WEISS WEALTH MANAGEMENT GROUP of RAYMOND JAMES®

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SMART AND STEADY

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LEONARD A. WEISS
SENIOR VICE PRESIDENT, INVESTMENTS
LEONARD.WEISS@RAYMONDJAMES.COM

LOWELL J. WEISS, J.D., CFP®
FINANCIAL ADVISOR
LOWELL.WEISS@RAYMONDJAMES.COM

WEISSWEALTHMANAGEMENT.COM

DJIA: 19,762 | NASDAQ: 5,383

There's a Great Big Beautiful Tomorrow…

This year marks the 40th anniversary of the beginnings of what we know today as Weiss Wealth Management Group of Raymond James. Certainly many things have changed since 1977. We can cite advances in technology, education, travel and health care that have changed how we live, work, and play. We've asked Senior Vice President Leonard Weiss to talk a bit about the changes he has seen over his four decades in the industry.

When the team asked me to write a more personal version of The Weiss Report I tried to think about how I could sum up forty years of change. Sometimes it felt like change was occurring at a snail's pace; others felt like everything changed in the blink of an eye. In some rare occasions it felt like both at the same time.

In fact, as I thought about what to write, I was reminded of one of my, and Lowell's, favorite attractions at Disney World – The Carousel of Progress. For those who haven't had the pleasure, the ride is a theater show following a family through four distinct times in the past – the early 1900's, the mid 1920's, the mid 1940's, and lastly the 21st century. The family talks about their daily life and more specifically how technology and culture has changed. An infectious song plays often during the ride – and the more I think about my history in the industry and the future of our practice, the words ring truer and truer. "There's a great big beautiful tomorrow…"

To me it is clear that the biggest changes are in three specific areas: technology, availability of information and product, and (perhaps most importantly) the scope of my role.

Looking back, sometimes I wonder how I was able to do the job! Back in 1977, the industry had very little automation so we used a lot of paper. All buy and sell orders were written on a three page ticket complete with carbon paper and then transmitted over a traditional teletype machine. I had a very small price monitor but mostly used the decade's old ticker tape above our desks to watch prices.

As computers became more prevalent, I was able to leverage my time. While I enjoyed the ability to use a word processor and print reports, I never imagined what would happen in the 90's and 2000's. Now, I am able to place trades in accounts in seconds rather than minutes. I have real-time quotes, immediate access to all the information in the world, and the ability to communicate with all members of my team instantly. Every aspect of the industry has been touched by the technology boom. While many of us old timers may pine for the good ol days, I'm not so sure I want to give up the amazing technology I get to use every day.

Another major area of change has been the expansion of product and information. It really started in the 80's as asset allocation theory became well known. As more investors wanted to be fully "asset allocated" there grew a need for more investment products. Suddenly there were new funds and new managers to learn about. In most cases this was a positive thing for individual investors. This explosion of options only accelerated in the 90's and is almost at record speed today.

In addition to mutual funds, our clients can invest in a multitude of other investment vehicles such as Exchange Traded Funds, Unit Investment Trusts, and a wide array of structured product. Not every investment vehicle is appropriate for every investor, but every investor can find a proper product. As a free market economist, I wildly support the idea that more choice is better for investors.

I would be remiss if I didn't mention the availability of information as a seismic change. In the 70's and 80's if a client wanted information about a stock, they had to call me – even if they just wanted a quote! Today, almost everything that can be known about a stock is known by all. Sometimes this can lead to bad results, as everyone thinks they are an expert because they read a Yahoo! article, however on the whole this has been a positive change as well. The increase in available information has also yielded an increase in investor participation. Actively engaged investors make great clients and on the whole, I have enjoyed the shift.

The last change I would like to discuss is the scope of my role. This has arguably been the biggest and most important change. In the 70's, there were no advisors. We were stock brokers. We sold you a stock or a bond, and would call again when it was time to sell that item or buy something else. The idea of financial planning was a very small part of the industry.

The marketplace served at that time was subdivided by banking laws. I only handled investments. Banking, insurance, and trust services had their own platforms and the lines between them all were easily identified.

The only compensation at the time was from getting a client to either buy or sell an investment. The primary path to expanding one's business was calling complete strangers on the phone and trying to establish a relationship.

In 1997, the Glass Steagall act, which kept investment banking separate from commercial banking, was repealed. This radically changed the industry. With prior barriers to business eliminated, a fresh white canvass emerged. A new financial industry was born.

It was in the 1990s that traditional brokers had a chance to recalibrate their business' to become true financial advisors. The biggest change post Glass Steagall's repeal was the creation of the asset based advisory fee. As the marketplace expanded from selling products to providing financial advice of all kinds, we realized that we could and should handle affairs for our clients that went far past the placing of investment products. The asset based fee allowed us to expand our offerings to include advising on college savings, retirement and gift planning. During this decade, financial affairs become much more detailed. We realized that Baby Boomers would live longer and have more active lifestyles than their parents, and that anyone still using the old "broker-salesman" model would become a dinosaur in time.

When we moved into the 21st Century, and survived Y2K, we spent more time on our client's need for financial advice in general and less so about managing only investments. In this decade, software that allowed us to do longer term planning was developed. This allowed the advisor to separate further from the old broker/salesman model. Advice became the most valued service we had to offer.

Today, in 2017, we celebrate our 40 years of service, but we are more excited that the evolution from broker/salesman to financial advisor is complete. The Weiss Wealth Management Group is better equipped to serve our clients in the future than when we began. Within our team we have expertise in areas that didn't even exist when we began in 1977. We have over 85 years of collective experience, yet have the youth within our team to help our clients for at least the next 30 years! It has been and still is our passion to help our clients fund and realize their financial dreams.

What do we expect ahead?

In our last edition titled, "What Now", we focused on the potential changes in economic policies and their market implications under a new administration. We saw the prior eight years of economic policy as headwinds for the economy and markets. Policies that increased taxes, regulation, and other labor costs could now be reversed, turning headwinds into tailwinds. We interpret the stock market's rise, and the sharp jump in interest rates, since the election as a vote of confidence for the observations made in the last edition.

We also mentioned that the stock market in general may be undervalued. The current 10 year period of returns is below its own growth trend lines of 30, 50 and even 70 years. We would think it's time for the markets to revert to their mean. Statistically this can only happen by the markets trading above its own long term trend of return for some time, lifting the market back to its historical norm.

With the market's reaction to the election outcome in the last few weeks, we are more convinced today of these shifts in trends then we were in November 2016. We think economic growth, corporate earnings, and markets will do very well in the next few years.

Portfolios:

Portfolios we manage by discretion had major changes implemented in the final months of 2016. We thought then that our portfolios would be best served by changing our focus from portfolios focused on individual securities to a portfolio that is much broader and diversified. We called it Operation Widen the Sail.

We created an asset allocation that emphasizes third party managed investment buckets. This strategy shift allows our portfolio to participate in a wider selection of sectors and investments. And, since we expect tailwinds to replace prior headwinds, we are confident this strategy will catch more of the new wind, helping us reach our future financial goals.

Enclosures:

Enclosure #1 is an article from Bloomberg that reports optimism from small business owners following the election. We have written often over the past few years that an indication of economic trouble was the relative poor health of small businesses. However many believe this will turn around soon.

Enclosure #2 is an interesting look at the future of hedge funds. While the media loves to gush about hedge funds, more investors are starting to question the traditional compensation these funds charge. This author questions what the future may hold in this space.

Enclosure #3 is a recent writing from one of our favorite economists, Brian Wesbury from First Trust Advisors. Regular readers of TWR will recognize the name. In this piece, written December 27, 2016, he gives some color as to First Trust Advisor's expectations for the new year.

Small Business Owners' Optimism Skyrockets Following Trump Victory

Small businesses seem to like a unified Republican government.

by Luke Kawa - Bloomberg Wire, December 13, 2016

President-elect Donald Trump's victory in the U.S. elections is a giant leap for small businesses, according to a survey of their owners.

The November reading of the National Federation of Independent Businesses' small business optimism index jumped to 98.4 from 94.9 — its sharpest surge since 2009 — with all of the increase in sentiment coming after the U.S. elections held on Nov. 8.

"This month we bifurcated the data to measure the results before and after the election," explained Chief Economist Bill Dunkelberg. "The November index was basically unchanged from October's reading up to the point of the election and then rose dramatically after the results of the election were known."

Among those who were surveyed following the election, the balance of opinion on whether business conditions were expected to improve skyrocketed from a reading of -6 to a whopping +38.

For the month as a whole, this subindex improved to 12, from -7, to reach its highest level since 2014. Similarly, the balance of opinion on sales expectations jumped by 10 percentage points to +11.

"Small businesses like unified Republican government," said Neil Dutta, head of U.S. economics at Renaissance Macro Research LLC, who highlighted that the NFIB's index fell in November 2012 — when Obama won re-election — but recorded a solid rise in November 2004 after voters granted George W. Bush a second term.

On a relative basis, Trump's plan to cut corporate taxes offers the most benefit to firms that earn more revenues domestically — a category most small businesses fall into. The possibility that Linda McMahon, who Trump nominated to lead the Small Business Administration, might roll back regulation and help fulfill the real-estate mogul's pledge to repeal Obamacare also contributed to higher optimism among small business owners, said Dunkelberg.

The vast majority of segments that showed improvements in November's survey were forward-looking in nature; on both actual sales and earnings changes, the balance of opinion remained steeply negative.

The NFIB reading is the latest in a number of gauges tracking sentiment in the U.S. economy to have soared since the election, including the University of Michigan's December report which showed that consumers' assessment of current government economic policy rose to its highest level since 2009.

The Beginning of the End of Hedge Funds?

Diana Britton | Nov 23, 2016

Two-thirds of hedge funds fail within three years of launch. The ones that remain are expensive, opaque and have spotty performance. Are HNW investors wising up to the hedge fund folly?

In the late 1980s and early 1990s, hedge fund performance was consistently strong, delivering upwards of 30 percent returns in some years.

So much for the rah-rah 1980s. More recent performance has been volatile. In 2015, the average hedge fund returned 0 percent, according to Tiburon Strategic Advisors. And consider that two-thirds of hedge funds in the major commercial database stop reporting—meaning they fail—within three years of launch.

Hedge fund managers promise different strategies: Absolute returns, non-correlated returns, amplified returns - and exclusivity. The goal, many fund managers will say, is not to beat the market, but to provide a hedge, meaning access to uncorrelated assets that mute an investor's overall positive returns, but cushion the downside. Other funds, led by rockstar managers with recognizable names, take an activist approach or focus on large-scale bets in an attempt to garner outsize returns. Hedge funds are really a compensation scheme, not an asset class; for years, many charged 2 percent of assets and 20 percent of returns.

That compensation scheme - along with a tendency to not live up to their marketing hype - seems to be their undoing. For the first time in six years, flows to hedge fund and liquid alternative managers have turned negative. Several large public pensions and institutional investors have abandoned the structure, and many of the strategies are available to retail investors in much less-expensive mutual fund wrappers.

“In the big scheme of life, this is the alternative investment product that everyone thinks is sexy—gets a lot of glamour, gets a lot of write-up—but you have a hard time convincing yourself that the median, or average, hedge fund is a good product,” said Chip Roame, Tiburon managing partner.

Assets in hedge funds have slipped from $3.2 trillion in 2015 to $3.1 trillion today, Roame said. At a recent Tiburon CEO Summit, 95 percent of industry executives said they don’t believe the average hedge fund manager adds value on a post-fee basis.

“The ability to pick a hedge fund product that will do well and will stay in business is extremely difficult,” he said. “I think of this a bit like the active manager argument.”

Proponents of passive investing argue that most long-only active managers underperform. More to the point, it's impossible to predict the few who will add value.

“The argument for hedge products is exactly the same, which is why so many of them are out of business three years later,” Roame said. “The ones that have the high returns are around; then they often implode. The ones that don’t have the high returns just disappear. So it’s a tough market to pick the right product in.”

Roame believes the only safe bet are the companies that provide due diligence or consulting services on hedge funds - there is opportunity there.

“I think that’s a pretty savvy business model because of the ratio of good funds to bad funds being so extreme towards the bad fund category,” he said. “It’s a bit like the story of the gold miners; you might make more money selling the shovels to them than by being one of them.”

Roame does not dismiss the possibility that the hedge-fund industry could self-correct and reverse the negative flow of funds. Perhaps a market down turn will weed out the bad managers from the good ones, leaving fewer funds to compete for the same assets. And, Roame says, for retail advisors there is still a cache to the mystique: “I think it’s a sales story that lots of financial advisors like.”

First Trust
Monday Morning OUTLOOK
630-517-7756 • www.ftportfolios.com December 27, 2016

2017: Dow 23,750, S&P 2700

Brian S. Wesbury – *Chief Economist*
Robert Stein, CFA – Dep. Chief *Economist*
Strider Elass – *Economist*

We have used the metaphor of the "Plow Horse" to define the US economy since 2009 – an economy driven by new technology and entrepreneurship (fracking, the cloud, smartphones, big data…), but held back by the friction of a growing and burdensome government.

Since mid-2009, real (inflation-adjusted) economic growth averaged a Plow Horse-like 2.1% per year. With the current forecast for Q4 real GDP at 2.5%, 2016 will finish right on that average.

The great news is that we finally have more than just hope to believe that this year, 2017, is the year the Plow Horse Economy finally gets a spring in its step.

We're looking for **real growth of about 2.6%**, led by faster growth in home building, a return to more normal growth in inventories, and, most importantly, more business investment.

That last part is key. Other than investment in technology, which has helped boost productivity, business investment has been weaker than normal. It looks very likely that President-Elect Trump and Congress are going to push for supply-side cuts in the corporate tax rate. In addition, cuts in regulation and less emphasis on government subsidies which direct resources toward politically-favored, and non-efficient industries will reduce economic friction. As a result, look for firms to both raise investment and use their pre-existing assets more efficiently.

In spite of these gains in efficiency, there is a massive amount of excess monetary liquidity in the system and inflation looks likely to pick up. In 2015, the consumer price index was up only 0.7%, held down by another year of falling energy prices. For 2016, it looks like the CPI will be up 2%. For 2017, look for an **increase in the CPI in the 2.5% to 3.0% range**.

Meanwhile, the unemployment rate will keep falling. Next year should end with the **jobless rate at 4.4%** (versus 4.6% in November), with risks more toward a lower rate than a higher one. Healthy job growth will continue, but companies will get more output growth from productivity.

On monetary policy, the Federal Reserve has consistently talked a more hawkish game then they have accomplished. This year, the Fed will deliver. **We're looking for three or four rate hikes on the table.** A March rate hike is possible, but we think the Fed will wait until after tax cuts become law before it pulls the trigger.

Longer-term interest rates are heading up as well. Look for the **10-year Treasury yield to finish next year at 3.25%.**

For the stock market, get ready for a strong bull market in 2017. We use a Capitalized Profits Model (the government's measure of profits from the GDP reports divided by interest rates) to measure fair value for stocks. Our traditional measure, using a current 10-year Treasury yield of about 2.5% suggests the S&P 500 is massively undervalued.

Using a 10-year yield of 3.5% suggests fair value for the S&P 500 is 2757, which is 22% higher than Friday's close. The model needs a 10-year yield of 4¼% to conclude that the S&P 500 is already at fair value, with current profits.

But profits have been held artificially low since mid-2014 due to the energy industry absorbing lower oil prices. Now that oil prices have rebounded, the energy sector should be a tailwind for economy-wide profits, not a headwind.

As a result, we're calling for the **S&P 500 to finish at 2700 next year**, up almost 20% from Friday's close and slightly more than 20% including dividends. **The Dow Jones Industrial Average should finish 2017 at 23,750.**

It's important to recognize, though, we are not market timers and are not saying a correction won't happen. Corrections come and go, like early in 2016, when the stock market recorded its worst two-week start to a year in history. Some investors were freaking out, while pessimistic forecasters were popping champagne and predicting a bear market.

For the past several years, we have been telling many investors that even though public policy isn't great, there are reasons for optimism, including the entrepreneurial spirit, which remains alive and well. Now we can look forward to tax cuts, a freer market in health care, less regulation, and more energy production than ever before. As we've been saying since 2009, and say even more emphatically now, those who stay optimistic will be richly rewarded. Stay optimistic and stay invested.

Date/Time (CST)	U.S. Economic Data	Consensus	First Trust	Actual	Previous
12-27 / 9:00 am	Consumer Confidence – Dec	109.0	**109.3**	113.7	109.4
12-29 / 7:30 am	Initial Claims – Dec 24	264K	**264K**		275K
12-30 / 8:45 am	Chicago PMI – Dec	57.0	**56.4**		57.6