Argent
Wealth Management, LLC

Investment Outlook

SPRING 2017

Second Quarter 2017 Outlook; First Quarter 2017 Review

The Trump Bump Continues; Will it Last?

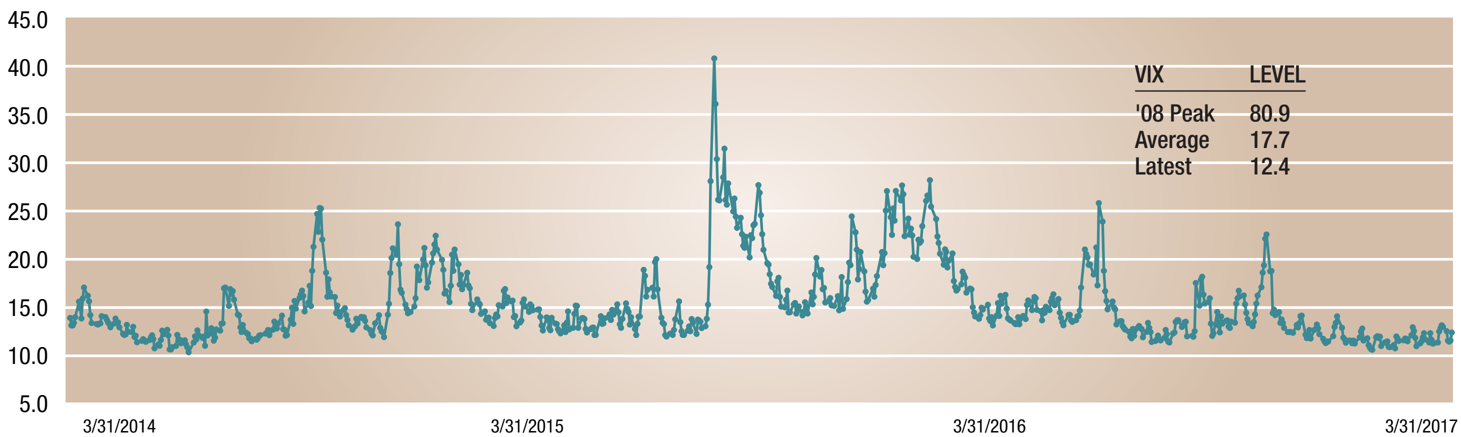
Equity markets and other risk assets, like High Yield bonds, enjoyed another excellent quarter. It has been a straight line higher since the surprise election victory. Measures of complacency and investor sentiment, such as the VIX, have also experienced an unusually long period of euphoric readings.

Undoubtedly, the prospect of business-friendly policies, such as regulatory relief and tax cuts have been a positive catalyst. Importantly, other factors have also been supportive. The global economy has been on an improving path, even before the Trump victory. Economic momentum has continued to broaden both in the U.S. and abroad. In fact, many of the best performing markets have been outside the U.S. Obviously, that would not have been the case if this was just a U.S. centric story.

A critical question now is how much of this potential good news is already built into elevated asset prices?

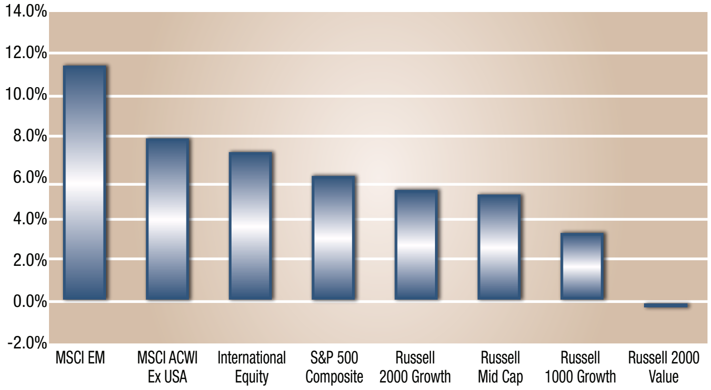
Starting with U.S. equity markets, we believe that the market has been rational to positively react to the combination of tax cuts, regulatory relief, and a more robustly expanding economy. However, valuation is now stretched to the upper limits of what we believe is reasonable. That does not suggest that markets are setting up for a major bear market. Rarely do full blown bear markets occur outside of recessions (or market bubbles), and that is not on the horizon any time soon. A much more likely scenario is a short and uncomfortable correction of maybe 5% or 10%. To be fair, we are surprised that such a normal correction within the context of a "cyclical bull" market has not already occurred.

Market Volatility (VIX)



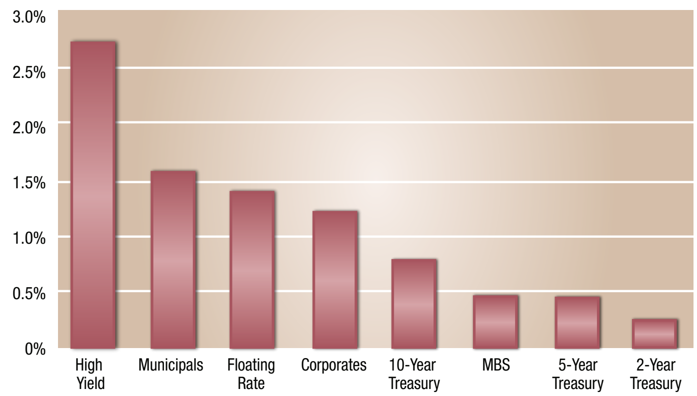
Source: Yahoo Finance, JPM; Chart: Argent Wealth Management, LLC © 2017

Global Equity Returns Quarter to Date



Source: Morningstar; Chart: Argent Wealth Management, LLC © 2017

Fixed Income Returns Quarter to Date



Source: Morningstar; Chart: Argent Wealth Management, LLC © 2017

Many International and Emerging equity markets have performed better than U.S. markets and remain more favorably positioned. Valuation levels in these markets are considerably lower. More importantly, many of these markets have the potential for a greater acceleration in earnings growth if economic strength continues to broaden. It must be noted that these markets also have greater political risk factors such as key looming elections in France and elsewhere. As such, we remain appropriately diversified but would not increase our allocations, until and unless, trends become more firmly entrenched.

Valuation Measure	Description	Latest	25-Year Average	Std. dev. Over/ under-valued
P/E	Forward P/E	17.5x	15.9x	0.5
CAPE	Shiller's P/E	29.0	26.1	0.5
P/B	Price to book	2.9	2.9	-0.1
P/CF	Price to cash flow	12.2	10.6	0.8

Source: JPM, S&P 500 Data as of 3/31/2017; Chart: Argent Wealth Management, LLC © 2017

Fixed income markets had a reasonable quarter, despite overwhelming expectations that yields would rise. On the top of the fixed income pack were High Yield and Senior Secured Loans. These are areas that we have been aggressively overweight since the oil related meltdown of 2016. Valuation has now moved definitively into expensive territory, particularly within High Yield. As such, we have been systematically reducing allocations.

We remain quite defensively positioned within higher grade fixed income markets, such as Treasury and Municipal Bonds. We do expect yields to rise (and prices to commensurately fall), although we never expected that to be a straight-line deal. As we noted in our last report, global inflation while rising remains extremely low and contained. That puts a limit as to how far yields can rise. We remain inclined to add to our higher grade fixed income allocations as the Fed continues down a path of increasing interest rates (more about that later).

	Average (1958-YTD 2017)	3/31/2017
Nominal Yields	6.14%	2.40%
Real Yields	2.40%	0.18%
Inflation	3.73%	2.22%

Source: JPM; Chart Argent Wealth Management, LLC © 2017

Fiscal Stimulus and a More Robustly Expanding Economy Could Result in a More Vigilant Fed

A critical potential offset to fiscal stimulus is the possibility of a more active and vigilant Fed. The Fed did bump the Fed Funds rate 25 basis points at their last meeting in March, ahead of what most analysts were expecting. More importantly, Chairwoman Yellen upgraded her expectations of economic strength and nudged upward the potential path of increases in 2017 to the possibility of four times.

An important factor in the interest rate path of the Fed is central bank policy in Europe and Asia. We live in a world of global interest rates. U.S. interest rates simply cannot rise that far without European and other rates moving away from the current zero bound rate policy.

Currency markets are the key linkage and transmission mechanism. If our Fed were to move in isolation the dollar would rally sharply as foreign investors would be attracted to our higher interest rates. That would exert downward pressure on prices, widen credit spreads, and depress corporate earnings. That is exactly what happened immediately following the first increase in Fed Funds in December 2015. Effectively, the market tightened monetary policy much more than the Fed intended.

Europe now appears on more solid footing. The dollar declined marginally versus the Euro during the first quarter and was a key factor in the Fed's ability to move. The fact that risk markets and the dollar did not adversely move this time around is a very good sign. A faster path of increases may be forthcoming, if Europe can continue to heal. We will be watching closely.

Fixed Income Markets; the Role of High Grade Bonds in a Diversified Portfolio

While we do expect Treasury and other higher grade bond yields to rise this year, we have always expected that rise to be irregular. We are not at all surprised that yields have declined marginally over the last several weeks (from 2.62% to 2.40% on a 10-year Treasury bond). This decline in yields occurred even as the Fed bumped up the short-term interest rate.

Such a "flattening" of the yield curve can only go on so long during an expanding economy. Major flattening or inversions of the yield curve (where long-interest rates are higher than short-term interest rates) typically precede recessions. That is highly unlikely at the current time.

Precise timing of an expected rise in yields is impossible. The June Fed meeting is on the table as long as economic momentum remains robust. Additionally, any hints of less accommodative policy from the ECB would set the stage for normalization of yields globally. That could come as early as after the French elections.

Importantly, that rise in yields will likely be less dramatic than in past cycles. Global inflation remains structurally depressed. Our current view is that a 3% yield on a 10-year Treasury Bond would be adequate to restore quite a bit of value back into the higher grade fixed income markets. We expect to be adding "duration" to our portfolios.

Higher grade fixed income (Treasuries and Municipals) play an essential role within a properly diversified portfolio. That role is not to produce higher returns than risk assets. It is to provide the critical "insurance policy" against market pullbacks. Fixed income allocations are designed to make owning risk assets more comfortable over full market cycles and no other asset category plays that role better.

Global Purchasing Managers' Index for Manufacturing

	Jan. '16	Feb. '16	March '16	April '16	May '16	June '16	July '16	Aug. '16	Sept. '16	Oct. '16	Nov. '16	Dec. '16	Jan. '17	Feb. '17	March '17
Global	50.9	50.0	50.7	50.2	50.1	50.4	51.0	50.7	51.0	51.9	52.0	52.7	52.7	53.0	53.0
Developed Markets	52.3	50.9	50.9	50.4	50.2	50.9	51.5	51.3	51.6	52.9	53.2	54.0	54.4	54.6	-
Emerging Markets	49.2	48.8	50.0	49.5	49.5	49.3	50.1	49.9	50.0	50.7	50.7	51.3	50.8	51.3	-
U.S.	52.4	51.3	51.5	50.8	50.7	51.3	52.9	52.0	51.5	53.4	54.1	54.3	55.0	54.2	53.3

<50 50-50.9 51-51.9 52-52.9 >53

Source: JPM; Chart Argent Wealth Management, LLC © 2017

How Will Equities and Other Risk Assets Respond to Rising Yields?

Traditionally a rise in yields from very low levels is a positive catalyst for equities and other risk assets such as High Yield bonds. That makes perfect intuitive sense as it is a signal of a more robustly expanding economy and the anticipation of faster earnings growth. But as yields continue to rise there is almost always an "inflection point" whereby additional increases are problematic.

It is foolish to think that we (or anyone else) has a perfect handle of where that inflection point is. Our instinct and analysis suggests that markets are still in a sweet spot for a while longer as yields are still too low to be realistic competition versus equities. The positive factor of accelerating corporate earnings should still be a more powerful influence.

> ***"Fixed income allocations are designed to make owning risk assets more comfortable over full market cycles and no other asset category plays that role better."***

Having said that, we also believe that the inflection point may occur at lower yield levels than in past cycles. Short-term interest rates have been anchored at zero for an extraordinarily long time. The demand for income assets has never been higher given an aging demographic. These factors do suggest that there may be significant reallocation of assets from equities to higher grade fixed income as yields become more normal.

Portfolio Construction/Rebalancing

Pulling all of these factors together, we have been moderately reducing risk allocations this past quarter and harvesting gains from some areas, such as High Yield bonds that have performed exceptionally well. We have also maintained the discipline of rebalancing client portfolios. As equities have surged these past two quarters, risk weights have increased materially. Pulling monies away from those areas that have done the best (and have grown in weight) is the most important discipline in our process. It is the "secret weapon" and has been proven by countless studies to significantly add value compared to a fixed or static allocation.

We are also taking a more careful and cautious approach with respect to investing any new monies. Generally expensive markets and a less accommodative Fed results in less than ideal conditions for adding risk.

This does not mean that we are massively bearish or abandoning long term (strategic) goals. Lower than normal positive returns are a whole lot better than near zero returns from cash. For now, it is about a somewhat higher degree of caution and a commensurately higher degree of liquidity. A reasonable correction within risk markets would be an excellent opportunity to be adding to risk allocations. We did that successfully during last February's correction.

Fortunately, corrections never occur evenly or rationally. There is always some asset class that becomes unusually attractively valued and we take great pride in finding those bargains.

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All of us at Argent thank you for your continued support and confidence. If you know of anyone that might benefit from Argent's services, we would welcome the opportunity to discuss their particular situation with them.