DANN ASSET ADVISORS, LLC

Third Quarter 2016 Update

October 14, 2016

3Q16 Highlights

- U.S. economic growth accelerates following a weak first half
- Fed continues to be “data dependent” as it considers raising rates
- Stock market has a remarkably tranquil quarter with a bias to the upside
- Interest rates bounce slightly from record low levels
- Clinton leading but election still a wild card

The table below summarizes the performance of some key indices during the third quarter and year to date:

Market Performance		
Index	% Ch. 3Q16	% Ch. YTD
S&P 500	3.9	7.8
MSCI Developed Markets (excl US)	6.4	1.7
MSCI Emerging Markets	9.0	16.0
MSCI All Country World	5.4	7.1
US Aggregate Bond (1)	0.5	5.8
Liquid High Yield (1)	5.1	13.8
US Dollar Emerging Markets Bond (1)	3.9	15.1

(1) Barclays indices

Equities. The third quarter marked the third consecutive quarter of modest gains for U.S. stocks, with the large cap S&P 500 index returning 3.9% for the three months. All of the gain came in July as the market digested and quickly recovered from the British vote in late June to leave the European Union. During August and most of September the markets were quiet, with fluctuations appearing to be driven by perceptions around if/when the Fed might raise rates.

International markets were relatively stronger than the U.S. We believe this partly reflects a weaker U.S. dollar (especially relative to several emerging market currencies) and economic data showing that Brexit is not leading to immediate economic slowing in Europe. We note that Britain has not given the EU formal notice of the exit decision, meaning we’re at least two years away from Britain leaving and the potential for more significant economic impacts. Weakness in the British pound may accelerate some of those impacts.

Emerging markets continued to be the leading geography in 2016, with stronger currencies, firming commodity prices and relatively better valuations likely key reasons. Brazil, Indonesia and Russia have been among the best performing markets. Their strong gains follow several years of significant declines.

Fixed income. Although yields bounced around a bit the 10-year U.S Treasury yield ended the quarter at 1.61%, close to unchanged from 1.51% at June 30. Intra-quarter fluctuations seemed driven by the release of economic indicators and investors’ perceptions about what those indicators might mean for the Fed’s monetary policies. Year to date the Barclays U.S. Aggregate Bond index (with a 5.3 year duration) has returned 5.8%. As indicated in the table more speculative sectors of the bond market have done substantially better.

General comments. Aside from a moderate downturn early in the year and a brief decline in June (Brexit), the market generally has moved up quietly through the year. The 7.8% return to September 30 marks the top end of what we'd been expecting for all of 2016 – not a bad year so far. But with earnings having declined year to date, the market's gain has been fueled by expansion in the multiple of what investors are willing to pay for lower earnings. Ultra-low interest rates likely are the driving force behind the multiple's expansion.

We believe the market would go through a period of volatility if Trump were to win the election. Beyond that, as always, the keys to the market will be interest rates, earnings and the strength of the economy. At this point we don't see anything that will cause earnings or the economy to break out significantly to the upside. As a result we continue to see modest gains at best for the market over the near to intermediate term.

Portfolio Positioning

At the risk of sounding like a broken record, we again took no significant actions in fixed income during the quarter. Even though longer duration fixed income has been the place to be in 2016, we're not comfortable increasing duration at this point. Given the foregoing, the fixed income component of most diversified (fixed income and equity) portfolios remains largely in short duration (three years and under), investment grade corporate and municipal bond funds. Complementing this conservative positioning is still modest exposure to intermediate term (five-to-six year duration) investment grade funds and small positions in more aggressive, credit-sensitive short duration funds.

The best performing broad U.S. market sectors during the third quarter were technology, materials and industrials, a potentially significant shift from a market that over the first half of 2016 had been led by high dividend stocks and stocks of companies that often rise when interest rates fall. This shift to more economically sensitive stocks may be indicating better times ahead for the economy. However, we note two items: 1) technology, which returned roughly 13% in the quarter, was led by the biggest companies with Apple, Alphabet (formerly Google) and Microsoft each up at least 13% (together these companies represent 32% of the sector and have an outsized impact), and 2) materials and industrials each were up less than 5% - so not substantially outperforming the market. However, if these leadership trends continue we believe implications for the economy would be positive. Utilities, telecommunications and consumer staples were the worst performing sectors.

Year to date, energy, utilities and materials were the top performers. Utilities likely benefitted from falling interest rates. Energy and materials entered 2016 at depressed levels and have been rebounding with the price of commodities. Healthcare is only just positive for the year and the weakest sector to date, likely because of high profile negative publicity around some companies' pricing strategies and politicians focusing on the industry during an election year. Financial and consumer discretionary stocks represent the other two lagging sectors, up roughly 3.5%.

We had another quiet quarter for equity-only accounts. The only action we took common to a number of equity-only accounts was to sell a small portion of a consumer staples, indexed exchange traded fund where we believed that many of the stocks held by the fund were close to fair value. Proceeds were left in cash or put into already-owned mutual funds.

Economy

U.S. GDP growth increased from 0.8% in the first quarter to 1.4% in the second. The increase was led by consumer spending, which rebounded strongly to 4.3% following a weak first quarter.

This gain was partially offset by a drop in inventory accumulation and lower government spending. Business investment and trade both were modest positives, partly reversing significant declines in 2015 into early 2016.

Analysts currently are projecting third quarter GDP (to be reported later this month) to grow 2.5%-3.0%. While consumer spending likely slowed from the second quarter pace, inventory replenishment and possibly continuing favorable trade figures (helped by a weaker U.S. dollar) could improve third quarter results. Recent employment and wage reports have been supportive of at least stable, if not increased growth.

Compared with most other developed economies, the U.S. continues to look robust. During the second quarter, the euro zone and Japanese economies grew only 0.3% and 0.2%, respectively. Ironically, even with the Brexit vote, the U.K. economy was one of the fastest growing at 2.2%. In developing economies, China's growth perhaps not surprisingly is coming in around the 6.5% projected by the government.

In our opinion central bank policies have supported markets in 2016 – one only has to look at the market's reaction to individual economic numbers or Fed statements in recent months. We find it more difficult to tell if these policies have improved economies as intended, and believe that fiscal stimulus would have more of a positive impact at this point.

Absent fiscal stimulus (unlikely until 2017 at the earliest) we are hard pressed to see reasons for a sustainable pick up in growth. Despite our outlook, we get the impression that the Fed would like to raise rates by year end if for no reason other than to have a cushion to reduce rates should the economy slow. While a rate increase could move the markets near term we don't believe it would have a material impact on the economy.

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