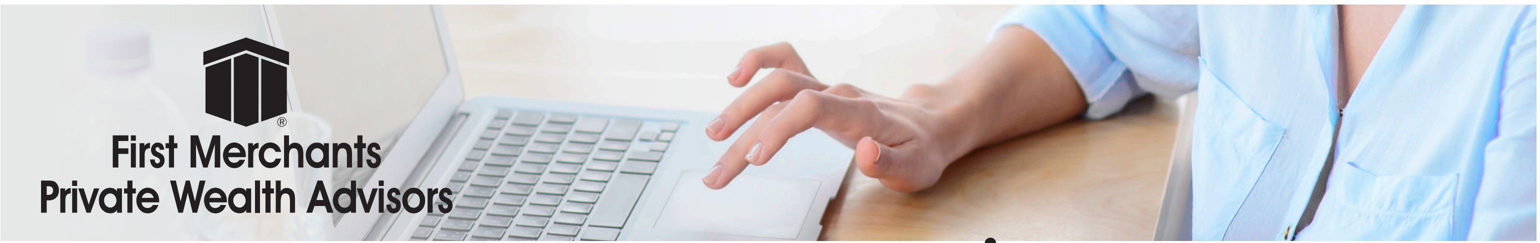


PRIVATE WEALTH *perspectives*

VERSION 17.2

Welcome to the second edition of Private Wealth Perspectives. We are excited to utilize this format as a means to provide timely updates and insights on all of our wealth management disciplines. In the current edition you will receive market and economic insights from Research Director, Jamie Wright, a 'never to early' primer on tax preparedness from Director of Trust Administration, David Forbes and an invitation to dream about what's possible for your home from Nancy Leming, our Director of Private Banking.

We sincerely appreciate your business and partnership. My door is always open to your thoughts and feedback on how we can continue to help in your pursuit of a secure financial future as well as how we can make our communications as impactful as possible.

Cheers to your continued success.

INVESTMENT MANAGEMENT

Inflation, Investment Markets, and the Federal Reserve

In our January communication, in the face of a potentially inflationary scenario of Tax Reform, ACA reformation, deregulation, and increased infrastructure spending we went out on a limb and predicted that commodity prices would not rise and that our economy would continue to tend towards deflation, not inflation. Unfortunately our scenario is still intact.

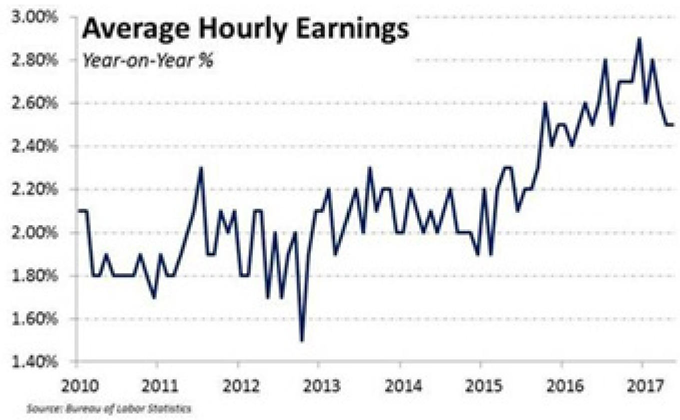
The April Personal Consumption Expenditure Deflator (PCE), the Fed's inflation measure of choice, was reported growing at a 1.7% year-over-year rate, down from 1.9% in March, below the Fed's target rate of 2% and making their prediction of a 1.9% rate by the end of 2017 looking increasingly unlikely. We doubt this report will deter the Fed from increasing short term rates by 0.25% at it's meeting in two weeks, but does call into question increases for the remainder of the year. Most Governors had voiced that three raises were in the cards for this year. If they do pass in June, it will indicate they see the recent slack in the economy as more widespread than most believe.

Both CPI and the PCE rose in January and February, but were likely due to increasing gasoline prices passing through the economy. We believed that once those increases were passed through, we would return to a lower-than-consensus rate. Though OPEC declared an extension of its production cuts a few weeks ago, the day it was declared crude prices fell by 4%. Oil market participants didn't believe that the cuts would make a dent in storage and/or supply, and it hasn't. The United States, long the global leader in technology in Health Care and Information Technology, has used extraordinary technological advances in crude production to not only reduce their cost of production, but by those means to also become the marginal global supplier. The days of Saudi Arabia and their OPEC compatriots controlling the oil markets and setting prices are done (this is not a good thing; lacking income from their basic means of GDP may severely distress their societal structures at some point).

We still maintain that labor-cost inflation is a ghost from the 60's and 70's, when labor unions forced wage costs to spiral out of control, causing cost-push (as opposed to demand-pull) inflation. A 4.4% unemployment rate notwithstanding, it is difficult if not impossible to see labor costs rising at anywhere near those rates, or at rates sufficiently high enough to cause an inflationary spike . While the costs of a skilled CAD/CAM operator may rise due to a shortgage of other skilled operators, it takes scores of same to collegially force employers to raise wages en masse. That is not in the cards. As well, though many employers of lower-wage employees bemoan the fact they can't find help, it's not new. One only has to go back to the 90's to find McDonalds advertising college assistance to new employees on their street signs rather than a special on Big Macs.

The chart below shows a reasonable rise in Average Hourly Earnings for a period of time, but more in keeping with the fairly strong increase in employment in the same time frame. As employment growth has slowed the last several months, so have gains in earnings. This is not necessarily a correlation with strong roots, but it seems to make more sense if one were to believe that many jobs created the last few years were more menial than significant. In other words, service workers attempted a one-day walkout in support of wage increases a few months ago. The next day they were back at work. We don't recall that happening at Deere or Caterpillar for many years.

Copper and iron ore prices continue to trend lower, as China's spectacular growth for three decades continues to wane. We continue to view commodities as more of a short-term bet than an investment of enduring quality. In our view, enduring quality resides in the balance sheet and cash flow statement of a business that cheaply produces things people want or need, not the long-cycle gyrations of commodity prices.



The Employment Report Friday was much weaker than expectations (138,000 jobs versus expectations of 182,000), but the downward revisions to the original March and April reports were very unhealthy. Gains in March were revised from 79,000 to 59,000, while gains in April were revised from 211,000 to 174,000. Where two years ago the three month average growth rate was close to 280,000, this report and the revisions are closer to 121,000. Still growing, but obviously in a less positive manner.

So where does this leave us? We do not see a recession in the cards. A slowing from very feeble rates of growth maybe, but a recession that would cause market disturbances, no. As Joseph Schumpeter said, “Booms create busts.” Economies that grow beyond their potential for some period of time are much more prone to the boom/bust cycle than is the economy that limps along at a Fed-supported 1.8% rate for eight years. And it appears the current Administration’s plans will be mired in Washington’s backwaters for some time; nothing causes running in quicksand faster than a Special Counsel (if you can’t beat them, slime them).

Bond markets are not overvalued; they simply reflect, in real-time, the collective thought of trillions of dollars placed every day on a spectrum called the yield curve. We will continue to believe in the placement of real money that has real consequences over the ramblings of market strategists who believe in an incipient inflation. To believe that wage earners in the U.S. are a more powerful force than a rapidly-aging global population is silly. And nine times out of ten the bond market gets it right.

Stocks are overvalued, by some measures as much as in 1999, before three years of declines erased many billions of dollars of net worth. HOWEVER, that should not imply doom is around the corner. Still-low interest rates around the world continue to lower the average corporate cost-of-capital, earnings have rebounded for two quarters, and business capital spending has begun to accelerate. We will say, to be sure, it does make “risk” markets much more prone to potentially excessive periodic volatility.

Thank you for being a client of First Merchants Wealth Advisors. Michael Joyce has assembled a cast of professionals capable of solving problems, setting a financial course for you, your family, and your business, and being a partner with you and your family for generations. Please call or email at any time with questions or concerns. In the meantime, best regards…

Jamie D. Wright, CFA

Portfolio Manager, Research Director

First Merchants Private Wealth Advisors

June 5, 2017

TRUST ADVISORS

Private Wealth Advisors can help with your charitable giving

Charitable giving is an important aspect of many people's lives. It may be wanting to help those in need, or to support a worthwhile cause like a church or favorite charity, or simply the desire to share one's good fortune with others. Whatever the reason, current tax law encourages charitable gifts with a tax deduction.

For many charitable gifts, writing a check or simply putting money in the plate is all that is required. However if you are considering making a more significant gift to your favorite charity it becomes important to consider how to best maximize the tax benefits involved.

For outright gifts, using appreciated assets such as stocks or mutual fund shares rather than cash has a real advantage. You can generally deduct the current market value of the asset gifted as a charitable deduction and you do not pay the capital gains tax that you would have owed if you had kept and sold the stock or fund yourself.

Another outright gift option if you are over 70 ½ years old is to make a gift to charity directly from your IRA. The IRS allows direct gifts of up to $100,000 per year from eligible IRA's which is treated as a tax free distribution regardless of whether or not you can itemize deductions. As an added benefit these gifts apply against your Required Minimum Distribution requirement allowing you to reduce your total taxable income.

For more substantial charitable gifts, a Charitable Remainder Trust or a Charitable Gift Annuity are methods that allow you to make a charitable gift that also pays you or a loved one income for life. There are three potential benefits. First, you receive a current income tax deduction for your gift. Second, assets contributed can be sold without capital gains tax. And finally, your favorite charity receives a significant future gift. This is an excellent method of turning an asset such as stock or real estate with large gains but little income, into monthly income and a charitable deduction. A true win – win.

While making a charitable gift is always about helping others rather than yourself, it is always wise to consider the tax implications of the gifts you make. By allowing Uncle Sam to help, you may be able to actually increase your charitable giving. You can truly help others while also helping yourself.

First Merchants Private Wealth Advisors would welcome the opportunity to partner with you to provide comprehensive solutions to your charitable giving goals in pursuit of a secure financial future.

David Forbes

PRIVATE BANKING

Almost Swimsuit Season

That thought came to mind on March 12th. It was then we all, collectively, took our first step toward the season of spring, and sprung our clocks forward. Despite the annual controversy of Daylight Savings Time in Indiana, and the loss of one hour of treasured sleep, we can agree that Spring is one of the most anticipated times of the year. Even you, Snowbird, is not exempt as you fly home to roost back in the Midwest. Spring is the blossoming gateway to summer … fireside conversation, cookouts, family gatherings and living outside the confines of walls and windows. Like clockwork, our minds are keenly focused back to personal health and our homes. Is your home in shape for the season?

I would assess my family in great shape. My husband and I have two active and athletic sons, Aaron and Matthew, ages 21 and 18. Along the subject line of swimsuits, their idea of a home in "great shape" includes an in-ground swimming pool. You and your family may consider a sunroom addition or architectural landscaping to bring the outside in as a way to get your home fit. Perhaps all of the above and then-some are being dreamed about and planned for.

As you consider the shape of your home and the wish list of improvements you would like to make, there are two healthy banking options to help achieve your goal. The first and most traditional vehicle is a home equity line of credit. By accessing established equity in your home, you can easily fund your project at your own pace. Based upon your level of need, lines can be available for up to either five or ten years. The second option is a portfolio line of credit. This financing vehicle properly leverages your First Merchants Private Wealth Advisors (FMPWA) managed assets as opposed to an untimely liquidation of those assets. This line of credit is a great way to finance a project and, either plan for or bridge an upcoming liquidity event. In either case, as a qualifying FMPWA client, you are afforded relationship-based terms through our Private Banking group.

Our First Merchants Private Wealth Advisors team and I look forward to seeing you over the coming year and wish great health to you and home.

Supercharging Retirement Savings with Cash Balance Plans

A Cash Balance plan is a type of retirement plan that belongs to the same general class of plans known as "Qualified Plans." A 401(k) is a qualified plan. These accounts are maintained by the plan actuary, who generates annual participant statements.

Participant accounts grow annually in two ways:

• The company contribution – a percentage of pay or a flat dollar amount – is determined by a formula specified in the plan document, and;

• An annual interest credit. The rate of return is guaranteed and is independent of the plan's investment performance. That rate changes each year but usually is equal to the yield on 30-year Treasury bonds, which has hovered around 5 percent in recent years.

When participants terminate employment, they are eligible to receive the vested portion of their account balances.

Advantages:

1. Cash balance plans help owners with a significant tax deduction for employee contributions, plus generous tax-deferred retirement contributions for themselves.
2. Small business owners also appreciate the asset protection characteristics of cash balance plans: As with any IRS-qualified retirement plan, cash balance assets are protected in the event of a lawsuit or bankruptcy.
3. Further, small business owners like the idea of using cash balance plans to catch up on delayed retirement savings. The age-weighted contribution limits permitted by the IRS allow older owners to squeeze 20 years of savings into 10 … Owners can typically double or triple their deferrals compared with a standalone 401(k).
4. Finally, small business owners see cash balance plans as being more effective at attracting and retaining talented employees compared with a standard 401(k).

Ideal Candidate:

1. **Partners or owners who desire to contribute more than $50,000 a year to their retirement accounts.** Many professionals and entrepreneurs neglect their personal retirement savings while they're building their practice or their company. They often have a need to catch up on years of retirement savings. Adding a Cash Balance Plan allows them to rapidly accelerate savings with pre-tax contributions as high as $100,000 to $260,000, depending on their age.

2. **Companies already contributing 3-4% to employees, or at least willing to do so.** While Cash Balance Plans are often established for the benefit of key executives and other highly compensated employees, other employees benefit as well. The plan normally provides a minimum contribution between 5% and 7.5% of pay for staff in the Cash Balance Plan or a separate Profit Sharing 401(k) plan.

3. **Companies that have demonstrated consistent profit patterns.** Because a Cash Balance Plan is a pension plan with required annual contributions, consistent cash flow and profit is very important.

4. **Partners or owners over 40 years of age who desire to "catch up" or accelerate their pension savings.** Maximum amounts allowed in Cash Balance Plans are age-dependent. The older the participant, the faster they can accelerate their savings.

THE STRENGTH OF BIG. **THE SERVICE OF SMALL.**

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