Executive Summary

I. Market Overview

A. Our Investment Philosophy: *Reversion to the Mean*.
B. 35-year-old bond bull market is likely over. Higher interest rates expected over next decade. Long-term Treasury bond down 20% in the last couple of months.
C. If interest rates start to rise, then equity markets will most likely decline as bonds become more attractive versus equities.
D. Any decline in stocks due to higher interest rates may be countered by real growth in the economy resulting from post-election fiscal stimuli.
E. At this point, nobody knows what is coming. It will take at least 4-6 months to ascertain post-election market trends.
F. Republicans are traditionally fiscally conservative. If so, then some of Trump's fiscal stimulus measures may be dampened.
G. If fiscal stimulus does occur, then expect stocks to rise in 2017. Under this scenario, expect higher interest rates and significantly lower bond prices in 2018-2020.
H. Stock market valuations are at extremes based on many valuation methodologies and higher than all other market peaks other than 1999-2000.
I. So far, the post-election rally is following a similar pattern to what ensued after Reagan won. First there was a rally followed by a big decline. It took a few years before the full benefit of Reagan's fiscal stimulus became realized. Reagan also had the combined advantages of declining interest rates and disinflation. Fiscal stimulus under Trump will be fighting headwinds from higher interest rates and inflation.

II. Where We Are in the Cycle

A. This bull market is extended beyond the typical length in history.
B. Why – Quantitative Easing = Monetary Liquidity = Money Printing from Fed.
C. Wealth Effect and Why - Effects on Financial and Other Assets.
D. End of Quantitative Easing = Tightening of Monetary Liquidity.
E. Higher interest rates already here since summer 2016.

III. Economic Fundamentals

A. Economic growth appears adequate and should improve for next year or so if fiscal stimulus materializes.
B. Strong dollar has been impacting corporate earnings.
C. That should continue if interest rates rise unless Europe and Japan follow with higher rates.