Financial Services Advisory
GROW WISER®

It Ain't Over—til It's Over
January 8, 2018

2017 was a year to celebrate gains in most stock markets around the world. The S&P 500 index continued to be the favored index, though some international markets also shone after a few years in the doldrums.

FSA is pleased to report gains in all our investment strategies—the best in recent years.

Some observers call this stock market rally "the most hated bull market ever." Even though stocks are up strongly since the lows of 2009, there has been surprisingly little euphoria by investors. All along the way, many analysts have been skeptical that the bull market could carry on, cautioning investors to tread carefully. And still the market continues to climb, in spite of a number of economic and political challenges over the past nine years.

2017 Overview
As we approached 2017, many observers warned that since the bull market was nearly eight years old, the next bear market must be around the corner. And there were reasons for concern. The first year of a presidential cycle is historically among the weakest. Also, the Federal Reserve planned to continue raising interest rates in 2017, which usually leads to more challenging times for investors. And finally, investors were becoming increasingly nervous at the growing political rancor in Washington.

Despite these concerns, stocks managed strong returns for the year with surprisingly low volatility. Historically, over the course of a year the Dow Jones Industrial Average rises or falls more than 1% in a day on average about 30% of the time. In 2017, there were only 12 days when the Dow moved more than 1% (either up or down), which equates to only 5% of the time. We haven't seen such low levels of volatility since the early 1960s.

Stocks weren't the only game in town as bonds also had a decent year. The standard broad bond index rose nearly 4% in 2017, with high yield bonds up almost 6%. These returns are actually quite good given the low level of interest rates, as well as the continued rate hikes by the Federal Reserve.

What to Expect in 2018
While it's very easy to be complacent in rising markets like the present one, our experience has taught us to keep an eye on the ball. Here are some areas of concern that we are tracking as we enter 2018:

- The stock market seems fully valued.
- The stock market has been generally rising for nearly nine years, among the longest advances in history.
- Political uncertainty in Washington, D.C., continues.
- Interest rates are on the rise.

So, a number of factors could create difficulties for investors in 2018. Last year, stocks were helped along in part by the promise of higher profits coming from deregulation and lower taxes for businesses. Now that the tax plan has passed, investors will be watching to see whether that promise pans out or peters out.

Amid these concerns, FSA's approach, as usual, is to follow the market closely and have an exit strategy ready if the upward trend reverses. That said, it's "all systems go" in the meantime as markets continue to rise.

<u>Portfolio Review</u>
Below, we review FSA's six broad investment strategies. Keep in mind that because we manage clients' portfolios individually, the results for your particular account may differ somewhat from the averages.

Income (Strategy 1)
This strategy is a good low-risk alternative to the minimal returns offered by banks and money market funds. High yield corporate and municipal funds provided solid returns, as did the mortgage backed funds we added in the middle of the year. During the fourth quarter we sold the emerging markets bond fund and added the proceeds to the mortgage backed funds we already owned. The portfolios remain fully invested, with a money market allocation below 5%.

Income & Growth (Strategy 2)
This strategy is focused more on generating positive, consistent returns over time. This means it's designed to carry less risk in order to keep losses at a minimum in down years. With overall market trends positive, this strategy is maintaining a fully invested position, with 50% in stock funds and 45% in bond funds.

Conservative Growth (Strategy 3)
This balanced strategy posted solid returns for 2017, thanks in part to strong returns from the international holdings, as well as the high yield municipal fund (for taxable accounts). The overall equity allocation is now 75% (the upper limit allowed for Conservative Growth), with 15%-20% of that in international funds. The portfolios hold 20% in bond funds, some of which are high yield (which tend to move in the same direction as stocks). There is less than 5% in money markets.

Core Equity (Strategy 4)
It was also a solid year for the Core Equity strategy, as it maintained a highly invested position all year. Underneath the surface, we rotated from small-cap and value-oriented areas of the market to growth-oriented areas. Core Equity finished the year with a distinctly growth tilt, which includes technology and transportation sector funds in the portfolios. These portfolios are well positioned if stocks continue to rally in the New Year.

Tactical Growth (Strategy 5)
2017 provided the best returns for Tactical Growth portfolios since 2013. Tactical Growth is our most eclectic strategy and has the widest latitude and flexibility for investment choices. During the quarter, we sold the gold funds and reduced the emerging markets position. That money was redirected to broad market funds, as well as an energy fund. This strategy remains nearly fully invested in stock funds with a money market allocation below 5%.

Sector Rotation (Strategy 6)
Sector Rotation performed as expected given its fully invested nature. Performance was helped by allocations to technology and health care for much of the year. This strategy currently holds funds invested among the following six sectors: basic materials, financial services, transportation, technology, internet and leisure.

Please remember to inform us of any changes in your life that could affect your investment objectives.

FSA Investment Team

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