BRIAN D. LOWDER, INC.

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FINANCIAL MARKET OVERVIEW

Amazingly, stocks finished the 2016 year with a respectable return of about 10% or 12.5% when dividends are included. No one was even close with their predictions. The first quarter of 2016 ended with stocks up slightly less than 1%, but during the first 45 days of the year, stocks were down over 10%.

Second quarter stock market performance was similar. Overall stock prices were down 6% after the Brexit vote (England voting to leave the European Union) and finished the second quarter up nearly 2%. If it were not for the 3% stock market gain during the last 4 trading days of June, the stock market would have posted a negative return during the second quarter.

Third quarter stock market performance was about average. On the last day of trading in September, stocks rallied- up 1%. Overall, the U.S. stock market averages were up about 4% during the third quarter when dividends are included. Through September, 2016, the stock market was up about 5% or 7% when dividends are included.

As we entered the fourth quarter of 2016, many forecasts and opinions were made within weeks of the presidential election, yet none of them closely matched how the fourth quarter ended. U.S. stocks rallied 6% over the final seven week period following the election and the 2016 year ended with a 10% gain or as high as 12% when dividends are included.

International stocks (world index excluding U.S.) earned less than 2% during 2016, with the Chinese stocks posting the largest decline of more than 12% and U.K. and Canada scoring gains of 14% and 17%. Emerging market stocks (small international companies) advanced 8.8% during 2016. Once again, emerging market stocks typically provide a higher return during periods when overall stock prices are up and larger losses during declining market periods.

Value stocks (companies that are mature, have stable sales, and pay dividends) were up over 15% and outperformed growth stocks by a margin of 7% or more in 2016.

Energy companies and energy mutual funds were the best performing sector – crude oil prices jumped 45% in 2016 after crashing from over $100 per barrel to about $28 per barrel during 2015. Health Care stocks were the only sector that posted a decline – down 4%. Gold prices rose over 8% in 2016.

Fixed income or bonds had a roller coaster ride in 2016, but ended the year with a fractional loss of -0.02%. The drop in bond prices (due to rising interest rates) was slightly larger than the interest income earned during the year. The 10-year U.S Treasury Note started the year paying 2.3%, dropped as low as 1.37% in July and finished the year paying 2.45%. Corporate and low-rated bonds posted positive returns in 2016 – but the U.S. stock market ended the year with better gains.

Real estate (REIT's) prices were down 4.5% during the fourth quarter after rising about 14% during the first 6 months of this year. The Federal Reserve raised interest rates in December and that increase adversely impacts mortgage rates and the rental income is slightly less

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valuable as interest rates rise. Likewise, another interest rate sensitive category, fixed income or bonds, also suffered small declines as well – with intermediate-term bonds declining about ½% in value.

The following chart displays sample returns of various asset categories during the fourth quarter and the entire 2016 calendar year:

Calendar Yr 2016	**4th Qtr. 2016**	**Index Return (*includes dividends reinvested*)**
+ 13.42%	**+ 7.94%**	**Dow Jones Industrial Average (^DJI)**
+ 9.64%	**+ 3.34%**	**Standard & Poor's 500 Index (^GSPC)**
+ 10.57%	**+ 3.58%**	**DJ U.S. Total Stock Market (VTI)**
+ 5.45%	**+ 0.70%**	**Large-company stock-Growth (IWF)**
+ 14.48%	**+ 6.07%**	**Large-company stock-Value (IWD)**
+ 5.95%	**+ 0.02%**	**Mid-Size Stocks – Growth (IWP)**
+ 17.14%	**+ 4.77%**	**Mid-Size Stocks – Value (IWS)**
+ 10.53%	**+ 3.38%**	**Small-company stock- Growth (IWO)**
+ 29.37%	**+ 13.55%**	**Small-company stock- Value (IWN)**
- 1.69%	**- 2.37%**	**International (EFA)**
+ 8.76%	**- 6.52%**	**Emerging Markets (EEM)**
+ 3.51%	**- 4.85%**	**Real Estate Investment Trusts (VNQ)**
		Fixed Income
+ 0.11%	**- 0.69%**	**Short-term U.S. Treasury (SHY)** *(includes appreciation)*
- 0.73%	**- 6.31%**	**Intermediate U.S. Treasury (IEF)** *(includes appreciation)*
		Alternative Investment Category
+ 8.03%	**- 12.76%**	**Gold (GLD)**

All returns calculated using adjusted historical quotes from finance.yahoo.com

FINANCIAL MARKET OUTLOOK

The world was supposed to end as we know it and the financial markets were predicted to crash if Trump won the election. When most experts, individuals or the media agree, something else is going to happen. Instead of crashing, stocks advanced nearly 6% during the last seven weeks of the year. By the end of the year, the overall U.S. stock market was up just over 10% (12% when dividends are included).

During the first 45 days of 2016, the stock market was down over 10%. The concern and consensus forecast was that the Federal Reserve would raise interest rates 4 times in 2016 – only one rate increase was made and that occurred much later in December. By the end of the first quarter, the stock market erased the entire earlier decline.

In the second quarter, the consensus was that England would reject the Brexit vote (England voting to leave the European Union). The opposite occurred and while the U.S. stock market dropped quickly, two days later the entire decline was erased.

The big finale was the 4th quarter consensus forecast that Clinton would win easily and the dire predictions of a big stock market decline should Trump win. Wrong on both accounts, again. Who knew that unpredictability and investing in the opposite direction of consensus forecasts could be so rewarding?

Sarcasm aside, the stock market is a forward looking machine. Stock prices today reflect what the consensus expects to be the most likely scenario 12 months into the future. Renewed economic growth – meaning something better than the 2% or less GDP growth rate over the past several years is and has been expected and therefore stock prices today are higher than what *normally* would be justified. And with all other investment categories performing poorly, stocks remain priced above what is "normal". Better economic growth must materialize soon for the stock market to maintain the recent gains and move higher. With stocks trading at 19 times earnings (14-15 range is considered average or normal), that's about a 25% premium. It's the non-economic events along the way (interest rate predictions, Brexit vote, presidential election, etc.) that can cause market volatility and a quick retreat to "normal valuations".

The good news or tail winds are: 1) the U.S. and world economies are growing slowly and should improve – but the growth rate needs to reach 3% or more soon; 2) consumer confidence has just reached a 9-year high; 3) Trump vows to improve economic growth and increase jobs through increased infrastructure spending/investment, increase defense spending, renegotiate international trade agreements, lower the

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U.S. corporate income tax rate (the current 35% tax rate is the highest in the world), halt the exodus of U.S. corporations moving overseas, and reduce regulations. Will it happen? Most of the agenda is likely to be implemented. When both houses of Congress have the same majority party as the President-elect plus Trump will inherit the famous pen and phone to take quick executive action, the probability of getting most of what he wants is better than 50%. Will it work? No one knows for sure.

The bad news or head winds are: 1) the rising value of the U.S. dollar (up 4% in 2016) does benefit U.S. citizens traveling abroad, but it makes our exports or products more expensive overseas and is a slight drag on our economic growth, 2) Trumps "protectionist" platform (renew trade agreements and make them more favorable to the U.S.) of charging tariffs or additional tax on China (or any other country that dumps imports on our shores) along with former U.S corporations manufacturing overseas and then selling lower-cost products back into the U.S. - the "protectionist" ideas carry the biggest risk. The financial markets do not react kindly to trade wars and future U.S trade policies are clearly a negative market risk in 2017.

INVESTMENT OUTLOOK AND RECOMMENDATIONS

The biggest uncertainty affecting the future of the financial markets – the U.S. election, is over. Clients experienced yet another example of how difficult it is to predict where the financial markets may go over the short-term. Nobody got it right.

Here is the scenario we think will unfold regarding the future direction of *the financial markets* – politics and social issues aside: The probability of a rising stock market ***1-2 years from now*** is higher than the probability of a lower stock market valuation. The transition will be challenging, but ultimately most of the changes outlined by the new President-elect will happen. Very simple. The Oval Office, House of Representatives, and the Senate are dominated by the same party. And, Trump will have a phone and pen (executive orders) and will use it just as the outgoing President did. From a *business* and financial markets perspective, *better economic growth* is a must.

The stock market already assumes better economic growth in the future (based on 25% premium valuation) and interest rates will continue to rise slowly over time. Growth is a must; otherwise, the financial markets WILL decline.

Previously, we were unable to assume a 50% or greater probability of occurrence to three general outcomes: 1) the stock and/or bond markets decline, 2) overall economic growth improves and the stock market continues to advance or 3) anemic economic growth continues and the financial markets deliver a slightly negative to slightly positive returns.

We believe number 3 above is unlikely – as change is coming. And, number one above is certainly possible during the 1-year transition toward a new direction. Ultimately, we believe number 2 above will prevail.

Therefore, we expect to increase our clients' allocation into the same growth areas that we had reduced back in August 2015. However, we do want to be wise and prudent regarding when to execute the purchases. The U.S. stock market is near an all-time high and has *already* jumped more than 6% since the election in anticipation of better economic environment down the road. There will be opportunities to buy at reasonable prices – the markets never move consistently in either direction in a smooth and continuous manner. We are still dealing with a divided Congress and their instinct to obstruct anyone and anything that doesn't conform to their thoughts is still alive and well. This change of course will take some time and terrorist acts can change the confidence level of investors at any time along the way.

Improved economic growth will benefit most sectors of the economy – the overall market should advance. Much has been written about which sectors will do best under a Trump presidency and we suggest spending less time trying to pick the needles in the haystacks. Yes,

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defense and infrastructure stocks should do well. Many have already risen more than 35% like Caterpillar and others. The Commodities sector should improve and Europe has had so much bad news, their stock prices are bargains comparable to shopping at Goodwill. Value stocks are outperforming growth stocks and small-company stocks have achieved twice the return of larger-company stocks.

We have multiple selections and there are many ways to invest during the transition. **Once again, we will not include any of the Blue Recommendation sheets you are accustomed to receiving at quarter-end in this mailing, but intend to include them in 2017.** There are too many selections to choose from.

We wish everyone a Happy New Year and we are looking forward to 2017.

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Best Regards

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