MARKET REVIEW & COMMENTARY

NOVEMBER 2017

TELEMUS®

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MARKET REVIEW

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November was another good month as equities of all flavors continued their relentless ascent. 'Value' reversed its underperformance versus 'Growth' and most capitalizations and styles in the U.S. experienced strikingly similar returns, perhaps presaging an attempted rotation from 'growth' to 'value'. In a sharp reversal, U.S. equity returns trounced most international equity returns in November. Fixed income was modestly negative across the board. Municipal paper was crushed relative to taxable paper as investors reacted to each nuance of the proposed tax bill. Hedge funds were modestly positive, while alternatives and real assets were broadly mixed.

Specifically, the S&P500 rose +3.07%, while high dividend payers gained +3.56%. Small cap value and growth were up nearly identical amounts, up +2.89% and +2.87%, respectively. Large cap value and growth also performed similarly, up +3.06% and +3.04%, respectively,. Although emerging markets, frontier markets and Europe are some of the year's top performers, their November returns were up only +0.20%, +1.16% and +0.22%, respectively.

International stocks as measured by EAFE gained +1.05%.

Fixed income returns were also remarkably similar across durations, although municipals of all types lost far more than taxable paper. Specifically, 1-3 year U.S. Treasuries were down -0.21% and 1-5 year corporate paper lost -0.30%. Treasuries with maturities of 10- 20 years experienced -0.14% to -0.21% losses, while corporates with maturities of 1-10+ years lost between -0.22% and -0.35%. Two of the best 2017 performers lost ground, possibly marking a digestion period. High yield paper lost -0.25% this month while emerging market bonds dropped -0.81%. On a small bright bond note, TIPS gained +0.13%, while world bonds gained +1.42%.

Alternatives and real assets continue their mixed returns. The HFRX Global Hedge Fund Index gained a slight +0.07%, the Bloomberg Commodity Index lost -0.46%, precious metals lost -0.82%, global natural resources were up +0.89%, and world real estate gained +2.75%. Energy actually gained +1.76% but energy MLP's continued their downward trend, losing -1.35%.

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YEAR-TO-DATE

This has been a wonderful market year and U.S. equities continue their upward march. However, there is a wide chasm between the returns of 'growth' and 'value' stocks. U.S. growth stocks are up between +22.02% (small cap growth) and +29.21% (large cap growth). U.S. value stocks have garnered only one-third of those returns, with U.S. small cap value stocks up +8.88% and U.S. large cap value stocks up +12.03%. The S&P500 has gained +20.49%, high dividend payers are up +17.11% but microcaps garnered 'only' a +13.71% return year-to-date. International markets 'lead' over U.S. markets is rapidly evaporating and international lost further ground in November. EAFE is up +23.06% and Europe is up +23.64%. Emerging and frontier markets however maintain a lead; up +32.53% and +27.86%, respectively.

Short Treasuries are up +0.42%, short credit is up +1.57% and short munis are up +1.34%. The 10-20 year Treasury Index is up +3.54%, Barclays Intermediate Corporate Bond Index is up +3.61% and the Bloomberg/Barclay Municipal Index has gained +4.36% year-to-date. TIPS are up +2.07%, emerging market paper (EMBI) is up +7.61% and high yield bonds are up +7.18% through November.

Alternatives and real assets have experienced varied year-to-date returns. The HFRX Global Hedge Fund Index has logged a respectable +5.22% gain while world real estate is up +13.75% and precious metals are up +3.98%. On the other hand, energy is down -10.75%, the Bloomberg Commodity Index is down -1.24% and the dollar has given up -8.96%.

INDEX RETURNS AS OF 11/30/2017

BASIC INDEX RETURNS

	MONTH TO DATE RETURN	QUARTER TO DATE RETURN	YEAR TO DATE RETURN	LATEST 3 YEARS RETURN	LATEST 5 YEARS RETURN	LATEST 10 YEARS RETURN
BALANCED INDEX (25% ACWI, 60% US Gov. Cr 1-5, 5% HFRX, 5% commodity, 5% bill)	0.29%	0.94%	6.16%	7.58%	16.19%	28.46%
HFRX GLOBAL HEDGE FUND INDEX	0.07%	0.76%	5.22%	3.80%	11.28%	-4.84%
CPI - SEASONALLY ADJUSTED	0.00%	0.11%	1.57%	4.04%	6.74%	16.98%
S&P 500 COMPOSITE	3.07%	5.47%	20.49%	37.36%	107.73%	123.30%
LIPPER LARGE - CAP CORE	2.90%	4.84%	19.24%	32.98%	97.20%	104.39%
WISDOM TREE LARGE CAP DIVIDEND	3.56%	5.33%	17.11%	34.05%	97.05%	114.17%
MSCI ALL COUNTRY WORLD INDEX NET	1.94%	4.05%	22.00%	26.89%	68.07%	53.90%
MSCI EAFE NET	1.05%	2.58%	23.06%	19.34%	48.54%	16.95%
BLOOMBERG BARCLAYS MUNICIPAL BOND 5Y (4 - 6)	-1.13%	-1.16%	2.67%	4.31%	8.27%	41.41%
BLOOMBERG BARCLAYS US AGGREGATE	-0.13%	-0.07%	3.07%	6.60%	10.29%	47.39%
BANK OF AMERICA / MERRILL LYNCH US T - BILL 3MONTH	0.08%	0.17%	0.74%	1.13%	1.24%	4.12%

EXTENDED INDEX RETURNS

	MONTH TO DATE RETURN	QUARTER TO DATE RETURN	YEAR TO DATE RETURN	LATEST 3 YEARS RETURN	LATEST 5 YEARS RETURN	LATEST 10 YEARS RETURN
RUSSELL 1000 GROWTH	3.04%	7.03%	29.21%	46.23%	120.53%	157.85%
RUSSELL 1000 VALUE	3.06%	3.81%	12.03%	27.80%	93.99%	94.88%
RUSSELL MIDCAP GROWTH	3.34%	6.23%	24.59%	34.86%	106.35%	139.11%
RUSSELL MIDCAP VALUE	3.38%	4.22%	11.97%	30.06%	101.08%	134.03%
RUSSELL SMALL CAP COMP GROWTH	2.78%	5.45%	25.80%	39.38%	114.62%	154.31%
RUSSELL SMALL CAP COMP VALUE	2.89%	3.51%	10.67%	32.41%	90.02%	121.98%
MSCI EM (EMERGING MARKETS) NET	0.20%	3.71%	32.53%	21.97%	25.28%	14.37%
BLOOMBERG BARCLAYS US TREASURY BILL 6 MONTH	0.08%	0.17%	0.87%	1.81%	2.14%	7.60%
BLOOMBERG BARCLAYS US AGENCY	-0.15%	-0.14%	1.93%	4.46%	6.48%	32.51%
JP MORGAN EMERGING MARKET BOND INDEX(EMBI) + COMPOSITE	-0.81%	-0.95%	7.61%	17.87%	17.93%	92.45%
CITI GROUP WORLD GOVERNMENT BOND	1.42%	0.88%	7.32%	4.33%	-0.48%	28.70%
BLOOMBERG COMMODITY	-0.46%	1.67%	-1.24%	-24.42%	-39.18%	-49.71%
PHILADELPHIA STOCK EXCHANGE GOLD / SILVER	-2.19%	-6.18%	0.71%	8.62%	-53.34%	-53.72%
LIPPER GLOBL NAT RES	0.89%	0.84%	0.69%	1.49%	2.95%	-21.28%
LIPPER PRECIOUS METAL FUND	-0.82%	-4.46%	3.98%	12.10%	-45.23%	-34.84%
MSCI WORLD REAL ESTATE	2.75%	3.57%	13.75%	16.73%	42.58%	28.99%
LIPPER REAL ESTATE FUND	2.74%	2.58%	6.94%	20.29%	49.75%	59.86%

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November is most known for celebrating Thanksgiving, one of our most cherished holidays of the year. Ironically, this time of year is also associated with the official launch of the Christmas season, the most commercial holiday of the year and pivotal to so many companies that rely so heavily on Christmas sales. However, these two November holiday staples fought for attention with the Mueller investigation, congressional tax legislation, North Korea, and sexual harassment run rampant. Meanwhile, ignoring the political and geopolitical challenges at hand, the domestic equity markets pushed to historic highs on the backs of improved corporate earnings and the increasing likelihood of some form of tax legislation being approved. No run of the mill November for sure! The following provides a closer look at some of the events of November:

Tax Legislation - With the one year anniversary of the Trump administration quickly approaching without any meaningful legislative wins, the GOP is fearful of showing up at the 2018 mid-term elections empty handed and possibly losing control of one or both houses. Accordingly, GOP members are racing to approve the proposed tax legislation in the face of complete opposition by congressional Democrats and meaningful differences of opinions among the various factions of congressional Republicans. Nevertheless, Republicans garnered enough votes to approve their respective tax bills in the House and Senate, which must now be reconciled and put forth for signature by the President. The House and Senate have now begun the reconciliation process and a reconciled bill is expected to be signed into law by Christmas. The GOP has cheered the bill with House Speaker Paul Ryan saying "This bill is the single biggest thing we can do to grow the economy, to restore opportunity, and to help struggling middle-class families." However, trickle down economics has historically proven unsuccessful and over the past several years additional cash in corporate coffers has gone to share repurchases and increased dividends and not business investment, increased wages, or new jobs. Moreover, an objective look at the proposed legislation makes it difficult to identify the provisions that actually provide meaningful help to middle-class families. We should know more by the end of the year and we'll see next year if jobs, wages, and the middle class will benefit.

Corporate Earnings – According to FactSet the estimated earnings growth rate for the S&P 500 for Q4 2017 is 10.5%. All eleven S&P 500 sectors are expected to report growth in Q4. Since the end of Q3 earnings estimates for Q4 have dropped 0.7%, which compares favorably to the average decline in the bottom-up EPS estimate recorded during the first two months of the fourth quarter since Q2 2001. The forward 12-month P/E for the S&P 500 is 18X, assuming a consensus 2018 estimate of $146 of S&P 500 earnings over the next 12 months. This also assumes that current tax legislation passes and corporate taxes are reduced to 20%. Ed Yardeni calculates that the tax rate cut would increase 2018 S&P 500 earnings by about 4.5%. In any event, current valuations on forward earnings are above the 5 and 10-year

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averages of 15.8X and 14.1X, respectively. Broader and more conservative valuation metrics including multiples on trailing twelve months and the Shiller CAPE Ratio reflect far more excessive equity market valuations.

China - Last month we commented about the importance of the 19th National Congress of the Communist Party of China. In particular, Xi Jinping used the 19th Congress to consolidate his power in and to enshrine his name with Mao's in China's history books. Xi's preparation for the 19th Congress began at the beginning of 2016 when the PBOC massively expanded credit to support the Chinese economy when it began to stall in the second half of 2015. This expansion of credit drove growth again and with it happy faces going into the 19th Congress.

As noted last month, with Mr. Xi's "coronation" as the new Mao, it now makes sense for Mr. Xi and the PBOC to follow through with credit reform and resetting expectations for economic growth. This will likely wash out the "walking dead" companies whose lives are sustained by more and more debt. Xi has five years before the next Party Congress, which provides him time to try and fix what he knows is an immensely problematic debt burden. As anticipated, since the conclusion of the 19th Congress China's sovereign bond market has sold off with 10-year yields topping 4% for the first time in three years, before settling at a current yield of 3.9%. China's $3.4 trillion corporate bond market is beginning to feel the pressure as well with AAA corporate yields reaching 5.3%. Unsurprisingly, China's equity markets are down anywhere from 5%-8% from the highs reached shortly after the close of the 19th Congress. We continue to watch these events carefully as global growth is linked closely to the Chinese economy. A ratcheting down of credit in China and the resultant slowing of their economic growth would ripple through the global economy and meaningfully impact equity markets that are discounting continued global economic growth.

Conclusion – In a recent article in The Economist, Brett Ryder summed up the current market environment quite well: "Rarely have so many asset classes – from stocks to bonds to property to bitcoins, exhibited such a sense of invulnerability. And rarely have creditors demanded so little insurance against default, even on the riskiest "junk" bonds. And, rarely have property prices around the world towered so high. Add to this the craze for exotica, such as cryptocurrencies, and the world is in the throes of a bull market in everything." While global growth remains historically moderate, it is on the rise. However, we believe that Ryder accurately describes the current dynamic of the asset markets and our many years of experience dictate a heightened sense of circumspection.

Alas, while we consider ourselves prudent stewards of capital, we have no crystal ball as to when the current economic recovery will wane or when asset prices will re-engage with fundamentals. The markets have proven time and again to swing too far in both directions as fear and greed take hold. Importantly, the markets have taught us the futility of timing such directional changes. As such, we continue to rebalance accounts in a disciplined way by reducing stocks to targets and reinvesting gains in shorter term bonds and alternative investment strategies that should maintain value better in case of a market decline.

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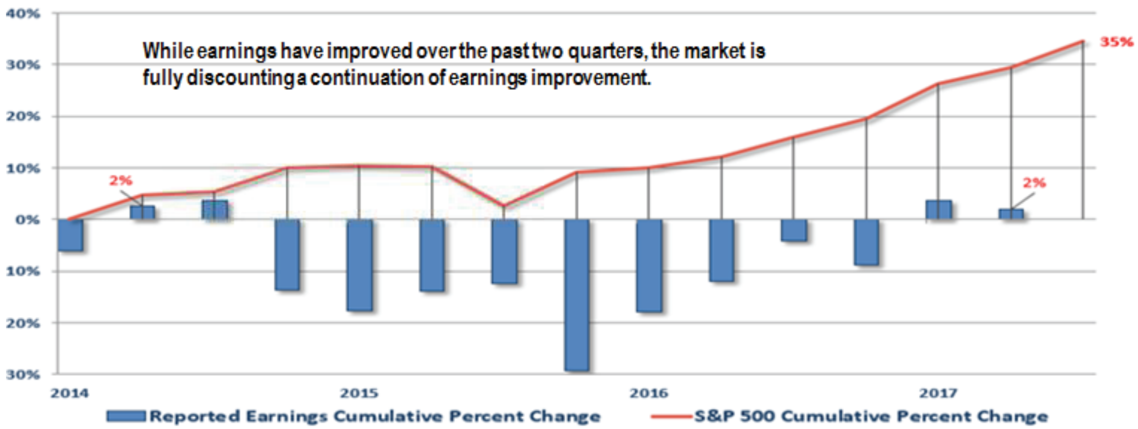

Source: Real Investment Advice

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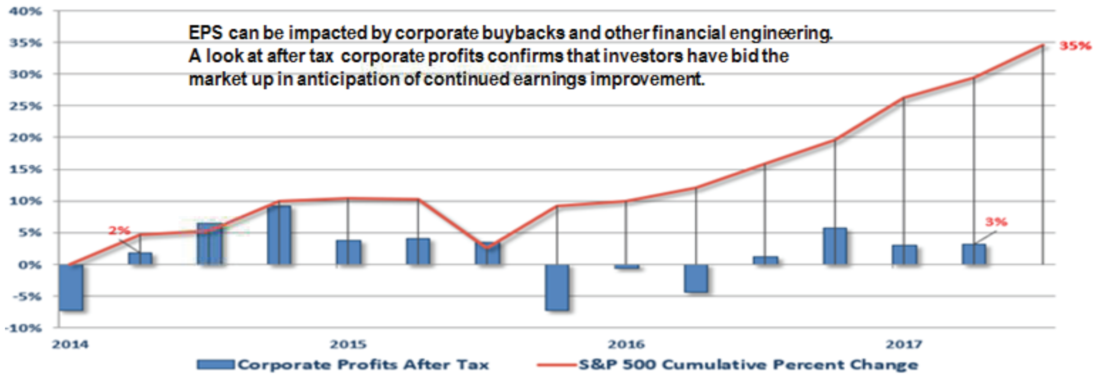

Source: Real Investment Advice

The art market has not been left out of the bull market of “everything” with the November auction price of $450 million paid for da Vinci’s “Salvator Mundi.”

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