Fall
2017

# Spreng Capital Management Inc.

*Spreng Capital Management* is an investment advisory firm with the Securities and Exchange Commission. Founded in 1999 by James Spreng, Spreng Capital has grown to encompass the very best in service and support for our clients.

Our client base is quite diverse. With clients in 25 states, we offer structured, customized investment management for individuals, profit sharing plans, Foundations, endowments and businesses. We are fee only investment managers, receiving no commissions nor do we sell any financial products. We are paid only by the investment management fees of our clients. We advise our clients on financial planning and manage their assets, making recommendations based entirely upon our clients' needs and goals. Everyone on the Spreng Capital team has a vested interest in the success of our clients' portfolios. Our team has a unique blend of experience, youth and business credentials.

Our use of high quality stocks and mutual funds along with investment grade bonds, allows us the opportunity to deliver consistent long term returns. We focus on minimizing risk and volatility, striving ultimately to deliver the very best after-tax returns possible, within the constraints you have established.

There is nothing that signals success more than referrals from existing clients. Our success is a result of our clients' continued confidence in us and their willingness to recommend us to their family and friends.

***"It was the best of times, it was the worst of times"***
***A Tale of Two Cities by Charles Dickens***

Writing well is difficult work, at least it is for me. Attempting to write a newsletter four times a year requires a great deal of research and time. It also requires the "hook" which is what we call the opening line at the beginning of each newsletter. We think that the hook is necessary hopefully to intrigue our readers enough that they will want to read on. Finding the hook is sometimes difficult. It is what made this one so interesting, at least to me, this time. It came to me in my sleep, or actually awakened me at exactly 1:36 A.M. last week. I awakened and the line from Dickens was in my head as clear as could be. As I thought about why that line stuck it became very clear to me. That quote perfectly sums up our current state of political and financial affairs in the 21st century.

The US stock markets have never been at higher levels, ever. Corporate profits have never been higher, ever. Inflation has rarely been so contained for such a long time period. The unemployment rate is below 5% which historically has been the number that economists have viewed as full employment. The last remaining 5% are, unfortunately, typically described as unemployable for a variety of reasons. Interest rates are still at 400 year lows. Technology continues to make our lives easier every day. Now you can speak to a box on your counter top and order your household needs and have them delivered to your doorstep in two days! In the future, we will drive across the country without having to put our hands on the steering wheel or our feet on the pedals. Medicine continues to improve longevity and quality of life with new gene therapy possibly presenting incredible changes. Hip replacements, knee replacements, back surgeries, shoulder replacements and heart bypass surgery were unheard of just 50 years ago. When my mother had cataract surgery 50 years ago she remained in the hospital for several days with sand bags placed around her head to prevent her from moving her head while her eyes healed. Now it is just a routine out-patient procedure. When my father had back surgery for a herniated disc in the late 1970s he was in the hospital for a week. When I had the same surgery in 2012, I went home a few hours after the surgery. My father was fond of saying, "I grew up in the "good old days". People can long for the good old days. I'll take today any time!!!"

| Index | Qtr. | YTD |
|---|---|---|
| DJIA | 4.71% | 13.37% |
| NASDAQ | 5.79% | 20.67% |
| S&P 500 | 3.96% | 12.53% |

But, as Charles Dickens so aptly put it 158 years ago, today can also be viewed as the worst of times. Investors have complained mightily about the "artificial stimulus" that the Federal Reserve has provided over the last twenty

years either by arbitrarily lowering interest rates or through the purchase of government bonds through quantitative easing to pour more cash into the economy. A quick refresher on what quantitative easing really means. The US Treasury needs to borrow money to run the day to day operations of our government. Since we can't seem to live within our means, the Treasury borrows billions of dollars each year. Quantitative easing means that the Federal Reserve, another division of the Federal government, buys the Treasury bonds. The fact that the Treasury can print the money out of thin air, sell bonds to "pay" for this paper money and oh by the way, another division of the government is buying these bonds or promises to repay, is an absolutely stunning sleight of hand. The irony is that this significant financial maneuvering has worked like a charm! It has provided a way to supply cheap money to consumers, businesses and investors.

While investors grudgingly admit that quantitative easing has been effective, now comes the difficult part, ending it. The Federal Reserve is slowly raising interest rates again. The discussion as to whether the economy can handle higher borrowing cost is not an insignificant exercise. The Fed has announced that they will be raising rates and at the same time, as the bonds that they purchased from the US Treasury mature, the Fed will not buy new bonds to replace the maturing ones that the Fed owns. Therefore, the Fed is trying to extricate itself from quantitative easing in a slow and long process. Will this work? Who will buy the new bonds to replace the maturing bonds that the Fed currently holds? What price or interest rate will be necessary to entice private investors to buy these new bonds and replace the Federal Reserve's trillion dollar investment? All good questions for which no one knows the answers because we have never used quantitative easing as a mechanism to prop up an economy before now.

This is a very serious situation because if there is a consistent action that has killed economic growth in the past, it is the Federal Reserve raising interest rates too much or too quickly. The famous quote attributed to the Federal Reserve's Chairman, William McChesney Martin, is that the job of the Fed is "to remove the punch bowl just as the party is getting started". This is a very delicate balancing act, to use the costs of borrowing money to stimulate, slow down or choke a National economy. We have said many times that today's consumers are addicted to low interest rates. If a potential home owner had to finance at traditional 30 year mortgage rates of 9% a year instead of 30 year mortgages financed at 3.8% a year now, the potential home buyer would have a stroke! Not really, they just would not buy anything that required them to borrow money to purchase the item. Almost every recession that has plagued the US economy since the advent of the Federal Reserve in 1913 has, to some degree, been due to the Fed raising the cost of borrowing too aggressively.

Will the Fed kill the eight year economic expansion that has lifted the US equity markets to record highs? Obviously, the current members of the Federal Reserve Board certainly don't want to be remembered as those who facilitated an eventual recession so they are moving very slowly and cautiously to implement the interest rate hikes and the cessation of buying Treasury bonds. But things have a way of spiraling out of control very quickly in today's fast paced world, especially with instant news broadcast to billions of cell phones around the world. One policy stumble, one ill-spoken utterance in front of an open microphone and things can change extremely quickly. The Fed does need to raise interest rates and to stop buying their own bonds if for no other reason than to give themselves room to maneuver when the next financial crisis erupts. Don't be alarmed by that comment and think that we anticipate another global meltdown like that of 2008. We do not anticipate anything even remotely similar to the mortgage crisis to be on the horizon. But common sense must tell investors that things happen, things for which everyone is ill-prepared, things that stress the global community's ability to respond. Therefore, the Fed needs the ability to respond to these unforeseen circumstances. The only way to do that is to attempt to return to more normalized interest rates while all the while acknowledging that the process of returning to normalized interest rates is itself, fraught with danger and uncertainty for the current state of economic affairs.

With interest rates not even keeping pace with the very low rate of inflation, investors have been forced to take on more risk and to invest in riskier assets just to keep the purchasing power of their money constant. Wages to workers have not kept pace with corporate profits or in response to full employment. Economic theory says that at full employment, wages should rise and employers should have to pay more in wages to entice workers to come work for them. This has not happened for several reasons. The demise of labor unions has left workers with less leverage to pressure employers for wage increases as a group. At the same time, technology has made it easier to replace workers with robots or at least computers with rudimentary artificial intelligence. Robbie Robot never goes on vacation, fights with his spouse, drinks too much the night before or fails to show up on time or at all to work. Robbie just wants a quart of oil or a consistent source of electricity and he is happy. Without increases in

wages over the last twenty years, the cost of all things that we considered "essential" to a pleasant life become much more difficult to obtain. I am hard pressed to grasp why a cell phone from Apple that will be thrown out in three years only because there is something that is newer and cooler, is "essential" to own for only $999.00! I've been accused of being somewhat of a Luddite before so what do I really know about what is essential in today's world. I was always taught that food, clothing and shelter were the essentials. Now I guess that we have to have 100% electronic access all of the time as a fourth staple of life, silly me. But I digress, lack of wage growth is a very serious issue and one that continues to plague our economy and in reality, the pursuit of the American Dream. It is no stretch to link today's political dysfunction to lack of wage growth. There is an angry electorate that has felt left out of the technologically fueled economic growth of the last 25 years, as it appears to them, to have been concentrated in the hands of fewer and fewer people.

The Republican party after 7 years of howling at the moon that if voters would just give the Republicans control of everything, the Senate, the House, the White House then they would have the answers to fix all of our problems. Well after 8 months, they have found out that things are not quite so easy after all. So with that we move on to the next issue, tax reform. We desperately need tax reform. Not trim around the edges, tinker here, modify there, but true tax reform. There are things in the current code that are real impediments to economic growth. We need to find a way to entice corporations to bring back the trillion dollars of profits that were made in their overseas subsidiaries. These profits are just sitting in overseas bank accounts and need to be brought back into the US to be re-invested in plants and people. The corporations do not want to bring the cash back here because they would have to pay a 35% corporate tax on these funds to the US government. They already have paid some tax in the foreign countries in which their subsidiaries are located so obviously, they don't want to pay twice. The Democrats are already screaming that this is a "corporate giveaway" to lower the tax on foreign profits overseas. The last time I looked, a 35% tax on zero dollars coming back to the US was still zero dollars of tax revenue collected. I tend to be an equal critic of both political parties right now. It is pretty easy to do. But once again, I digress, tax reform is hard work and ***must*** be broad enough to actually make a difference. The only way to do this is with bi-partisan support from both parties. The Democrats made a huge mistake, ramming Obamacare down the throats of the American public with a vote entirely along party lines. Remember the classic, "if you like your doctor, you can keep your doctor." How about one of the chief architect's comment that it was marketed to "take advantage of the stupidity of the American voter." And let's not forget the Speaker of the House, Nancy Pelosi's, all-time classic, "We have to pass the bill so that we can find out what is in it." Yes, I know, it is difficult to imagine that there can be any piece of good legislation passed anymore with geniuses like this making policy. But we need tax reform and we need buy-in from both parties to write it correctly and to pass it into legislation. The Republicans will be making a huge mistake just like the Democrats did with Obamacare if they try to pass this along party lines. The Republicans need a win, the Democrats need a win, President Trump needs a win, and the American people need a win. One can only hope that Congress and the President can put petty partisan politics aside and actually pass legislation that is good for the citizens and for our economy. As a side light, everyone seems to hate their Congress as evidenced by Congress's low approval rating. Yet incumbents are overwhelmingly re-elected in every election cycle. Blame gerrymandering, lobbyists with easy cash or just plain "my guy is ok, it's yours that is the bad one." Either way, the average margin of victory for incumbent Congress people in Ohio in the 2016 election was ***36 percent***! The closest re-election for an incumbent was still a whopping 18% margin of victory. No wonder they are not exactly responsive when voters ask for more from their elected officials. Why worry, when it is all said and done, they will be re-elected in a landslide.

The markets have done very well for the first 9 months of 2017. Should the markets prove to be stagnant over the next 3 months, it still would be considered a good year. It is interesting that in our last newsletter we discussed the Amazon Effect and how dangerous it may be for the overall economy. In the last three months, there have been a great deal of articles and videos discussing Amazon and even indicating that it may be in everyone's best interests if the Department of Justice were to investigate Amazon for anti-trust violations. There was a great article by Professor Scott Galloway of NYU talking about how Amazon has changed the rules for investors by not making any profits but offering the panacea of perpetual and unlimited growth. These investors have been dazzled by the thought of eternal growth. Historically, investors would have demanded by now that Amazon turn their growth machine into a profit machine for the owners/investors. Amazon eventually has to make some profit somewhere, don't they? Amazon basically got Whole Foods for free. Amazon stock was bid up in value more than the $13.7 billion that they paid for Whole Foods in just the first day of trading after the purchase was announced. Amazon did not even announce how they were going to

*Americans spent over $80 billion on lottery tickets in 2016. This is more than was spent on movies, video games, music and sports tickets combined. West Virginia and Michigan rely on lottery spending for 35% of their state revenues. Ohio takes in 10% of state revenues and North Dakota the least at 2%.*

integrate Whole Foods into their strategy. They just announced that they bought it and their stock just soared. Imagine just trying to compete with Amazon when they make very little profit, while your investors will crucify your company's stock if you miss earnings by a penny per share. Investors literally give them money for free to pursue any adventure Amazon thinks sounds interesting to try. Amazon has been a phenomenal story, but there is a dark side to their success that awaits a final chapter.

The two recent horrible hurricanes and the damage done will tend to adversely affect economic data in the short run. Lost productivity due to the storms will show up in the data and may cause some short term volatility in the markets. This odd data should be replaced in the long run with better numbers as the cost of repair and rebuilding the affected areas passes into labor and products consumers will need to rebuild.

North Korea is still a very real danger, not just for economic reasons but for the entire world. We were pleased when it was announced just yesterday that the US and North Korea have set up back channels and are at least talking to each other. We will keep our fingers crossed that the dialogue is allowed and will be productive

We had a wonderful time at our Annual Client Appreciation evening in September. We had close to 300 clients and their families and friends in attendance again. We know that we had a great time seeing and visiting with everyone and from the responses and emails that we received, it appeared everyone else had a good time as well. As of right now, we will plan on doing this again next September. We hope that you will be able to join us.

We are excited and optimistic about the future both for you and for our firm. We continue to receive large influxes of new funds thanks to you and your many referrals that we receive every month. No one said securing a viable financial future is easy; nor should it be. There are many challenges and headwinds that we will face every day. The markets contain risk and they offer reward. Our task is to balance the two and to deliver good returns with an acceptable amount of risk.

If you have questions about your holdings or about the general condition of the economy, please contact us at once. If we do not have a current email address for you would you please email us and allow us to add you to our regular list of clients with whom we correspond. Our email addresses are jspreng@sprengcapital.com, tbrown@sprengcapital.com and lemory@sprengcapital.com Please be assured that we are monitoring market situations at all times.

***If there have been any changes in your financial circumstances of which we should be made aware, please notify us at once. If you would like a copy of our most recent Form ADV or our Privacy Policy, please call the office.*** If you have not visited our website, please do so at www.sprengcapital.com

We appreciate the opportunity to work with you, your families and your businesses. We are very grateful for the many referrals that you have provided to us. We can think of no greater compliment than to have you recommend us to your family and friends. We will continue to do our very best to provide you with healthy, consistent returns with a minimum of risk. Always remember, "Investing is a marathon, not a sprint." ***"Risk means more things can happen than will happen!"*** Elroy Dimson-London Business School

***"Investing is a marathon, not a sprint."***


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