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MARKET COMMENTARY November 15, 2017

Dow Jones Industrial Avg.	**22,405.09**	**Standard and Poor's 500**	**2,519.36**
2017(YTD) + 13.4%	3rd Qtr. + 4.9%	2017(YTD) + 12.5%	3rd Qtr. + 4.0%

Look Before you Leap - "Don't be the last bear or the last bull standing, let history guide you, be contrary to the crowd, and let the tape tell you when to act." Jeffrey A. Hirsch, Editor, Stock Trader's Almanac.

On Cruise Control - Investors have reason to be pleased with this year's market performance, however there is a sense of unease in the air. Why? The economy continues to hum along with the last two quarters achieving three percent growth for the first time in ten years. Interest rates remain near historic lows. Corporate profitability has exhibited steady growth. Overseas economies have rebounded as have many foreign stock markets. Perhaps the most obvious negative is the contentious political atmosphere and the number one antagonist is our President. That is why individuals gathered in cities across the country last week on the anniversary of his election to SCREAM!? There is also the dysfunctional Congress to be considered. Finally, and most importantly, valuations are stretched. Price/earnings ratios are well above historic norms and the average dividend yield for the Standard & Poor's 500 is now below two percent. Unless corporate earnings accelerate from current levels, it will be difficult to justify a meaningful advance from current levels. Another looming concern is interest rates. It has been well telegraphed that the Federal Reserve (i.e., the FED) is likely to increase the federal funds rate by 25 basis points (or ¼ of one percent) next month. In addition, the FED is rumored to be considering three more quarter point increases during 2018 before the President decided to replace Janet Yellen as Chair. There is a legitimate concern that higher interest rates will erode support for stocks and set the stage for the inevitable market correction. As a consequence, liquid investments will once again provide at least a modest return for those who shun risk.

Finding Cover- When things have been going well for an extended period of time, it is easy to be lulled into a false sense of security. Investors expect continued gains in market prices until the correction begins. Before they can decide on which way to turn, the losses are piling up. Therefore, the time to begin thinking defensively is when there are no clouds on the horizon. Squirrels do not start gathering their acorns when they are covered with snow, and investors shouldn't wait to reap some gains until the correction is underway. One tactic used to maintain reasonable portfolio balance and reduce stock exposure before a serious correction is to rebalance a portfolio on a regular basis. For example, if the stock allocation is 50 percent and a rising market increases it to 60 percent or more, the indicated action is to reduce stocks back to the 50 percent level. Such an approach applied in both rising and falling markets helps to reduce volatility and vulnerability to any sudden decline. Sales made as a result of this strategy should be carefully chosen so as not to generate a large capital gain liability. In summary, given the significant gain in stock prices since last fall's election, now is an excellent time to examine a portfolio's current allocation to determine whether or not rebalancing is appropriate.

Tax Cut or Tax Reform? – Before answering that question, our President and the Congress should first be prepared to answer another question, "What are you trying to accomplish?" The Republican mantra of "Tax cut! Tax cut!" is ill-timed. Fiscal stimulus at this point in the economic cycle is likely to prove counterproductive over the near term. With unemployment approximating four percent, there is little slack in the economy. Moreover, with the economy accelerating as witnessed by growth of three percent in the last two quarters, stimulus of this magnitude is likely to result in an overheated economy and a possible resurgence of inflation. Interest rates have begun to move higher, so a more robust economy would only serve to exacerbate these undesirable trends. The Republicans are always quick to label the Democrats as tax-and-spend liberals, while they are now proving to be tax cut- and-spend conservatives. What do they have in common? Easy, an unbridled willingness to spend. Even the supposed conservative budget hawks in Congress, who owed their success to the Tea Party voters a few election cycles ago, have been neutered by either the establishment Republicans or the dreaded tweeting of the President. The end result is the swamp creatures in Washington have prevailed and the annual deficits and the $20,000,000,000,000 (yes, trillion) national debt are no longer a serious concern. The sad truth is we are sowing the seeds of our own destruction by continuously demanding the government provide us more goodies, yet always expecting someone else to pay for it – you know, the top 10% are paying 70% of the bill. Tax reform and regulatory relief are changes capable of providing the maximum long-term benefit with little added cost and the potential for some additional revenue.

No Diamonds; Only Rough – Pick your market and the answer is the same. There are no compelling ideas. Stocks are, generally speaking, too rich (i.e., pricey). Bonds and other fixed income investments do not yield enough, although there are finally some signs that is beginning to change. For several years, money market funds yielded zero (0!), now they are around 0.50% and climbing. Even better, six month U.S. Treasury bills yield 1.3% and moving higher as well. Unfortunately rates for longer maturities remain disappointingly low. Spreads over Treasuries are minimal. Investors are not being adequately compensated for the added risk. Thus far this year, equities have provided above average total returns, but little of the credit goes to the dividend contribution, which has shrunk to less than two percent. What this likely means is more investors will be taking more risk than they should to capture returns that may never materialize. Unless some miraculous pro-growth legislation is generated in Washington soon, investors should plan for mid-single digit returns at best in 2018.

Wrapping Up the Year with a Bow – With Thanksgiving coming next week (Yikes!), it is time to provide a few financial housekeeping tips to address before the end of the year. Any investor over 70 and ½ who owns an IRA is required to take a required minimum distribution every year. Failure to take your withdrawal leaves you vulnerable to a severe penalty. Now is a good time to reexamine the holdings in your investment portfolio. Many stocks have achieved healthy gains this year, so if you wish to realize some profits or if you decide it would be wise to employ the re-balancing strategy mentioned earlier, it provides an opportunity to eliminate any underperforming investments. Your losses can be used to offset your gains, and therefore reduce your capital gain liability. Any extra losses can be used to reduce your taxable income (up to $3000 per year for a joint return). Two other important reminders at the end of a good year are to review the list of charitable organizations you chose to support and perhaps consider an increase in some cases. Keep in mind you can gift appreciated securities, avoiding the capital gain tax, yet still write off the full market value. It is worth noting you can use this approach in making gifts to family members as well, especially if they are in a low tax bracket, of course you cannot write off gifts to family. With any of the recommendations above you should speak with your tax preparer to insure you take the right steps in a timely manner.

Finally, with winter on our doorstep we have to consider there may be extended electrical outages. If so and you're unable to reach us at our office you can accomplish any task we ordinarily provide (except for advice) by contacting Schwab directly through their Schwab Alliance service at 800-515-2157 or www.schwaballiance.com.

Have a Happy Holiday Season!! --JML