February 2017

Stocks ended lower on the last day of the month with Small Caps being particularly hard hit as the Russell 2000 closed down 1.5%. However, that was preceded by the Dow setting a new record on 12 consecutive days, matching the longest such feat with two other times in its 120-year history. Quoting last night's SentimenTrader: "Extreme momentum out of pessimistic conditions is extremely bullish for forward returns. When at an all-time high, not so much."

With sentiment indicators continuing to register extreme optimism, we remain cautious, especially on U.S. stocks. As previously shared, while existing clients remain fully invested according to their Risk Profiles and Objectives, new funds targeting individual stocks are being placed in TOTL, instead of Transitional Funds, as we watch for opportunities. BCA Research from last Friday's Global Investment Strategy's Weekly Report:

"The global economy remains in recovery mode. As we discussed last week, leading indicators point to strong global growth and accelerating earnings over the next six months. This justifies a cyclically overweight tilt towards global equities.

Still, we worry that equity markets have gotten ahead of themselves. We thought that the backup in yields late last year, along with Trump's protectionist rhetoric, would cause stocks to correct to the downside, at least temporarily. Instead, they ripped higher, causing our short NASDAQ hedge trade to briefly go through its 10% stop loss on Wednesday. **("Far more money has been lost by investors preparing for corrections, or trying to anticipate corrections, than has been lost in corrections themselves." -** Peter Lynch)

Our technical indicators continue to point to heightened risks of a correction. Whether such a correction proves to be the proverbial "buying opportunity" – our baseline view – or morphs into something more ominous will depend on the durability of the economic backdrop. ..."

Two articles worth sharing, the first from the WSJ and the second from Morningstar:

It's Like the Financial Crisis Never Happened...

A decade since the U.S. subprime crisis began, and everything's wonderful on Wall Street

By **JAMES MACKINTOSH**

Feb. 22, 2017

It is 10 years since the U.S. subprime crisis began, and everything is wonderful on Wall Street.

A decade after the world began to notice the losses on derivatives linked to the toxic waste of structured subprime mortgages, American stocks have produced such big returns that the biggest crash in generations barely registers.

The 10-year average compound return on U.S. shares was 4.9% a year after inflation at the start of 2016, only slightly below the average for world stocks since the end of the Gilded Age in 1900, according to calculations for Credit Suisse by Elroy Dimson, Paul Marsh and Mike Staunton of London Business School.

The same isn't true for the rest of the world. British stocks made only 3% after inflation, including dividends, in the past decade, while real Japanese returns were barely positive and French shares delivered less than 2%. German stocks weren't quite so bad thanks to its export powerhouses, and their 4.3% return adjusted for inflation is in line with the very long-term return from the world outside the U.S.

This global divergence is covered up by the record highs of global stocks in the past week. On Wednesday morning in London the MSCI All-Country World index (the All Cap version of which is our benchmark) was setting another new high after breaking the 2015 high a week ago.

Look below the headline, and the high is all about the U.S., which makes up more than half of the market value of the global benchmark. Japanese, European and emerging-market stocks all remain below their post crisis highs, let alone their pre crisis highs, in both dollars and local currency.

Delve into the figures and American shares lose some of their shine—although the rest of the world still looks worse. U.S. stocks only beat bonds by 0.3 percentage point a year over the past decade, with dividends and coupons reinvested, far below the long-run global average of 3.2 points a year. That is a paltry reward for the extreme volatility of holding on to risky shares through a crash that wiped out more than half of the S&P 500's value.

British, French, German and Japanese shares were all even worse, with their country's bonds beating local stocks over a decade. Returns on British long-dated bonds are ahead of the FTSE 100 since the Big Bang deregulation of the London stock market in October 1986, while Japanese 10-year bonds—big winners from deflation—beat Japanese shares since at least 1983.

The return on U.S. shares looks better by comparison, but was still worse than the long-run U.S. average of 6.4% a year. Mr. Marsh points out that the U.S. long-term performance is helped by being one of the "lucky countries" not to have been occupied by a foreign power. Other countries beating the world average since 1900 include the U.K. and Sweden, as well as resource-rich Canada, New Zealand, Australia and South Africa.

Mr. Marsh argues that future returns are likely to be lower than in the past. He expects long-term returns, again including dividends and adjusted for inflation, to be below 4% in all the major markets, based on a premium above cash of 3% to 3.5% for holding equities. Because cash, measured by short-term government bills, yields so little, the base is low.

"If you look just at the U.S. [history], you're exaggerating the returns investors could earn world-wide and you're almost certainly exaggerating the return Americans can look forward to as well," he said.

This seems overly harsh; world stocks produced a higher premium over cash from 1900 to now even taking into account two world wars and the 1917 and

1949 confiscation of Russian and Chinese shares, which once constituted a decent chunk of the global market.

It is true that the global order is looking shaky and trade is under attack, while demographics are less supportive of the economy than before. It is also true that U.S. stocks in particular stand at high valuations today, making future gains harder. But the real stock-market lesson of the past century is that the key to solid performance is to avoid dictatorship or a catastrophic war. Fingers crossed.

Beware the Pessimists!

By John Rekenthaler | 02-24-17

About Those Fedcoins
My wife's friend was frantic. According to a video posted by *The New Yorker*, cash as we know it may be scrapped, replaced by electronic "Fedcoins" that would become the global currency. This, suggested the video, might lead to the Federal Reserve's failure, which would have cataclysmic effects on global stock and bond prices. What did I think?

What I thought was that it was remarkable that such a huge event had escaped my attention. Google searches revealed: The concept of Fedcoins has been advanced by bitcoin enthusiasts. There is no *New Yorker* link. Smaller, more-exotic websites (for example, theeconomiccollapseblog, which also wonders "Why is NASA Using the Discovery of 7 New Earth-Sized Planets to Promote the Idea that Alien Life May Exist?") have expanded those musings into likelihoods. And gloomsayers have made their prediction.

Here a Crisis, There a Crisis
The gloomsayer who caught my acquaintance's eye was one Doug Casey, whose books' titles reveal his themes. "Crisis Investing: Opportunities and Profits in the Coming Great Depression" (1979); "Crisis Investing for the Rest of the 90s" (1993); "Totally Incorrect" (2012); and "Right on the Money" (2013). Totally incorrect, yes; right on the money, not so much. Although it's true that a deep recession followed his 1979 book, any advice other than to buy mainstream stocks and bonds was wrong for the upcoming decade. As for that impending 1990s crisis… was 15 years too early?

The bogeyman needn't have been Casey. There's no shortage of those who have made their livings by forecasting woes that never arrived. Bob Prechter expected the Dow Jones Industrial Average to hit 400 in the late 1980s; 30 years later, he continues to stand by that very same prediction (you would think he would adjust for inflation, but no), only the date has been bumped to 2021. In 2011, ex-mutual-fund manager Harry Dent foresaw the Dow dropping to 5,000 (better than 400, I suppose). Then there was the Reverend David Wilkerson. Gulp.

The track record of betting against America, to use Warren Buffett's phrase, has been abysmal. It floundered in the 1950s. It misfired in the 1960s. It succeeded frequently in the 1970s. It flopped in the 1980s. It bombed in the 1990s. It was hit-and-miss during the Oughts. It has sputtered in the 2010s. For the seven decades, the score reads as one clear victory, one mixed result, and five failures.

That is a whole lot of wrong. While no single Cassandra moves a great deal of money, the breed as a whole has caused hundreds of billions of dollars of damage. True, one investor's loss is another investor's gain;

effectively, retirees who cripple their personal finances by selling low and watching the markets go high enrich those who take the other side of those trades. The overall economy is untouched. But much misery is created.

Running Scared

The question arises: Why do people still listen? Why does my wife's friend listen to variations of arguments—the collapse of the U.S. dollar, a crisis at the Federal Reserve, rampant inflation—that have fizzled, year after year, decade after decade? Why would an intelligent, highly educated, and well-informed person believe sweeping arguments that rely on a mountain of speculation and a molehill of data?

Three reasons, two of which relate to age.

One, the pessimists *were* largely correct in the 1970s. Terrible bond returns, the 1973-74 stock-market crash, and surging inflation ensured that, during the middle of the decade, just about every U.S. investor lost purchasing power. The rare exceptions were those who fled the mainstream, finding sanctuary in hard assets and cash. Those who are old enough to have invested during the 1970s have difficulty shaking that memory. They fear a new war—and, as with all former combatants, that vision tends to resemble the last war.

Second, fear plays to the elderly. The young respond to hope and greed—day trading, pyramid schemes, double-your-money offers. (Those were my father's idea of "investing.") The way to separate them from their money is to convince them that life is surprisingly easy. There are shortcuts that others just haven't figured out. It's the opposite with the old. They are all too willing to believe that the world is degrading. Tell them that their fears are correct. The cataclysm really is coming.

The third is politics. I've written before how right-wing talk radio hosts impoverished their listeners by persuading them to sell stocks during Barack Obama's presidency, because the Democrats would bring financial ruin. Uh-huh. My acquaintance has the opposite problem: She dreads the "Trumpocalypse." Different party, same diagnosis.

Most of you, I realize, need no prompts to ignore the prophets. After all, you are reading this article, not that one. For such readers, treat this column as a friendly reminder to stay on the straight and narrow path. And consider the possibility of sending it to friends of a certain age who are feeling insecure about the financial markets, and might be prone to being sold a scare package. If this article helps to prevent such an action, it will be among my more useful deeds.

(Note: Yes, I myself sounded a cautionary note in January's column, "Is the Contrarian Bell Clanging for Stocks?" But there's a world of difference between ruminating that perhaps—or perhaps not—stocks are due for a temporary loss, and claiming with apparent certainty when and how the market will suffer a catastrophe.) ...

John Rekenthaler has been researching the fund industry since 1988. He is now a columnist for Morningstar.com and a member of Morningstar's investment research department. John is quick to point out that while Morningstar typically agrees with the views of the Rekenthaler Report, his views are his own.

John Rekenthaler is Vice President of Research for Morningstar.

Positions

ANGIX - 5% positions for a client focused on Income and a new client seeking a balance between Capital Preservation, Appreciation and Income. This "Fund seeks the best risk-adjusted opportunities in fixed income that offer the potential for both stable, monthly dividends and price appreciation. The Fund employs a top-down strategy to identify relative valuation opportunities within the structured credit markets and a bottom-up credit selection process to selecting individual issues. The managers will invest opportunistically across a wide range of credits and issuer types based on relative value within fixed income. Specifically, the Fund targets opportunities in:

- Non-Agency Residential Mortgage-Backed Securities (NA RMBS)
- Commercial Mortgage-Backed Securities (CMBS)
- Collateralized Loan Obligations (CLO)
- Asset-Backed Securities (ABS)
- Agency Residential Mortgage-Backed Securities (RMBS)

Currently, the Fund has a bias towards credit and low duration assets to manage interest rate risk. ...

Its "$1.0 mil Min. Inv." doesn't apply to RIA clients.

AWP - We would have preferred to sell this CEF for the client focused on Income prior to year's end, but its discount to NAV was over 17%. With the discount subsequently narrowing to just over 14%, a level more than 2 standard deviations below its average discount (1-Year Z-Statistic of 2.69), it was time to sell.

Alpine Global Premier Property AWP

Add to Portfolio | Get E-mail Alerts | ? Data Question

Quote | **Chart** | CEF Analysis | Distribution | Performance | Ratings & Risk | Portfolio | Management & Fees | Ownership | Filings

Last Price $5.49 | **Day Change** ↑0.01 | 0.18%

As of Thu 02/02/2017 9:40 AM EST | USD

Last Closing Share Price	Day Range	52-WK Range	1-Year Z-Statistic	Market Value	Total Leverage Ratio
5.48	5.48-5.49	4.63-5.90	2.69	468.0 mil	2.26 %

Last Actual NAV	Last Actual NAV Date	Last Actual Disc/Prem	6-Month Avg Disc/Prem	3-Year Avg Disc/Prem	Total Dist. Rate (Share Price)
6.38	02/01/2017	-14.11 %	-16.93 %	-14.51 %	10.95 %

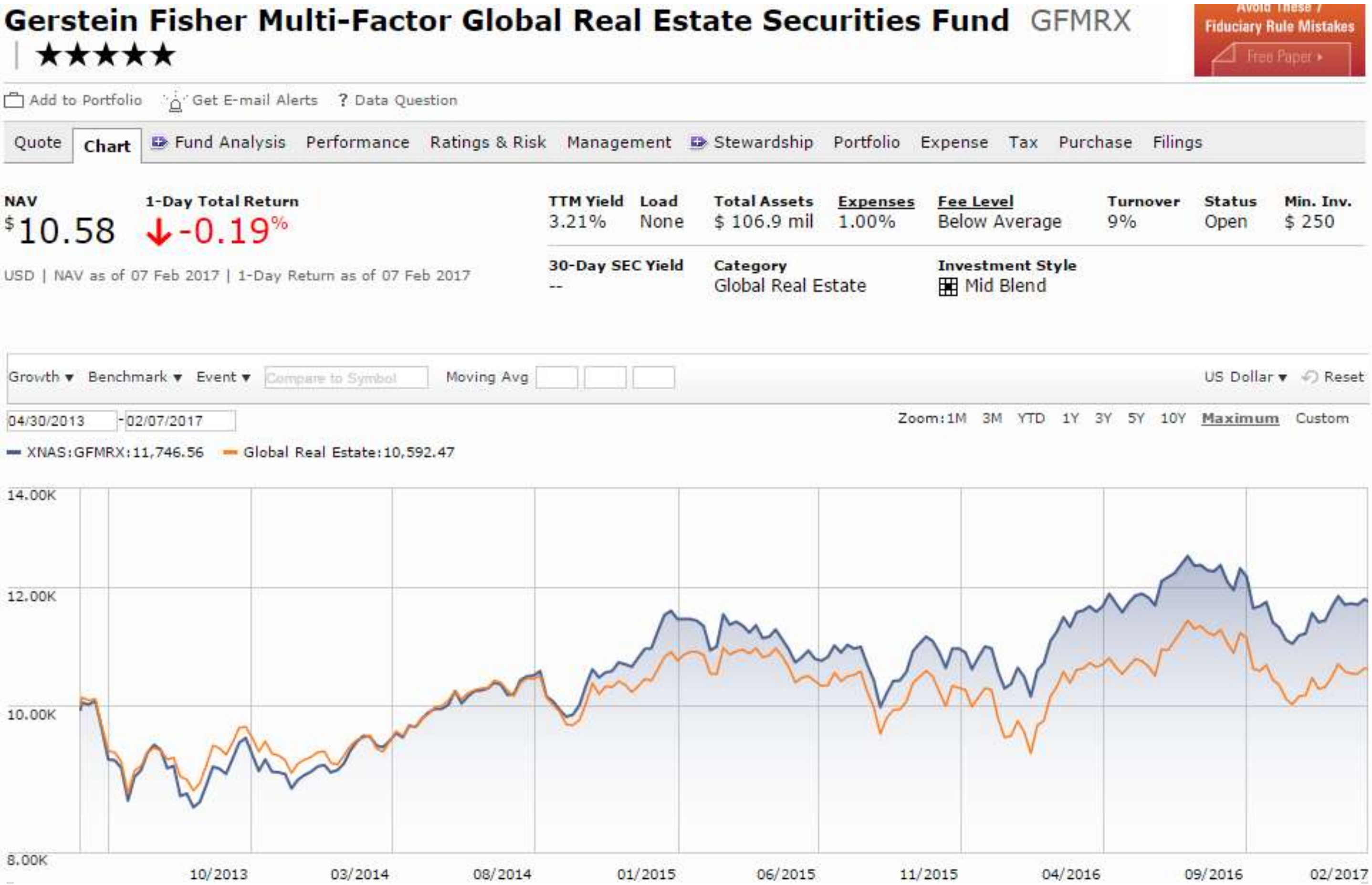
As of 02/01/2017

Benchmark ▾ | Event ▾ | Compare to Symbol | Simple Moving Avg | Reset

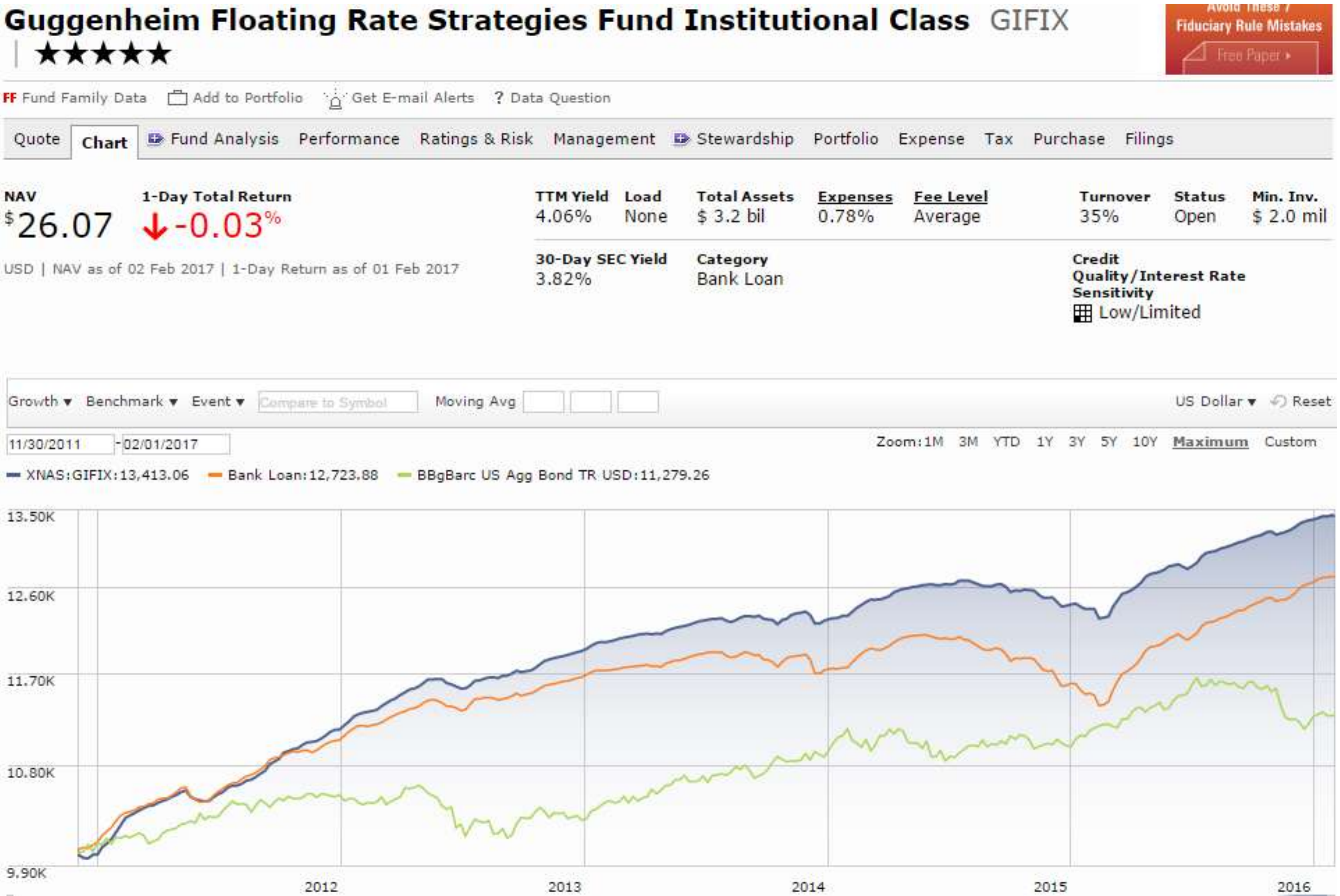
05/23/2014 - 02/01/2017 | Zoom: 1D 5D 1M 3M YTD 1Y 3Y 5Y 10Y Maximum **Custom**

XNYS:AWP: -1.73|-23.99% | Nav: -1.70|-21.04%

GFMRX - A 10% position for our newest client. As previously shared, this is our favorite Quantitative global Real Estate OEF:



GIFIX - In a rising interest rate environment where the Fed isn't attempting to slow the economy Bank Loan Funds become attractive. ETFs should be avoided due to liquidity, and CEFs, while ideal, are currently expensive. This is one of the two best OEFs. The other OEF we track wouldn't waive their $250,000.00 Minimum Investment. Again, 5% positions:



KNOW - The Morningstar chart below shows this Multifactor ETF's performance (blue line) compared to the S&P 500 (orange line). We have previously written about this Quantitative Fund which screens for Insider Buying and positive Earnings Estimate trends with a Value overlay. We use it as both a Core and Transitional Fund depending on the client. In this case a 5% Core holding for the new client:

MTUM - While QMOM is currently our preferred ETF for the Momentum Factor if the client is focused solely on Capital Appreciation, MTUM is the best choice for clients also concerned about volatility and is ideal, due to its low expense and high liquidity, as a Transitional Fund. A 10% Core holding for the new client:

A New Client

With the proliferation of Smart Beta Funds over the last several years, the roster of Funds we are currently using has changed. Here is the HCM portfolio for the new client mentioned above. They transferred 85% of their funds from Quest Opportunity Fund, which HCM is a sub-advisor to:

%	Symbol	Type	Description	Factors (1)	Dist.	(2)	Risk (3)
20	QMNIX	OEF	Global Long/Short Equity-Mid Blend	V, M, Q	2.4%	A	0
10	BIICX	OEF	Global Tactical Allocation		4.7%	M	0.6
5	ANGIX	OEF	Multisector Bond		6.6%	M	0.8
5	GIFIX	OEF	Bank Loan		4.1%	M	0.4
10	GFMRX	OEF	Global Real Estate		3.2%	Q	1.1
15			QOF	I, V, E			1.8
10	MTUM	ETF	US Large Growth	M	1.2%	Q	1.0
5	KNOW	ETF	US Mid Blend	I, E, V	1.4%	Q	1.0
5	IVAL	ETF	Foreign Large Value	V, Q	1.4%	Q	1.3
5	IMOM	ETF	Foreign Large Blend	M, Q	0.9%	S	1.2
10	GPIIX	OEF	Foreign Small/Mid Growth	S, V, Q	4.7%	A	1.7
				Weighted Average:	**2.6%**		**0.9**

Notes	
1	V=Value, M=Momentum, Q=Quality, I=Insiders, E=Earnings, S=Size
2	Distribution Frequency: A=Annual, S=Semi-annual, Q=Quarterly, M=Monthly
3	Ratio of average historical Max. Drawdowns to S&P 500 declines greater than 10%