Central Trust Company

THE CENTRAL VIEW

CENTRAL TRUST COMPANY IS PROUD TO PROVIDE YOU
THE FOLLOWING MARKET COMMENTARY.

January 2017

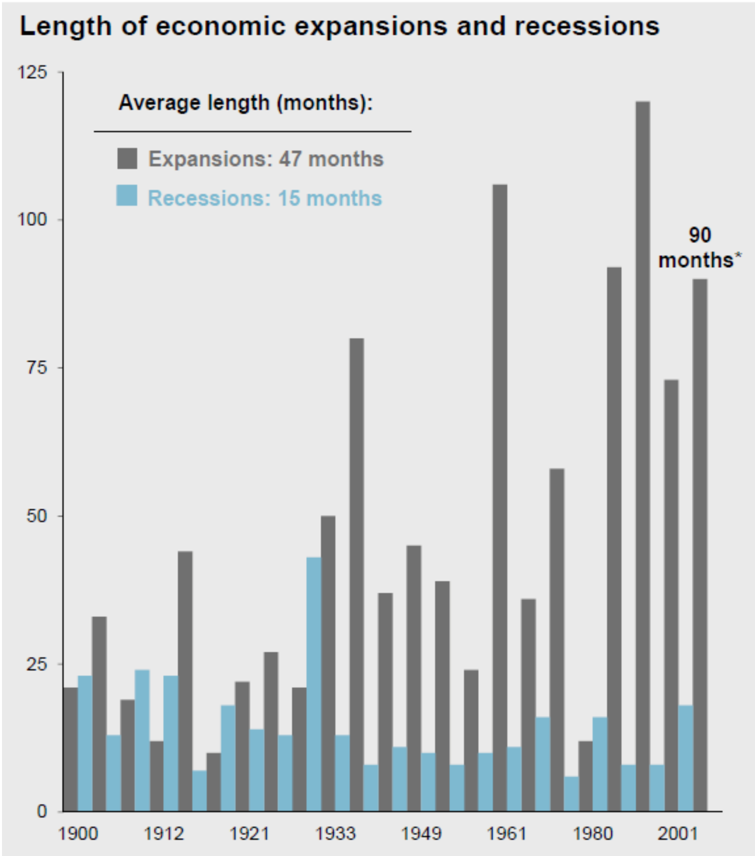
INVESTMENT OUTLOOK FOR 2017

2016 was a good year for the equity markets, especially in the U.S. The year was also filled with surprises, many of which were political including the Brexit vote, the U.S. presidential election, and the "No" vote to Italian constitutional reform. Global interest rates began to normalize from very low levels and Central Bankers began to realize that quantitative easing and negative interest rates are reaching the limits of effectiveness. On the economic front, the key development has been the strengthening in the global economy that began in the second half of 2016.

The strengthening of the global economy that began in the second half of 2016 continues as we enter 2017. The U.S. economy is now in its eighth year of economic expansion.

As we enter 2017, the global economy is warming. The U.S. economy is in its eighth year of economic expansion. In March, the current expansion will become the third longest on record since 1900 (Exhibit 1).

Exhibit 1 - J.P. Morgan



Economic growth in this recovery has been a sub-par 1.8% per year, which is below historical post-World War II expansions. Overall inflation remains low, short-term interest rates are rising, but remain extremely low, the labor market is strengthening and earnings are growing after the end of the profits recession.

The current bull market that started in March 2009 has been one of the most unloved bull markets in history. Memories of the Great Recession remain fresh in investors' minds. Since the recovery began, there have been net redemptions from domestic equity funds and ETFs every year except 2013 and 2014. The beneficiary of those redemptions have been the bond market, that has garnered nearly $1.5 trillion inflows from stock and money market funds.

The 35-year decline in interest rates has ended (Exhibit 2). U.S. yields have risen on the prospects of higher inflation and growth. This has the potential to spur a significant rotation out of bonds and into stocks that could support another leg higher in the current bull market.

A challenge for U.S. equity markets is the current valuation levels that are elevated compared to historical levels, with the current trailing price-earnings (PE) multiple at 19 times earnings compared to 15 times historically. However, stock valuations are only about one standard deviation above historical averages (Exhibit 3). Exhibit 4 illustrates that the sweet spot for valuations is zero to 2% inflation, which is the current level. Historically, if inflation rises to the 2% - 4% range, PE multiples haven't been impacted significantly.

Another potential concern for stocks is the rise in interest rates. Modest interest rate increases in 2017 can be viewed as a positive, indicating a transition from slow growth and deflation to stronger economic growth and more confidence by central bankers. Exhibit 5 shows that a modest rate increase from low levels usually doesn't hurt the stock market until yields rise above 5%.

The U.S. stock market had a strong advance post-election going into the end of the year on improving global growth and in anticipation of pro-growth legislation that could drive growth higher. We would not be surprised by a normal correction in the first few months of the year as the legislative process encounters delays tempering the current high level of investor optimism.

Overall, stronger global growth is positive for global equities and a headwind for bonds. However, uncertainties and risks remain including rising and elevated debt levels (Exhibit 6) , a potential overshoot on inflation, rising populism and limits to monetary policy.

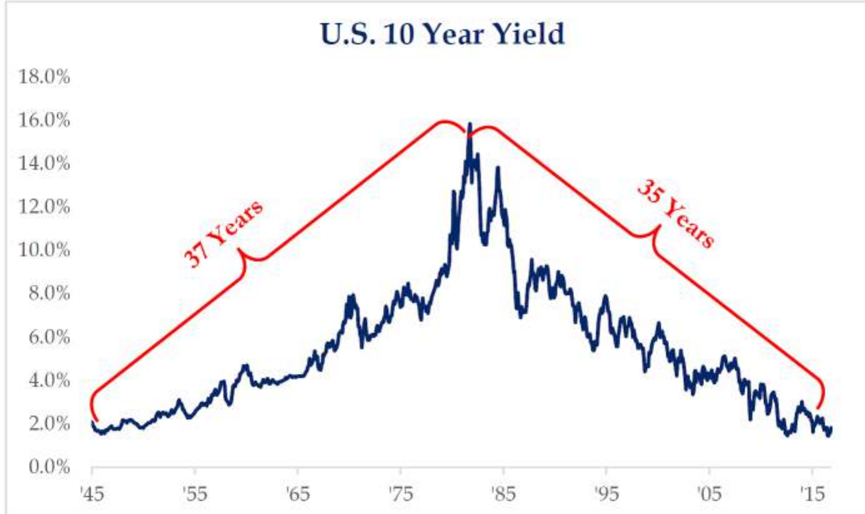


Exhibit 2 - Strategas Research Partners (12/16)

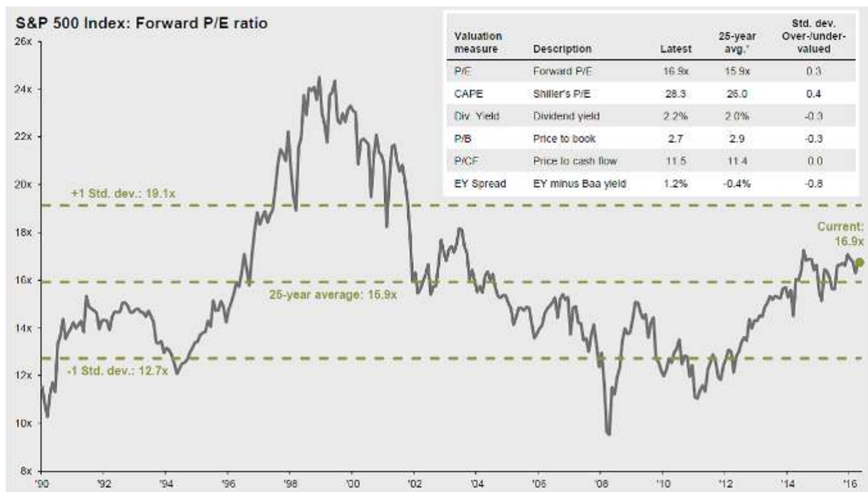


Exhibit 3 - J.P. Morgan Asset Management

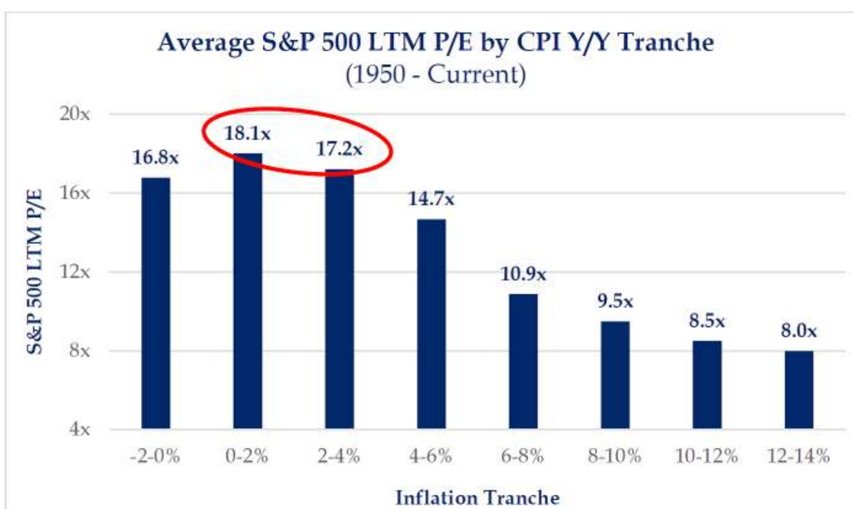


Exhibit 4 - Strategas Research Partners (12/16)

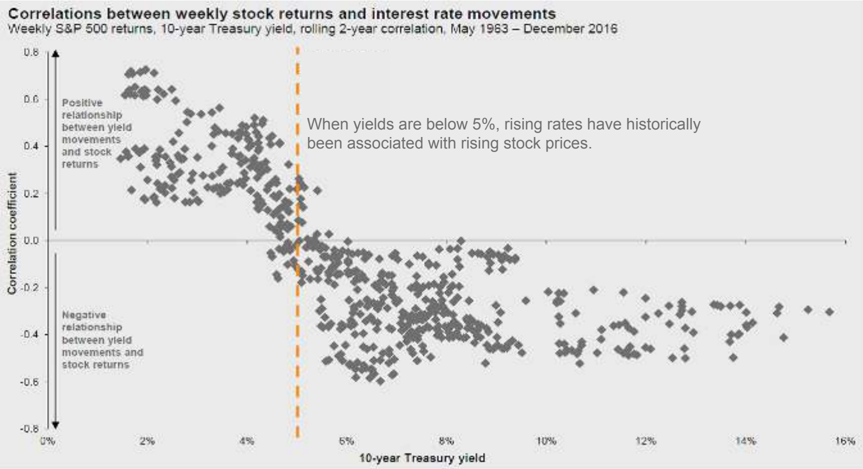


Exhibit 5 - J.P. Morgan Asset Management

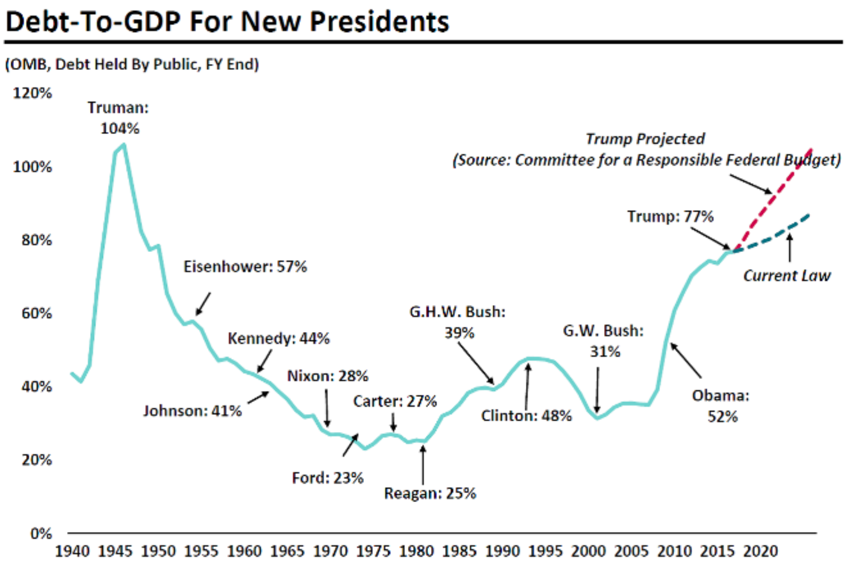


Exhibit 6 - Strategas Research Partners (12/16)

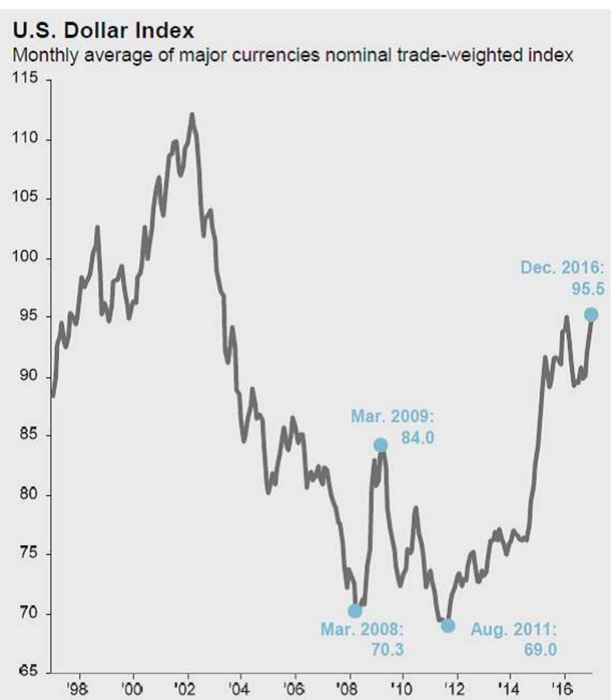


Exhibit 7 - J.P. Morgan

You can be confident that we are staying abreast of current events. Our outlook for the global markets is under continual review and will be adjusted as needed to reflect real fundamental changes, but we will stay firmly positioned when the "news" is deemed to simply be noise or distraction without relevance to investment results over the long term.

TEN MAJOR INVESTMENT THEMES FOR 2017 (BASE CASE)

As we venture forth with our **Ten Major Investment Themes for 2017,** we seek to identify the most important themes that will drive investment markets and returns in 2017. In our base case scenario for 2017, the current economic expansion continues as global growth improves over 2016. We see the reflation trend continuing into 2017. Our views are subject to revision and we will use deviations from these ten themes to make adjustments to portfolios as the year progresses.

1. U.S. and Global Growth Accelerates Modestly.

Global growth improved in the second half of 2016. Global GDP is expected to end 2016 at 3.0% and increase to 3.4 - 3.6% in 2017 as inflation picks up, fiscal policy is supportive and interest rates remain subdued. U.S. growth accelerates from 1.6% last year to 2.0 - 2.5% in 2017. Principal drivers are improving earnings; higher business investment due to corporate tax cuts and deregulation; and strong consumer spending from a further drop in unemployment, rising wages and the prospects of lower personal income taxes.

2. U.S. Dollar Strengthens.

The U.S. dollar strengthens modestly for a third straight year as U.S. growth accelerates and outpaces the Eurozone and Japan. The combination of faster growth, Fed rate increases, corporate tax reform, deregulation and fiscal stimulus attract foreign funds into the U.S. Dollar appreciation will likely be modest as President Trump has voiced concern on too strong a dollar as it hurts U.S. manufacturers and exports. The dollar is at a 14-year high (Exhibit 7).

3. Disinflation to Inflation.

The global economy shook off deflationary concerns in early 2016 and is transitioning to reflation as energy, commodities and wage growth are in uptrends. Higher inflation leads to higher consumer and investment spending in the near-term, which is supportive of risk assets. The baseline case is for inflation to rise above the 2% level in the U.S. but remain contained.

4. Treasury Yields Rise on Higher Growth and the Fed Increases Rates Two to Three Times in 2017.

The 35 year bull market in bonds and declining interest rates has likely ended. Yields will move higher but not in a linear fashion. Global central banks continue to remain accommodative with monetary policy, thereby limiting the rise in bond yields in the U.S. and globally. The U.S. 10-Yr. Treasury yield rises to over 3% by year-end.

5. Operating Earnings for the S&P 500 rise to $127 - $129 in 2017 Driving Stocks Higher.

S&P 500 operating earnings rise from $118 in 2016 to $127 - $129 in 2017 as the earnings recession ended in 2016. Stocks move higher as price-earnings multiples remain evaluated as inflation and interest rates continue to be contained.

6. Stocks Outperform Bonds as Rotation Develops.

The current bull market in stocks started in 2009. It has been one of the most unloved bull markets in history as investor's memories of 2008 remain. Since the start of the recovery, there have been net outflows from U.S. equities (mutual funds and ETFs) in five of the seven years of the recovery. Bond funds have been the beneficiary garnering inflows in six of the seven years. Since the election, as interest rates have increased, the trend has reversed as money has flowed out of bonds into stocks.

7. Populism and the Move Away from Globalization Accelerates Around the Globe.

2016 will be remembered for the rise of populism in Europe and the U.S. with the surprise Brexit vote, the U.S. presidential election and the Italian "No" vote. The trend away from globalization will intensify as countries become more inward focused in dealing with internal issues at home. Populism will continue to be an issue in Europe, which faces key votes in France in April and Germany in October of this year.

8. An All Out Trade War is Avoided.

A key concern regarding the new administration is the election talk about potential protectionist trade policies. As a base case, tensions between the U.S., China and Mexico flare but the new administration does not impose punitive tariffs that lead to a trade war. China's currency continues to depreciate but at a gradual rate of 5 - 7% in 2017.

9. Fiscal Policy Becomes Supportive for the Economy but the Implementation is Delayed Until Mid-to-Late Year.

A stimulus package in the U.S. that includes infrastructure spending is passed mid-year. The implementation takes place in mid-to-late year and is not retroactive to the beginning of 2017. Therefore, much of the impact will be in 2018, which creates a headwind for U.S. growth in 2017.

10. Major Transitions Increase Market Volatility and Divergences Among Regions and Asset Classes.

There are several major transitions underway that are increasing volatility and divergences in the markets. First, monetary policy is beginning to become less effective while pro-growth fiscal policy is taking center stage in the U.S. with a new administration. Second, the move from deflation to reflation is causing divergences across asset classes and regions. Thirdly, globalization is waning as countries become more focused on internal issues. The combination of these major transitions will influence the economy and investment markets in 2017.

ASSET ALLOCATION VIEWS AND PORTFOLIO POSITIONING

The following are our current views on asset allocation. The implications to your portfolio may vary depending on your particular individual situation. Please consult with your Central Trust Company financial advisor. We build portfolios by utilizing five major asset classes: equities, fixed income, real assets, alternatives and cash.

Asset Allocation

As we enter 2017, the global economy is experiencing somewhat higher growth, rising inflation and higher interest rates. U.S. economic growth and inflation is trending higher, which could be accelerated by the new administration's pro-growth fiscal policies. U.S. corporate earnings are expected to grow 7 to 10%, without any benefit from new fiscal stimulus. Overall, this combination is positive for global equities and negative for bonds. We expect stocks to outperform bonds over the next 12 - 18 months.

The U.S. dollar should be boosted by rising yields in the U.S. Risks remain elevated resulting in a wider range of potential outcomes on both the downside and upside. Against the backdrop of uncertainty and a range of possible scenarios, portfolio positioning will emphasize diversification to mitigate market volatility.

Overall, our asset allocation has a small overweight to equities, is underweight fixed income, market weight real assets and market weight alternatives. Higher levels of cash provide higher liquidity to dampen volatility and take advantage of opportunities.

Investment Returns

Due to the combination of slower than historical global growth, high levels of debt, and generally fair to full valuations, we think investors should expect more modest investment returns across almost all the major asset classes over the intermediate term.

Equities

In the near term, stocks are benefiting by a pickup in growth and the prospects for fiscal stimulus and deregulation that would increase GDP growth. In the long run, earnings are the main driver of stock prices. With growth improving and corporate earnings projected to rise in 2017, equities should trend higher following earnings. We are cautious in the near term and would not be surprised by a pullback in the market based on the year-end advance and high level of investor optimism. Historically, the stock market has a 10% correction about once a year, which is normal in an uptrending market.

While we continue to favor equities, we reiterate our view that volatility will increase in global equity markets as monetary policy exhaustion increases and the transition to fiscal policy occurs causing interest rates to trend higher toward more normal levels. We continue to favor domestic equities and are cautious on the Eurozone due to political, monetary policy and trade related risks. We are more constructive on emerging markets as growth and inflation accelerates and valuations are low.

Fixed Income

A reflationary outlook and modest interest rate increases are a positive for growth and are good for financial markets. However, this is a challenging environment for fixed income. Investment grade core fixed income provides stable income and acts as a hedge against growth sectors of a diversified portfolio during an economic downturn. Traditional core fixed income is important as we are in the late cycle of the current U.S. expansion that is 90 months old. We favor TIPS (Treasury Inflation Protected Securities) as they are a good hedge against inflation. We have an underweight to duration to lessen interest rate sensitivity.

For diversification, we utilize the Credit sector of fixed income that has less interest rate sensitivity. High-yield bonds offer attractive yields despite spreads being near full value. Floating rate bonds have yields that increase when interest rates rise offering protection in a rising rate environment. International core fixed income is avoided due to the lower levels of interest rates relative to the U.S. and the foreign currency risk from a rising dollar.

Real Assets

Real assets provide inflation protection and are a portfolio diversifier. Our allocation to gold acts as insurance during periods of financial uncertainty.

Alternatives

The alternative strategies we utilize in building portfolios are designed to lower portfolio volatility and improve portfolio efficiency due to low correlations with other asset classes. Alternatives act as a hedge in volatile markets and provide better performance in a rising interest rate environment than bonds.

Cash

Portfolios will typically have a small amount of cash due to interest income and dividends being generated. At times, higher allocations of cash are beneficial to decrease portfolio volatility and provide a source of funds for purchase of attractive opportunities.

MARKET RECAP FOR THE YEAR 2016

In 2016, nearly all asset classes posted gains, with stocks outperforming bonds. Markets started the year weak (falling stock prices, interest rates, and oil) and ended the year strong (rising stock prices, interest rates, and oil). The U.S. Dollar rose 3.7% benefiting U.S. Investments. The dollar reached its highest level since 2001.

The year 2016 can be broken down in three parts:

- **Recession Fears:** In January, growing concerns over plunging oil prices, a China hard landing, and the Fed targeting four rate hikes in 2016 drove the S&P 500 down over 10% by early February.
- **Stabilization and Recovery:** Markets found a low February 11th. Earnings began to trough, oil made a low and began to recover, and the Fed backed off four rate hikes. In June, the recovery was temporarily halted as the surprise Brexit vote caused a two day plunge in stocks before recovering. Interest rates reached a low around the Brexit vote and began to trend higher as growth started to warm up.
- **Post-Election Rally:** Based on the pro-growth agenda of the new administration and hopes for a large fiscal stimulus program, stocks rallied strongly gaining 5% into the year-end.

Exhibit 1: Equity *Trailing Performance (Annualized when > 1 year)*

Asset Class	Index	QTD	YTD	1Y	3Y	5Y	10Y
Equity	MSCI All Country World IMI	1.3%	8.4%	8.4%	3.2%	9.6%	3.8%
Large Cap	S&P 500	3.8%	12.0%	12.0%	8.9%	14.7%	6.9%
Styles	Russell 1000	3.8%	12.0%	12.0%	8.6%	14.7%	7.1%
	R1000 Growth	1.0%	7.1%	7.1%	8.5%	14.5%	8.3%
	R1000 Value	6.7%	17.3%	17.3%	8.6%	14.8%	5.7%
Sectors	Real Estate	-4.4%	1.1%	1.1%	8.9%	8.1%	0.8%
Long-Short	S&P 500 / LIBOR plus 3	2.4%	7.7%	7.7%	6.1%	9.0%	5.5%
Small/Mid Cap	Russell 2500	6.1%	17.6%	17.6%	6.9%	14.6%	7.7%
Mid Cap	Russell Mid Cap	3.2%	13.8%	13.8%	7.9%	14.7%	7.8%
Small Cap	Russell Small Cap	8.8%	21.3%	21.3%	6.7%	14.5%	7.1%
International	MSCI World Ex US (net)	-0.4%	2.7%	2.7%	-1.6%	6.1%	0.9%
Emerging Markets	MSCI Emerging Markets (net)	-4.2%	11.2%	11.2%	-2.6%	1.3%	1.8%

Source: Central Trust Company

Equities: Stocks posted solid gains in 2016 ending near-record highs in the U.S. In 2016, the S&P 500 gained 9.4% (11.9% with dividends) and the MSCI All Country World Index advanced 8.4%. International developed equity markets gained 2.7% as the U.S. continued to outperform. Emerging markets declined in the fourth quarter on higher interest rates and a rising dollar reducing the gain for the year to 11%. The U.S. market is triple the level of the lows reached in 2009.

Equity markets were marked by major reversals in 2016. The market was led by defensive sectors (energy, staples, telecom, and utilities) in the first half of the year. Leadership dramatically reversed in the second half as cyclical sectors (financials, industrials,technology, and materials) led. Value outperformed Growth significantly in 2016 by 1051 basis points reversing a multi-year trend. Small Cap outperformed Large Cap. Quality stocks underperformed as lower quality, economically sensitive stocks jumped on the reflation theme.

Fixed Income: Bond markets also experienced a trend reversal last year as the 35-year decline in interest rates likely ended. Yields hit a low mid-year and then spiked over 100 bps from a low of 1.32% in July to end the year at 2.44% on the U.S. 10-year bond on stronger economic growth and inflation. In 2016, the Barclays Aggregate Index gained 2.6%. TIPs outperformed almost doubling the return of Treasuries gaining 4.8% as inflation accelerated from low levels. The credit sector was very strong as spreads tightened from early 2016 leading to gains in high-yield of 17.1%, floating rate debt of 10.2%, and emerging market debt of 10.2%.

Exhibit 2: Fixed Income *Trailing Performance (Annualized when > 1 year)*

Asset Class	Index	QTD	YTD	1Y	3Y	5Y	10Y
Global	Citi World Broad Investment Grade	-6.6%	1.9%	1.9%	-0.2%	0.3%	3.4%
U.S. Aggregate	Barclays US Aggregate	-3.0%	2.6%	2.6%	3.0%	2.2%	4.3%
Money Market	Citigroup 1-month T-Bill	0.0%	0.2%	0.2%	0.1%	0.1%	0.6%
U.S. Government	Bloomberg Bond Index US Govt (ST)	-0.5%	0.9%	0.9%	0.7%	0.6%	2.2%
	Bloomberg Bond Index US Govt (IT)	-2.1%	1.3%	1.3%	1.7%	1.1%	3.8%
	Bloomberg Bond Index US Govt (LT)	-11.7%	1.1%	1.1%	7.8%	2.5%	6.7%
U.S. TIPS	Citi U.S. Inflation Linked Securities	-2.7%	4.8%	4.8%	2.5%	0.9%	4.4%
Tax Exempt	S&P Municipal Bond Index	-3.3%	0.8%	0.8%	4.4%	3.6%	4.2%
U.S. Corporate	Barclays iShares Intermediate Corp	-2.1%	3.3%	3.3%	2.6%	2.9%	0.8%
U.S. Corp High Yield	Barclays US Corporate High Yield	1.8%	17.1%	17.1%	4.7%	7.4%	7.5%
U.S. Floating Rate	S&P/LSTA Leveraged Loan	2.3%	10.2%	10.2%	3.6%	5.1%	4.6%
International	Citi Non USD WGBI	-10.8%	1.8%	1.8%	-2.2%	-1.9%	2.5%
Emerging Markets	JPM Emerging Markets	-4.2%	10.2%	10.2%	5.6%	5.4%	6.8%

Source: Central Trust Company

Real Assets: Real assets rebounded on the reflation theme as recession concerns receded, energy prices recovered and prospects for growth improved. Commodities gained 11.8% as growth and inflation picked up. Gold corrected from the highs reached mid-year to close with a 7.7% gain for the year. Gold benefits from financial uncertainty. Oil had a major recovery as it doubled from its early year low and ended the year at $53 per barrel.

Exhibit 3: Real Assets *Trailing Performance (Annualized when > 1 year)*

Asset Class	Index	QTD	YTD	1Y	3Y	5Y	10Y
REAL ASSETS	Gold	-12.7%	7.7%	7.7%	-1.9%	-6.5%	5.3%
Inflation	Consumer Price Index	0.6%	1.8%	1.8%	1.1%	1.3%	1.8%
Commodities	Bloomberg Commodities	2.7%	11.8%	11.8%	-11.3%	-9.0%	-5.6%
Silver	LBMA Silver Price	-16.1%	17.5%	17.5%	-5.9%	-10.4%	2.3%

Source: Central Trust Company

Alternatives: Alternatives provide additional stability to portfolios by enhancing diversification and reducing volatility due to low correlations with other asset classes. They are an attractive alternative to traditional fixed income in a rising interest rate environment.

Exhibit 4: Alternatives *Trailing Performance (Annualized when > 1 year)*

Asset Class	Index	QTD	YTD	1Y	3Y	5Y	10Y
ALTERNATIVES	LIBOR + 3	0.9%	3.5%	3.5%	3.3%	3.3%	4.0%
Conservative	Hedge Fund Reseach HFRI FOF	1.2%	1.5%	1.5%	1.7%	3.4%	1.2%
Multi-Strategy	HFRI Multi Strategy	0.0%	4.7%	4.7%	2.9%	4.9%	3.6%
Global Macro	Credit Suisse Global Macro Ind	3.5%	2.5%	2.5%	1.9%	2.9%	5.7%
Managed Futures	Credit Suisse Managed Futures	-5.8%	-7.0%	-7.0%	2.9%	0.6%	2.7%

Source: Central Trust Company

Written by:
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Please consult with your Central Trust Company advisor for more guidance on how Central Trust can tailor solutions for your particular needs based on these evolving economic and market conditions.

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