nVEST nSIGHTS

MARCH 31, 2017

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nvest WEALTH STRATEGIES

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WASHINGTON CIRCUS

Bill Henderly, CFA, Nvest Wealth Strategies, Inc.

Being a circus fan requires admiration for the show under the big top; all the sideshows, and much more. Recently, Ringling Brothers and Barnum & Bailey Circus announced their upcoming closure. For many, that's sad news. One late-night host offered a joking reason for the shocking news: "apparently the circus doesn't think they can compete against a Trump presidency." Funny, but from our perspective the real circus is Washington in general; the biggest show on earth that is disappointing to watch. And generally, sarcastic comments from comedians who repeatedly hammer on a subject, to me, become inappropriate. We all struggle to interpret the latest twists and turns of the circus we call Washington, our federal government.

Recall our March commentary, "Plans of Mice and Men", wherein part of the message reviewed the prospects for a pause or consolidation in the near-term. Aside from the argument that a pause seems overdue following several months of remarkable strength for the markets, new presidents often experience a bad month as they find their "sea legs" and make what are perceived to be policy mistakes. While that did not happen in February, March produced a generally flat result for domestic stocks. As history predicted, new Presidents often "bump a few heads" with Congress that cause the markets to stumble. While a 5% to 10% pullback is not yet revealed, partisan politics as usual in Washington are raising doubts that President Trump will achieve his pro-growth, pro-business agenda that is attributed with exciting financial markets since the election (reform ACA, tax reform, less regulations, new infrastructure spending, and etc.). We anticipate additional struggles between Trump and Congress to enact policy changes. These struggles may cause the markets to revalue asset prices. This is normal; yet past presidents ultimately learn how to work with Congress and progress ultimately occurs. Pro-growth, pro-business policies will be enacted, but will probably look different than pledges made during the campaign.

The 1st quarter (2017) was encouraging and investor friendly. The S&P500 was up +6% and the NASDAQ jumped +10%. January and February were particularly strong while March was generally flat for domestic stocks; to the surprise of many, Foreign stocks beat domestic by +3% in March. Since 1950, there are 26 instances where both January and February were positive. In 24 of those times, the full year ended positive. Yet, there was usually a pause/correction of roughly -10% along the path of what a year being firmly positive overall. Further, when the 1st quarter generated a return of +5% or more, both 2nd quarter and 3/31 – 12/31 results were skewed to the upside versus historical averages – advancing in 2Q another +3% versus historical average of +1.7%; and the rest of the year (9 months) rising +9.6% compared to +6.4% on average (see chart of skew on page 3). We would guess the probability of these historical parallels is highest IF the pro-growth policies are enacted that support enhanced economic growth and rising stock prices. In the short term, a pause to the market advance may exist. Investors need to monitor the Washington circus atmosphere for signs of improved bi-partisan cooperation that promotes continued economic growth. At the moment, investor expectations for the new Administration to advance legislation or regulatory reform of any substance, seems low. The chances for upside surprise, thus, seem rather large.

If domestic political drama weren't enough, there will likely be another round of European referendum elections, or "neverendums" with the coming French elections, followed by Germany later this year.

How long will investors stay with the current 8-year old bull market, helping it continue to advance? Global monetary policy is still easy and accommodative. Fiscal and regulatory relief may also be starting to provide economic benefit. While the US economic expansion is chronologically old, it is not economically old. Given the current low rate of inflation and interest rates, we hear that robust expansion is everywhere (Detroit, Boston, Atlanta, Nashville, Charlotte, Boise, Sioux Falls, etc.), and oil

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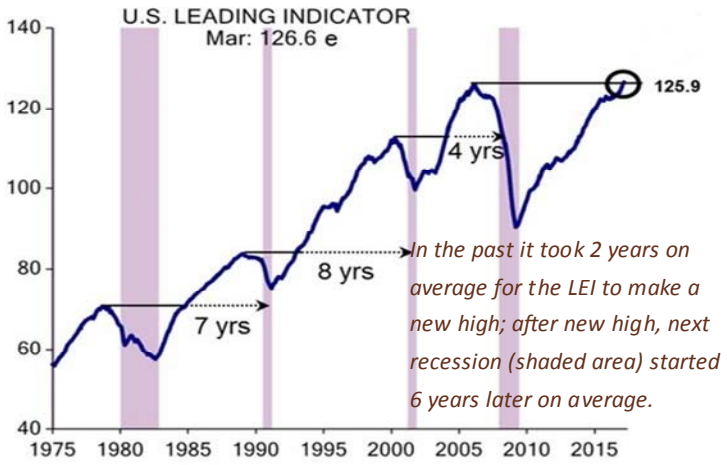
"Historically when the government's index of Leading Economic Indicators (LEI) reaches its prior peak, the next recession did not begin for over 5 years, on average ."

prices are low. Looking at the chart to the right, historically when the government's index of Leading Economic Indicators (LEI) reaches its prior economic peak (just occurred in March), the next recession did not begin for approximately 6 years, on average. It is difficult to describe the market (stocks) with this backdrop as overly expensive. If earnings grow, it precludes the economy being in a recession. Stocks are advancing; they will advance because economic growth and earnings are advancing. Prices will advance further, not on government policy expectation, but because of a growing economic backdrop. That's good! It seems more dangerous to be a long-term bear, than a long-term bull.



"The continued global phenomenon of rising asset values since the beginning of 2017 generally reflects improving fundamentals."

"REFLATION TRADE" OR "TRUMP BUMP"

A *global* economic expansion appears to finally be self-sustaining. Led by both the US and China, this looks to be true even if pro-growth policies in the US do not fully materialize. In financial circles, the attractive performance in recent months is being referred to as both the "Reflation Trade" and the "Trump Bump." But while they are often discussed synonymously, they are not the same thing. Late last summer (2016) the stock market started to advance ahead of the election results in November. Remarkably often, the financial markets and stocks in particular, have an uncanny way of correctly anticipating many events before the outcome is known. The efficient "voting machine" (stock market) is one of the government's leading indicators. As the election results developed, the stock market traded with a looking forward orientation – expectations of pro-growth, pro-business policies to bolster the economy filtered into asset prices. The "Trump Trade" largely occurred before, in and around, and post-November elections. But the "Trump Trade" is not the "Reflation Trade", which is now occurring. Reflation is more about a reversion back toward longer-term inflation and growth that is typically associated with healthy, advancing economies following a recession or period of stagnation. Sure, the Trump pro-growth polices will bolster what the "Reflation Trade" is about; pro-growth policies would boost underlying economic growth developments that are naturally occurring. Reflation economic developments will assist the US and global economies to advance.

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The continued global phenomenon of rising asset values since the beginning of 2017 generally reflects improving fundamentals. Unlike recent years marked by very narrow market participation, we are seeing many different asset classes advancing in value – high yield bond prices are making new highs (not likely if economic conditions were deteriorating); cyclical stocks were and will again perform better than defensive names; and basic commodities (iron, copper) are rising in value; to name a few. As employment gains are pushing up wages, both are boosting consumer spending which helps businesses feel confident to invest in new plants and equipment and add to their workforce. Home prices are also rising, which lifts consumer spending and encourages more construction. Of course, corporate profits play an important role, as they support higher stock prices. These conditions create a wealth effect and self-sustaining expansion. In recessions, these same economic vectors create negative feedback loops which prompt policymakers to stimulate, which seems to no avail like "pushing on a string." In latter stages of a self-sustaining expansion, policymakers tighten, which also seems too late at first and of no avail. The US economic backdrop is now in a self-sustaining expansion mode, where reflation will boost profits and stock prices for a while longer.

In addition, the current bull market has room to run because the international economic backdrop is starting (at an earlier point) to show self-sustaining expansion. China is massive. Employment in China increased +13.1 million in 2016 (the US increase was +2.2 million). While China has its share of problems and skeptics, economic growth is on the rebound. Europe is the third leg of the global self-sustaining expansion – and many leading economic indicators reflect improved activity despite Brexit and upcoming political/referendum worries. Japan offers a 4th leg of self-sustaining global

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ANNOUNCEMENTS:

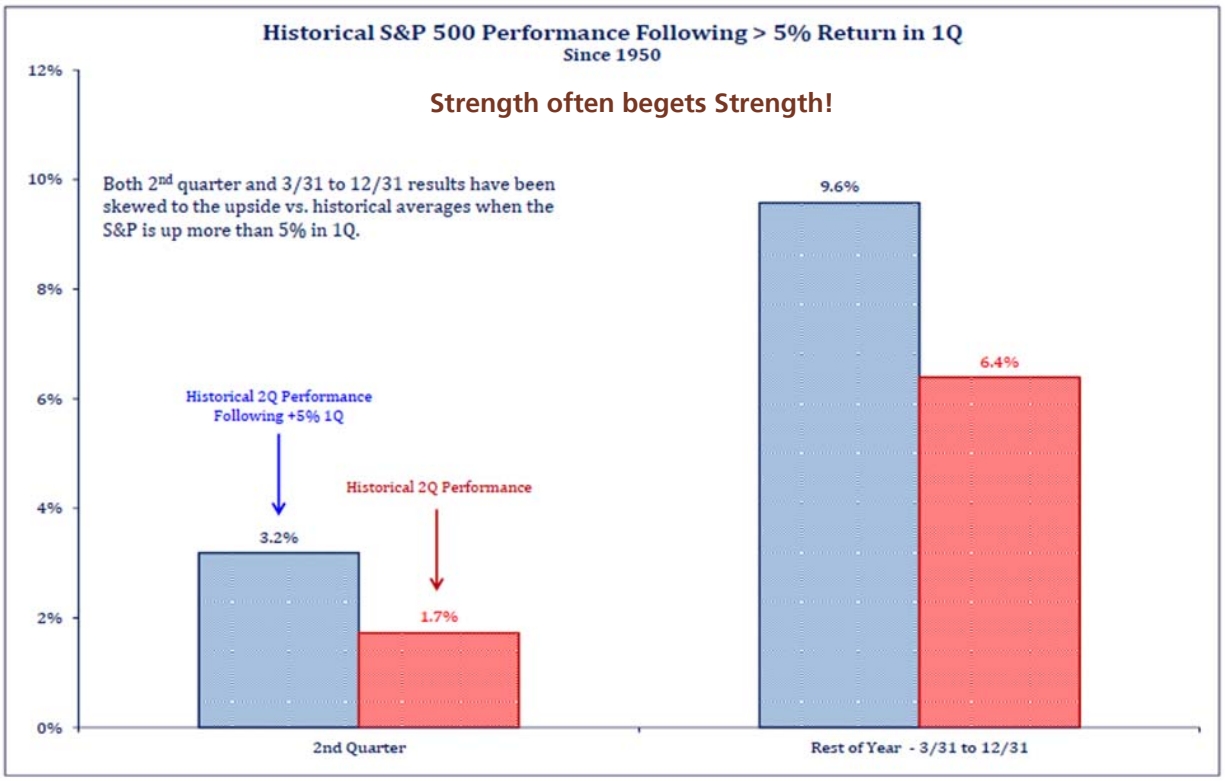
- Early April - 2Q 2017 fees collected. Performance reporting packages sent
- April 14 - Good Friday; financial markets closed.
- April 18 - Deadline to file personal income taxes; Traditional and Roth IRA contributions for the 2016 tax year not accepted after this date.
- May 29 - Memorial Day; banks and financial markets closed
- June 30 - End of 2Q 2017
- July 4 - Independence Day; banks and financial markets closed
- Our ADV Part 2A & B as required by the SEC & Ohio (and other states) is available to you anytime upon request.

BENCHMARKING AS OF MARCH 31, 2017

Summary of index portfolio returns compiled by Nvest Wealth Strategies, Inc.

Index Portfolio	Stock/Bond Allocation		Total Return Through 3/31/2017			
			1st Qtr	12 Mths	3 Years	5 Years
Capital Preservation	0% / 100%	*Cumulative*	0.6%	1.5%	3.0%	6.0%
		Annualized		1.5%	1.0%	1.2%
Income	20% / 80%	*Cumulative*	1.7%	4.4%	5.9%	15.5%
		Annualized		4.4%	1.9%	2.9%
Balanced Conservative	35% / 65%	*Cumulative*	2.2%	5.8%	7.4%	20.5%
		Annualized		5.8%	2.4%	3.8%
Balanced	50% / 50%	*Cumulative*	3.1%	7.9%	9.8%	28.4%
		Annualized		7.9%	3.2%	5.1%
Balanced Growth	65% / 35%	*Cumulative*	3.9%	10.0%	11.7%	35.9%
		Annualized		10.0%	3.7%	6.3%
Growth	80% / 20%	*Cumulative*	4.7%	12.2%	14.2%	45.0%
		Annualized		12.2%	4.5%	7.7%
Aggressive Growth	95% / 5%	*Cumulative*	5.2%	13.7%	15.5%	50.5%
		Annualized		13.7%	4.9%	8.5%

The index returns reflect returns of various mutual fund averages compiled by Morningstar and allocated as follows: Capital Preservation: 90% Bond Average, 10% Treasury Bill Index; Income: 80% Bond, 10% Large Cap, 3% Mid Cap, 2% Small Cap, 5% International; Balanced Conservative: 65% Bond, 15% Large Cap, 5% Mid Cap, 3% Small Cap, 7% International; Balanced: 50% Bond, 24% Large Cap, 7% Mid Cap, 4% Small Cap, 10% International; Balanced Growth: 35% Bond, 30% Large Cap, 9% Mid Cap, 6% Small Cap, 15% International; Growth: 20% Bond, 38% Large Cap, 12% Mid Cap, 8% Small Cap, 17% International; Aggressive Growth: 10% Bond, 40% Large Cap, 15% Mid Cap, 10% Small Cap, 20%



Selected Mutual Funds - Total Return Performance Summary

As of March 31, 2017

Bond Funds - Taxable	Style	1st Qtr	12 Mths	3 Years	5 Years
Taxable Short-Term Bond Average		*0.7%*	*1.7%*	*1.1%*	*1.3%*
Taxable Intermediate Bond Average		*0.9%*	*1.3%*	*2.3%*	*2.4%*
Wells Fargo Ultra Short	AS	0.4%	1.4%	0.6%	0.7%
AC Alternatives Market Neutral Value	AS	2.1%	3.0%	3.8%	3.2%
Vanguard Short Federal	HS	0.4%	0.2%	1.0%	0.8%
American Century Short Duration	HS	0.6%	1.9%	1.4%	1.3%
Pioneer Short-Term Income	HS	0.6%	2.0%	1.2%	1.6%
PIMCO Low Duration	HS	0.5%	1.9%	1.2%	1.7%
Vanguard Short-Term Investment Grade	HS	0.8%	1.8%	1.8%	2.0%
American Century GNMA Income	HI	0.2%	-0.3%	1.8%	1.3%
Diamond Hill Corporate Credit	LI	2.7%	12.2%	5.3%	5.6%
Miller Convertible	LI	1.6%	11.6%	3.4%	6.7%
Bond Funds - Tax Exempt					
Tax-Free Intermediate Bond Average		*1.3%*	*-0.5%*	*2.3%*	*2.1%*
Vanguard Muni Limited Term	HS	1.1%	0.3%	1.2%	1.2%
T. Rowe Price Tax Free S/I	HS	1.1%	0.1%	1.1%	1.2%
Vanguard Muni Intermediate Term	HI	1.4%	-0.1%	2.9%	2.9%
Vanguard Ohio Long-Term	HL	1.3%	0.4%	4.4%	3.9%
Stock Funds - Domestic					
S&P 500 Index		*6.1%*	*17.2%*	*10.4%*	*13.3%*
Equity Fund Average		4.8%	*16.5%*	*6.3%*	*10.4%*
Schwab Large Cap Growth	LG	8.6%	16.6%	10.8%	13.4%
Parnassus Endeavor	LG	4.1%	25.5%	14.6%	16.5%
Sit Dividend Growth	LV	5.3%	13.6%	8.8%	11.4%
Hennessy Focus	MG	4.5%	9.8%	9.0%	13.1%
John Hancock Disciplined Value Mid-Cap	MV	4.2%	20.0%	10.0%	14.9%
SPDR S&P600 Small Cap Growth	SG	2.4%	24.6%	10.0%	14.4%
Neuberger & Berman Genesis	SB	3.0%	19.7%	7.2%	11.4%
Diamond Hill Small-Cap	SV	0.8%	14.4%	4.3%	10.8%
Wells Fargo Small-Cap Value	SV	3.4%	29.9%	5.4%	9.2%
Stock Funds - International					
Morgan Stanley EAFE Index (Foreign)		*7.8%*	*11.6%*	*0.9%*	*5.9%*
Oakmark International	LV	9.4%	21.7%	2.2%	9.0%
John Hancock International Growth	LG	10.8%	7.9%	4.0%	8.6%
Thornburg Developing World	LG	8.3%	7.5%	-2.9%	2.0%
Harding Loevner International Small Company	SG	9.2%	9.9%	1.4%	7.6%
Hennessy Japan	LB	5.6%	16.7%	12.4%	13.0%
Stock Funds - Specialty					
Salient-Forward Select Income (REIT)	MV	0.9%	11.9%	7.2%	8.9%
Neuberger Berman Real Estate Securities	MV	3.3%	2.3%	8.4%	7.9%

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Continued from page 2: "REFLATION TRADE" OR "TRUMP BUMP"

expansion as reports show export and land prices hitting 9-year highs. From an asset valuation risk/reward perspective, both Japan (in particular) and Europe arguably offer better return prospects than domestic stocks. Pro-growth, pro-business strategies of a new administration (if implemented, or in part) only help that outlook even if they accomplish nothing more than promote heightened business and consumer confidence. They further boost the outlook for the domestic economies, and should boost company stock prices. Reflation fundaments are thereby more important, as they support rising asset values. Not to be appearing too rosy, there are certain to be times in coming months wherein some economic data will appear soft, or the pro-growth agenda appears unlikely. Geopolitical tensions rising (such as recent events with Syria and Russia, North Korea) or other unforeseen shocks could also cause asset prices to pause and/or draw down. But a recession or bear market drop is not part of this outlook so long as economic and corporate fundamentals remain advancing.

It was stated, "profits are an opinion; dividends are a fact." S&P dividends increased at 7.7% quarter over quarter (annual rate) in the 1Q2017, and +6% year-over-year. From the prior peak in 2007, dividends increased +64%. Companies do not increase dividends unless they feel confident they can support the payment in the future. Nothing is more suicidal to a company's stock price than cutting a dividend. Investors lose confidence in management's lack of foresight when they reduce dividend rates. It is for this reason that profits regularly vary, but dividends are generally slow to change. The point is, real growth is believed to be self-sustaining; it appears to be turning up. And that is an important idea to keep in mind, and invest for the long-term.

PERSONAL FINANCE: RETIREMENT DOORSTEPS

Can you picture what your life looks like in retirement? During working years, most talk about someday retiring. We anticipate what life would be like without needing to work to support self and family. We look forward to enjoying the luxury of time without punching the old time clock. Instead of being a "people-at-work", we look forward to enjoying life with our "money at work." Retirees often express surprise in retirement when they discover the true luxury of time and the flexibility to pursue hobbies and interests. Today, retirement is viewed as more "active", more "purpose-filled". "Active" is not a requirement; but often it allows one to discover they are in charge of their routines - not their boss, their clients, nor their children. The most exhilarating surprise is the freedom of how to fill your own schedule, rather than vice versa.

Despite how much time people consume dreaming of retirement, studies reflect a growing savings crisis. According to one study, 52% of American households are at risk of being unable to maintain their standard of living in retirement (up from 45% in 2004). This savings crisis exists because most fail to save in earnest until being on the doorsteps of retirement. Inadequate savings, both personal and retirement, limit the ability to retire and enjoy your money at work. Often, part-time work may be required to help support the lifestyle pursued while working. As the retirement doorstep approaches, this goal motivates frenetic saving, but often proves itself too late. For one to truly enjoy retirement, it's the old adage, "save now or pay (a lot) later."

A key strategy is to make early and regular saving a habit by making the future feel more vivid and real. When retirement is staring you in the face, one is much more willing to save. In monitoring savers, when instructed to imagine retiring in 30 years, most procrastinated or saved in minimal ways; years feels too distant. But when told their time horizon was "just" 10,950 days (same amount of time), the concept of days caused one to save earlier, more consistently, and at greater levels. Using days made the future more pressing. Seems the closer we get to the goal, the more motivated we become.

It is from that perspective then that we should develop sub-goals, or small goals that are both realistic and challenging. Short dated, small goals are easier to participate in, than way-out-in-time goals. Automate your saving to reduce the temptation to spend and force some level of financial restraint. Monitor the amounts being deposited, instead of the account value (value is important, but time and compounding will provide a great surprise). Disciplined, automated savings also lessens the impulse to change investment decisions because of market moves and emotion… AND, it is proven to create more excitement, motivation, and satisfaction than the deposit of a single lump-sum. Always keep time your greatest ally – stay disciplined in saving and investing.

True story – Albert Einstein, the great physicist was once traveling from Princeton on a train, when the conductor came down the aisle, punching tickets of every passenger. When he came to Einstein, Einstein reached in his vest pocket. He couldn't find his ticket, so he reached in his trouser pockets. It wasn't there, so he looked in his briefcase, on the seat beside him, and could not find it. The conductor said, "Dr. Einstein, I know who you are. We all know who you are. I'm sure you bought a ticket. Don't worry about it." Einstein nodded appreciatively. The conductor continued down the aisle punching tickets. As he was ready to move to the next car, he turned around to see the great physicist down on his hands/knees looking under his seat for his ticket. Rushing back, he said, "Dr Einstein, Dr. Einstein, don't worry. I know who you are. No problem. You don't need a ticket. I'm sure you bought one!" Einstein looked at him and said, "Young man, I too, know who I am. What I don't know is where I'm going."

Approaching retirement? Yes, we all are. Some are closer than others. Yet, we all need to plan, and execute short-term goals to reach our long-term goal - living life pursuant to our own standard of living.