2016 Year-End Review & Outlook

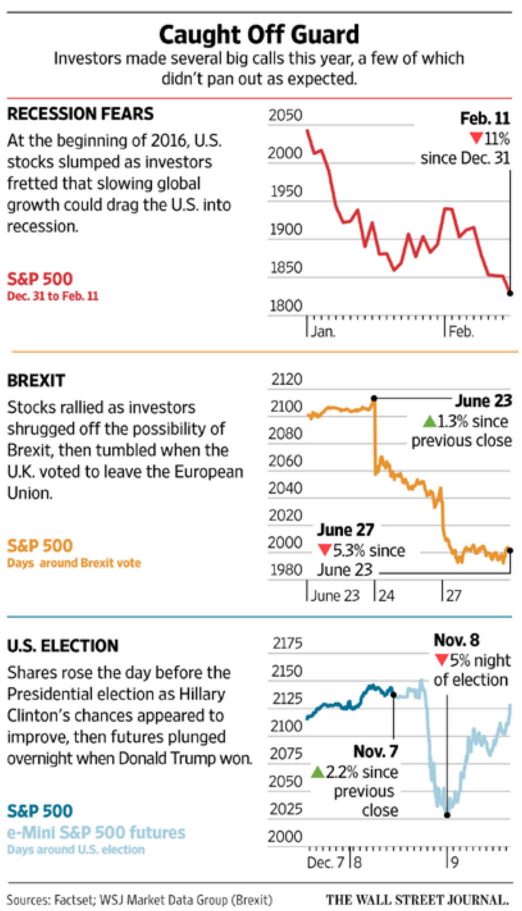
Market Review

> *Hope for stronger growth via Republican fiscal progress/reduced regulation/and tax reform have encouraged risk ... The assessment of future growth and associated risk spreads is still uncertain of course.*
> —Bill Gross, Janus Capital Group portfolio manager; legendary bond investor

Equities

U.S. stocks shook off a poor start for the year to log its best performance since 2013. Stocks weathered several shocks in 2016, including a possible global recession scare during the first quarter, Britain's surprising vote to exit the European Union (Brexit) in the second quarter, and the shocking election of Donald Trump in November. The bulk of 2016's gains came in the second half of the year. A rebound in corporate earnings, accelerating U.S. economic growth and stabilizing oil prices helped stoke investor enthusiasm for stocks. The rally gathered pace after the election of Mr. Trump as investors bet the new administration would usher in business-friendly policies such as tax cuts, looser regulations and fiscal stimulus such as infrastructure spending.

This year's rally extends a bull market that has tripled the Dow Jones Industrial Average from its March 2009 low during the financial crisis/Great Recession. For 2016 the Dow Jones Industrial Average of 30 blue-chip stocks gained 13%, the S&P 500 Index added 9.5% and the Nasdaq Composite rose 7.5%.



STRATEGIC FINANCIAL CONCEPTS
PART OF THE ALLIANCE

Fixed Income

U.S. Treasury bond holders could have slept through 2016 and would hardly have noticed the difference. The yield on the benchmark widely-held 10-year Treasury note closed 2016 near where it finished 2015. However, there was much turbulence during the year. Yields, which fall as prices rise, tumbled nearly a percentage point by the summer, with the 10-year hitting a record low in early July over recession and Brexit fears. The remarkable rally was then followed by the biggest three-month selloff in more than two decades. The 10-year Treasury yield climbed about 1% between October and December—the largest quarterly yield gain since 1994, thus the largest drop in price—as investors regained faith in stocks and raised concerns over future Federal Reserve lending rate hikes, which could pressure bonds prices even further downward.

Global Market Performance

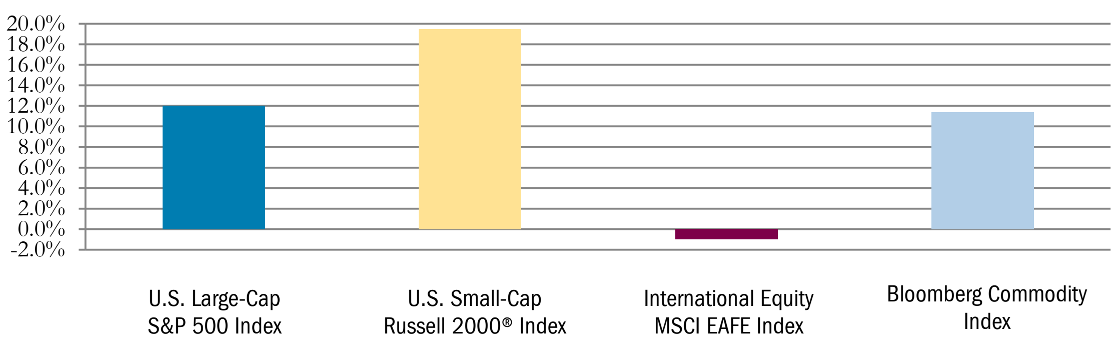
The broad stock S&P 500 Index advanced by 3.8% for the fourth quarter, and closed the year up 12.0% (dividends reinvested). The Russell 2000 Index of small-company stocks jumped 7.5% for the quarter and 19.5% for 2016, as this index's performance finally beat large company stocks with investor expectations of higher returns under a pro-business Trump administration. The tech-heavy Nasdaq Composite ended flat for the quarter and 7.5% in 2016, losing its 2015 lead as the highest performing U.S. stock index. The best performing sectors for the year were energy, industrials and materials. The worst performing were consumer staples, real estate and health care.

Developed international stocks were down 1.0% in 2016 as measured by the MSCI EAFE Index (in U.S.-dollar terms), marking its fourth year in a row for trailing U.S. stocks, and six out of the last seven calendar years. In 2016, money managers soured on Europe. In the first three quarters of the year, the Eurozone suffered net outflows of €405.4 billion ($423.8 billion) in investments, according to European Central Bank (ECB) data. No doubt that trend continued in the fourth quarter.

Emerging markets (EM) stocks had fared very poorly over the last four out of five years through 2015, resulting in negative cumulative returns. But 2016 proved to be the turnaround year for EM, rising 11.3% despite losses in the fourth quarter due to a strong U.S. dollar. Rising commodity prices during the year stabilized the economies of these export-oriented natural resource countries. And, up until the final quarter, a stable dollar vs. EM currencies also buoyed its stock prices, benefiting foreign investors.

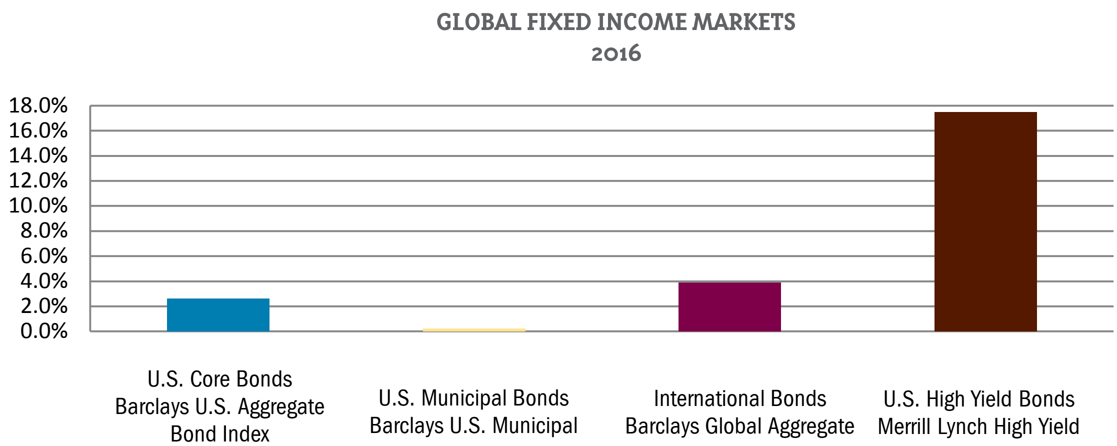
Natural resources and other commodities advanced 3.2% for the fourth quarter despite gold losing its shine, dropping double digits. Commodities recorded an 11.4% profit for 2016 (as measured by The Bloomberg Commodity Index). Crude oil held on to its impressive gains for the year (up 45% in 2016), and increasing precious metals and other natural resources prices also propelled the commodities sector. The potential end of "pump at will" by OPEC and other foreign producers, stabilizing the supply side, helped to support energy prices. OPEC recently met and agreed to cut future production—followed by other non-OPEC countries—which could support oil prices in 2017. But history shows that these agreements are usual not fully followed.

GLOBAL EQUITY AND COMMODITY MARKETS
For the Year 2016



As mentioned, the extremes of the 2016 bond market tell a story of fear and hope. And, unlike stock investors who are hopeful, bond investors typically prefer fear. Investors flocked to the world's largest bond market (U.S. Treasuries) for safety as the year began, when a sinking Chinese stock market and currency heightened worries about the global economy. Bonds got another boost after the U.K.'s surprising vote in late June to leave the European Union fed the fear trade. But over the past quarter, favorable global economic data and Federal Reserve pronouncements of future rate hikes drove investors away from bonds and into stocks. The pro-equity growth narrative was then accentuated by the prospect of greater federal spending on infrastructure, lower taxes and lighter regulations under a Trump administration.

After all these gyrations, the Barclays U.S. Aggregate Index of high-quality government and corporate bonds ended up only 2.6% in 2016. Non-investment grade (junk bonds) rose 17.5%, measured by the Bank of America/Merrill Lynch High Yield Master Index, as credit spreads tightened (the difference between high-quality and junk bond yields). As non-investment grade bonds more closely follow the returns of stocks rather than bonds, a surging stock market propelled junk bond prices along with investor inflows into these high-risk debt securities. State government municipal bonds were virtually flat for the year, up 0.2% as measured by the Barclays Capital Municipal Bond Index. Excess supply of new-issue municipal debt securities, along with the possibility of lower tax brackets for the wealthiest investors during the Trump presidency, suppressed price gains for these tax-free dividend bonds. The Barclays Capital Global Bond Index was up 3.9% for 2016, due mainly to stabilized emerging market growth and currencies.



Portfolio Review

We are pleased to report that our SFC TIS portfolios overall registered positive returns for clients and their advisors on both an absolute (total gains) and relative (to assigned benchmarks) basis for 2016. Moreover, although our tactical positioning has been conservative by being underweighted in stocks and bonds for the year (and overweighed in cash), our investments nevertheless outperformed versus the respective stock and bond benchmarks. Also, investing approximately a third of excess portfolio cash in stocks near the February market low resulted in additional profits. And about 20% gains from natural resources/precious metals holdings added to a solid performance in 2016. A detractor from returns was an alternative investment in a hedged structured emerging markets note bought in September (accounts over $25,000); down about 5% for the year. Overall, alternative investments in long/short funds and a newly purchased U.S. stock options fund only added slightly to portfolio gains for 2016.

For the fourth quarter, the following changes were made to SFC TIS portfolios:

> Adding 361 Global Long/Short Equity Fund Inv. AGAQX. (Selling comparable TFS Market Neutral Fund TFSMX.)

> Adding Glenmede Secured Options Portfolio GTSOX

> Adding JP Morgan Mid Cap Value (JAMCX). (Selling approximately 50% of PRIMCAP Odyssey Aggressive Growth POAGX (accounts over $100k), or Schwab U.S. Mid Cap ETF (SCHM)/Vanguard Mid Cap ETF (VO) (accounts between $25k to $100k).
> Adding Schwab Emerging Markets Equity (SCHE)/Vanguard FTSE Emerging Markets ETF (VWO) to accounts under $25k. (Accounts over $25k have the JP Morgan structured note tied to equity emerging markets iShares MSCI Emerging Markets ETF (EEM).

As discussed in recent *Investment Insights* and *Market & Portfolio Update* pieces, odds are we will be in a volatile stock market in the short- to mid-term, albeit hopefully trending upward. It is possible that we'll experience a bear market at some point in the coming years as this bull market cycle is now 7 years old—the second longest on record, according to Bespoke Investment Group—and thus is historically due for a pullback at some point. And although cautiously optimistic (for additional reasons mentioned in the next Market Outlook section), it's best to be conservatively positioned with broad diversification in different asset classes (including alternative investments and natural resources) to mitigate risk while achieving a reasonable return to help advisors and their clients reach long-term goals.

Market Outlook

The first few months of 2017 are going to be more important, as we read the tea leaves, than the past few months.
—Jim Tierney, CIO of U.S. Growth at AllianceBernstein Holdings LP

We begin 2017 with a regime change that brings with it investor optimism that pro-business policies will spur economic growth and new jobs. President-elect Trump tweets and markets listen for now, but ultimately company stock values thus future prices are dependent on a jump from the anemic 2% gross domestic product (GDP) rate of the past 10 years to a 3%+ annual advance, as Mr. Trump has promised. Three percent and higher growth rates historically have propelled corporate profits. Two percent GDP or less typically has suppressed corporate profits. So just a 1% difference in GDP growth is therefore critical to continued stock gains in 2017, especially since stock prices in general are already fully valued. Shares of companies in the S&P 500 index traded at an average of roughly 21 times its past 12 months of earnings at year end, above its 10-year average of 16, according to FactSet.

U.S. GDP did advance at a 3.5% annualized rate in the third quarter, according to the Commerce Department. It was the strongest reading in two years and followed three straight quarters of sub-2% growth. The unemployment rate has fallen to 4.6%, and U.S. corporate earnings are growing after several quarters of declines.

Brighter economic prospects have boosted the dollar late last year. The WSJ Dollar Index, which measures the dollar against a basket of 16 other currencies, was up 3% in 2016. However, a strengthening U.S. currency could threaten the nascent recovery in U.S. corporate earnings by making U.S. exports more expensive to foreign buyers and reducing the value of companies' overseas revenues. So the value of the dollar versus other major currencies in 2017 will be a factor in helping or hurting U.S. stocks. Foreign stock prices, for U.S. investors, are also hurt by a strong dollar.

Overseas in Europe, there are reasons some analysts think that this year will offer a disappointing repeat performance of the last. Like with Brexit, anti-euro parties could score big wins in French, Dutch and German elections, putting the future of the European Union in question and risking a blow to the region's growth. Still, other analysts foresee possible decent economic growth and a strong performance from European banks that could be just what investors have hoped for. And unlike the Federal Reserve, the European Central Bank (along with the Bank of Japan) continue to keep borrowing rates historically low, and buy back domestic securities to prop up economic growth plus stock and bond prices. Also, stocks listed on the Euro Stoxx index now trade cheaper than their counterparts on the S&P 500 index, making European stocks more attractively priced. It's also important to note that the most favorably valued global equity market is emerging markets, and investors (such as ourselves) have taken notice.

The outlook for investment-grade U.S. government and corporate bonds in 2017 is less favorable than stocks. Especially if improved economic and employment wage growth continue. The Federal Reserve held off on raising interest rates for most of the year before moving in December for the first time since the end of 2015, which helped to support debt security prices. The Fed also signaled more increases are on the way, reflecting optimism about the U.S. economy. If Fed hikes come to fruition this year, bond prices will most likely come under pressure.

In light of the above factors we remain cautiously optimistic, somewhat conservatively positioned, and well-diversified with many asset class investments in financial advisors clients' accounts. Our belief is that actions during the first six months or so of a Trump administration will set the tone for markets mainly in the U.S., but also possibly across the globe. As always, we will be observing these events and making portfolio adjustments as warranted.

We appreciate your continued confidence. Your inquiries are welcomed.

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Sources: Bloomberg Commodity Index, *Tables & Charts*, December 2016; First Trust Advisors, *Quarterly Investment Overview*, October 2016; Janus Capital Group, *Investment Outlook by Bill* Gross, January 2017; J.P. Morgan Asset Management; *A review of global markets and portfolio positioning in Q4 2016*, 4Q 2016; USA Today, (multiple publications); The Wall Street Journal (multiple publications).

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