Hamilton-Bates
Market Update
December 4, 2017

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Capital Hill Lets Make a Deal

The financial markets are getting ready to close out a pretty good year. After dallying and delaying Capital Hill seems to be trying to get its act together and finally passed a Tax Cut Bill in the Senate. Getting this done could give stocks and the economy an added boost heading into 2018. There was also another 'deal', General Flynn's guilty plea deal with Mueller. After a brief dip the markets mostly took the plea deal in stride and not as a sign of further shoes to fall. The major averages were up 1-3% for the week, led by value stocks–like those that make up the DJIA.

After lagging **Growth** stocks like Amazon (for ever it seams), **Value** stocks found bids and might have bottomed after over a decade of underperformance. This could be an emerging theme for the next few years and could be a source of outsized performance in 2018 to take advantage of.

Economic and Earnings Outlook

Economic strength has been solid, with 3Q GDP getting revised up to 3.3%. The Atlanta Fed expects 3.5% for Q4 2017. The economic trend remains strong globally, which bodes well for 2018. This synchronized growth has been key to the strength across all world markets for 2017. <u>This growth cycle is likely to remain strong into 2018 as long as our Fed doesn't hike rates too much or too soon</u>. Rate hikes slow growth, but as long as the moves are slow and measured the market should be able to cope with a measured pace. At some point rates will rise high enough to slow the economy, but that time doesn't appear to be at hand. For now strong global growth has delivered good earnings, and good market returns. The Tax Cut deal sure looks to be coming, and as we noted previously <u>"Tax cuts on top of the current economic and earnings picture keep the fundamental outlook positive heading into 2018."</u>

Market and Investment Outlook

The initial response to the Senate's Tax Cut Bill has been positive, and we are likely to see that supportive tone last through year end. The positive potential impact of a tax cut, even if it is not a ambitious as once hoped for, is still likely enough to keep positive momentum going. Seasonal and historical factors remain positive through Q1 of next year, although mid-December can often see a bit of a dip.

The long-time leading technology sector has finally started to look a bit ragged, and we are seeing some rotation OUT of tech into other areas of the market like financials and telecom. This goes hand in hand with the rotation from 'growth' to 'value' we are seeing on the style level. Don't be surprised if we see the market back and fill into mid-December, we fully expect to see 'Santa' for a rally that closes out the year.

Managed Portfolios are on pace to finish the year with solid gains, with strength across the board in equities along with exposure to the correct bond sectors combining for good gains relative to our benchmarks. This year we emphasized equities over bonds, while in the bond market we remained invested in high-yield and flexible sectors over government bonds. These decisions helped add to performance. Our Sector Equity Portfolio is on pace to beat the S&P for the year. More on the portfolios later in the month.

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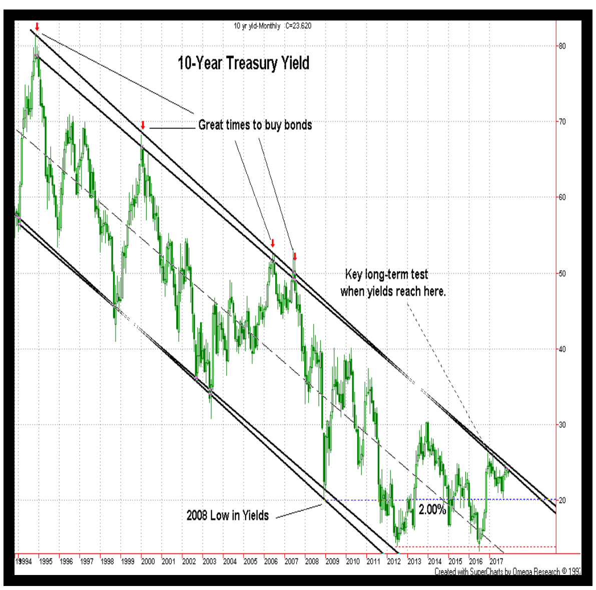
Market Charts : Stock Market Trend Intact but Bond Bull In Trouble

S&P 500 Long-Term View—As we near year end it's a good time to take a step back from the market and look at it in terms of the bigger picture. As you can see in the top chart, the 2017 has been the definition of a good year—up and to the right with hardly a hiccup. This in turn continues the trend that goes all the way back to 2009.

With the major averages trending higher and well above the 10-month average (in red), the stock market heads into 2018 with the bull trend intact.



Bond Market & Interest Rates—Just as the stock market has been up and to the right—the classic definition of an uptrend, interest rates have been the opposite (down and to the right) for a very long time. The bottom chart shows the 10-Year Treasury Bond yield all the way back to the early 1990's. Since that time the long-term trend in interest rates has been down. This has been a tremendous tailwind for all assets. Periodic rises in rates/yields have been capped by the upper trend line each time it has been tested, and rates turned lower.

Rates are heading up once again, and challenging that upper trend line. The double lows in place in 2012 and 2016 suggest the long-term trend in rates may be changing. If that happens in 2018 we will be prepared to make the appropriate portfolio allocation changes.

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