3.5% in the prior quarter. Consumer weakness was related to a slowdown in automobile purchases and reduced spending on utilities.							
LABOR MARKET	**Unemployment Rate**	7.40%	6.20%	5.30%	4.90%	4.30%**	4.40%	
	The unemployment rate fell to 4.3% in May, its lowest level since May 2001. The drop in unemployment came as many Americans stopped looking for work, pushing the participation rate down. A decline in the number of involuntary part-time workers lowered the U6 to 8.4%, the lowest level since 2007.							
	Payroll Employment	193k	251k	229k	187k	138k**	165k	
	U.S. employers pulled back on hiring in May, adding only 138k new non-farm jobs. Restaurants, health care firms, and construction contributed a large portion of May's jobs. Workers continued to see modest wage growth, with average hourly earnings up 2.5% y/y.							
HOUSING	**Housing Starts**	925k	1,003k	1,111k	1,166k	1,172k***	1,250k	
	U.S. housing starts fell 2.6% in April to an annual rate of 1,172k units, leaving home building at its lowest point in five months. The weakness was led by a large drop in apartment construction, a volatile sector.							
	Building Permits	987k	1,053k	1,178	1,172	1,228k***	1,250k	
	Building permits for future construction fell 2.5% to an annual rate of 1,228k. The decline was driven by a 4.5% drop in the single-family segment while multi-family permits rose 1.4%.							
	Housing Prices YoY	13.40%	4.30%	5.60%	5.30%	5.90%***	4.00%	
	Home values continued to climb in March, up 5.9% y/y to a nearly three-year high. Tight supply continues to put upward pressure on home prices, which are now rising at three times the rate of incomes. More sellers listed their homes in April, but the number of listings was still 9% lower than a year ago.							
INFLATION	**PCE Index YoY**	1.30%	1.50%	0.30%	1.10%	1.70%***	1.70%	
	The U.S. PCE Index rose 0.2% month over month in April after falling 0.2% in March. In the 12-month period ending in April, the PCE price index increased 1.7%. We expect inflation to increase over the next few years as wage gains accelerate due to the tightening labor market.							
	Core PCE Index YoY	1.50%	1.60%	1.40%	1.70%	1.50%***	2.00%	
	The core PCE deflator rose 0.2% in April after dipping 0.1% in March. Despite the increase, the year-on-year rate still decelerated to 1.5%. We expect an upward trend to core inflation over the next few years.							
	Consumer Price Index (CPI) YoY	1.50%	1.60%	0.10%	1.30%	2.20%***	1.90%	
	Following twelve months of gains, consumer prices rose 2.2% y/in April, a deceleration from March's 2.4% rate. Declines in the gasoline and energy indices were the largest factors in April's moderate inflation.							
	Core CPI YoY	1.80%	1.70%	1.80%	2.10%	1.90%***	2.40%	
	Core consumer prices, which excludes volatile food and energy, dropped 0.1% in April after a flat February. Over the past 12 months, core prices have risen 1.9%.							

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2017 Outlook by the Numbers

		2013 (year end)	2014 (year end)	2015 (year end)	2016 (year end)	Most Recent	2017E[1]	Trend
CONSUMER	**Consumer Spending (PCE)**	1.50%	2.90%	3.20%	2.70%	2.60%*	2.90%	
	U.S. consumer spending increased 2.6% y/y in April. Consumer spending will likely remain supported amid the growing optimism surrounding the economy, low unemployment, and rising wages.							
	Consumer Confidence (U of MI)	79.2	84.1	92.9	91.8	97.1**	96.0	
	Measures of consumer confidence for May rose slightly to 97.1, lower than market expectations of 97.6. Consumers' attitudes about economic conditions remain favorable despite the retreat, due largely to division among political party lines.							
INTEREST RATES	**Projected Fed Funds**	0.25%	0.25%	0.50%	0.75%	1.00%**	1.50%	
	We believe the Fed will raise the Fed Funds rate three times in 2017, reaching 1.5% by year-end. Fed rate increases are a positive reflection of the improvement in economic conditions, but at the same time tighten financial conditions.							
	Projected 10-Year Treasury	3.00%	2.17%	2.30%	2.44%	2.20%**	3.00%	
	The 10 year Treasury yield will likely be driven by increasing inflation expectations from an improved fiscal policy outlook. We expect the 10 year Treasury yield to trend higher throughout 2017.							
EQUITIES	**S&P 500 Price**	1,848	2,059	2,044	2,239	2,412**	2,440	
	The market continues to trade near highs as investors weigh the potential economic and earnings benefit of a more growth-focused fiscal policy from the Federal government under the new administration. We believe returns will be in the upper-single to low-double digit range over the next 12 months.							
	S&P 500 Operating EPS Growth	6.80%	6.30%	-3.30%	0.00%	17.72%*****	15.00%	
	We believe earnings will grow by 15% y/y in 2017 as the drag from the energy sector wanes. There is meaningful upside to our earnings estimates if we get corporate tax reform sometime in 2017, as the S&P 500 effective tax rate is around 28% compared to proposals of 15-20%.							
GLOBAL ECONOMY	**World GDP**	3.30%	3.40%	3.10%	3.10%	2.90%*	3.20%	
	Global economic growth continues to be subdued at around 3% given secular challenges, such as a slowing labor force population, weak productivity, and high levels of debt. We feel political risk is waning, which is beneficial for economic growth.							
	Emerging Markets GDP	5.00%	4.60%	4.40%	5.40%	5.10%*	4.60%	
	Emerging market growth has been pressured as commodity prices have been weak and China is attempting to stimulate its economy. We believe the recent rebound in commodity prices could help stabilize growth. China continues to be the economic growth engine in the emerging markets.							

*Quarter over Quarter Seasonally Adjusted Annualized Rate, as of 1Q 2017
**As of May, 2017
***As of April, 2017
****As of March, 2017
*****Trailing 4 quarters
[1] E=Estimate

Positive
Neutral
Negative

Trending Down
Trending Up
Trending Down
Trending Up

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