Quarterly Market Review

Fourth Quarter 2017

THE MILESTONE GROUP
Wealth Through Discipline

Asset Class Performance

Commodities were the best performing asset class for the final quarter of 2017, with a return of 9.9% driven partially by a weakening US dollar. However, commodities are still the worst performer over the previous decade, returning -10.2% annualized. Foreign and domestic stocks outperformed bonds in the fourth quarter as the narrative of synchronized global growth continued to take shape. Emerging Markets once again had a strong quarter returning 7.4%, as well as being the best asset class for 2017 with a return of 37.3%.

The Federal Reserve raised rates for the third time in 2017, hiking the Federal Funds target range to 1.25% to 1.50% which put pressure on bond prices. MLPs were the worst performer with a return of -2% on the quarter and a -7.9% return for 2017.

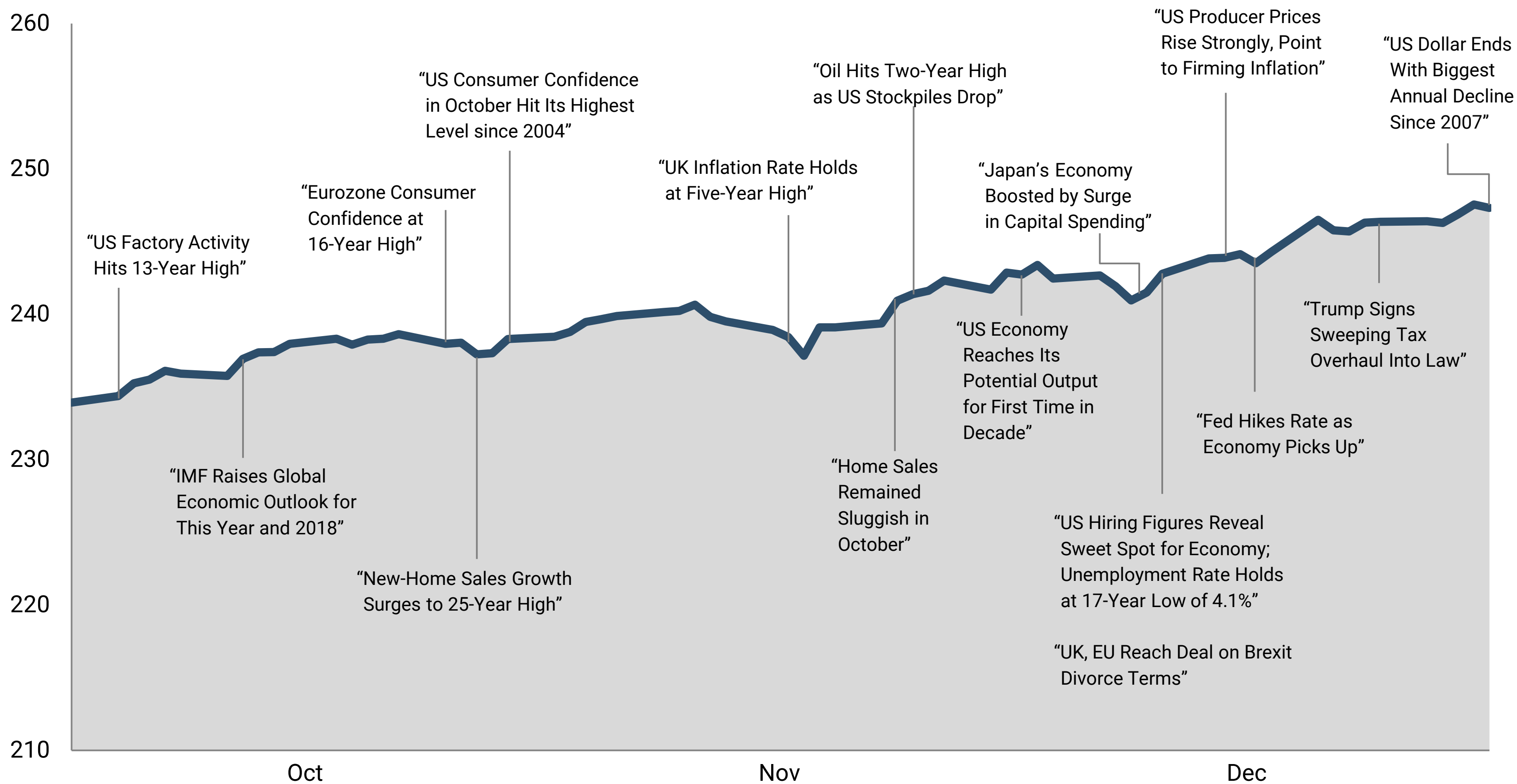
Asset Class	Fourth Quarter 2017	2017	Past 10 Years*
Commodities: GSCI	9.9%	5.8%	-10.2%
Emerging Market Stocks	7.4%	37.3%	1.7%
U.S. Large Stocks: S&P 500	6.6%	21.8%	8.5%
Foreign Real Estate	6.6%	15.6%	2.0%
Foreign Large Value Stocks	5.4%	26.1%	1.6%
U.S. Large Value Stocks	5.3%	13.7%	7.1%
Foreign Small Stocks	4.6%	30.2%	5.6%
Foreign Large Stocks	4.2%	25.0%	1.9%
Foreign Small Value Stocks	3.8%	28.0%	5.8%
U.S. Small Stocks	3.3%	14.7%	8.7%
U.S. Micro Cap Stocks	2.7%	11.2%	9.4%
U.S. Real Estate	2.5%	8.7%	7.8%
Long-Term U.S. Govt. Bonds	2.2%	8.2%	6.5%
U.S. Small Value Stocks	2.0%	7.8%	8.2%
U.S. Inflation Indexed Bonds	1.3%	3.0%	3.5%
Foreign Hedged Govt. Bonds	0.8%	2.2%	4.0%
Municipal Bonds	0.7%	5.5%	4.5%
High Yield Bonds	0.5%	7.0%	7.6%
U.S. T-Bills / Cash	0.3%	0.8%	0.3%
Corporate Bonds	-0.1%	2.9%	3.3%
Short-Term U.S. Govt. Bonds	-0.3%	0.4%	1.5%
U.S. Intermediate Govt Bonds	-0.4%	1.1%	2.8%
Master Limited Partnerships	-2.0%	-7.9%	N/A

***Annualized**

World Stock Market Performance [1]

Fourth Quarter 2017

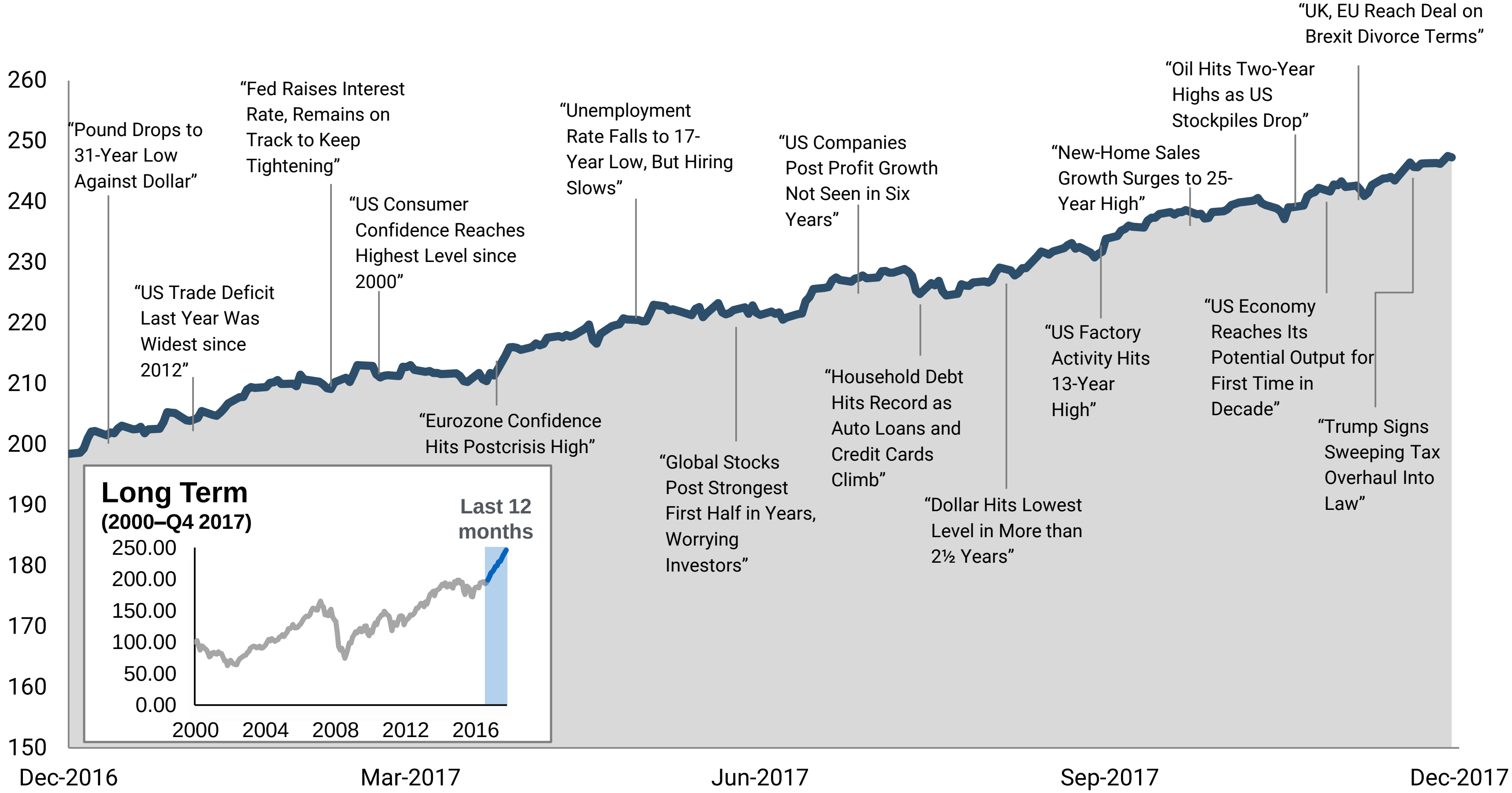
With selected headlines from Q4 2017



[1] MSCI ACWI Index (USD) [net div.]. MSCI data © MSCI 2018, all rights reserved.
These headlines are not offered to explain market returns. Instead, they serve as a reminder that investors should view daily events from a long-term perspective and avoid making investment decisions based solely on the news. Investors cannot invest directly in an index. Performance does not reflect the expenses associated with management of an actual portfolio. Past performance is not a guarantee of future results.

World Stock Market Performance [1]

With selected headlines for the past 12 months



[1] MSCI ACWI Index (USD) [net div.]. MSCI data © MSCI 2018, all rights reserved.
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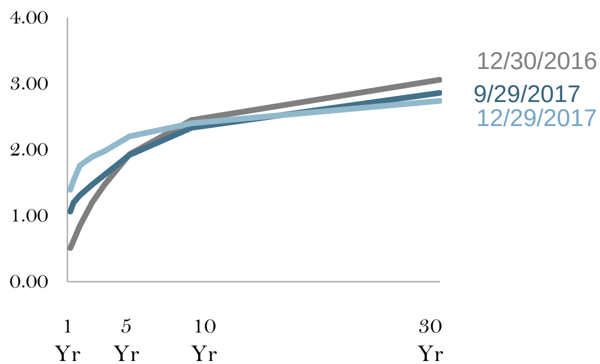
Fixed Income Performance & Yield Analysis

Interest rate changes across the US fixed income market were mixed during the fourth quarter. The yield on the 5-year Treasury note rose 28 basis points (bps), ending at 2.20%. The yield on the 10-year Treasury note increased 7 bps to 2.40%. The 30-year Treasury bond yield decreased 12 bps to finish at 2.74%.

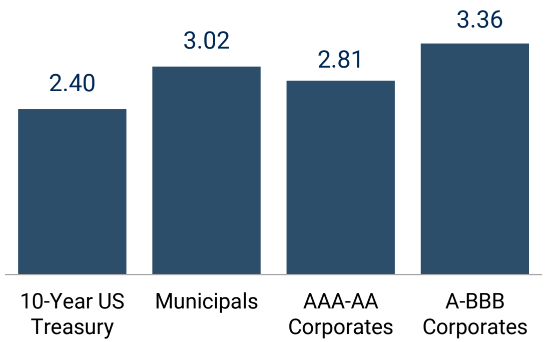
In terms of total returns, short-term corporate bonds declined 0.04% during the quarter but increased 1.85% for the year. Intermediate-term corporate bonds gained 0.17% for the quarter and 3.92% for the year.

The total returns for short-term municipal bonds were –0.65% for the quarter and 1.61% for the year. Intermediate-term municipal bonds fell 0.09% for the quarter but gained 4.70% for the year. Revenue bonds outperformed general obligation bonds for the year.

US Treasury Yield Curve (%) [2]



Bond Yields across Issuers (%) [3]



Period Returns (%) [4]

** Annualized*

Asset Class	1 Year	3 Years*	5 Years*	10 Years*
Bloomberg Barclays Long US Government Bond Index	8.53	2.85	3.49	6.49
Bloomberg Barclays US Corporate High Yield Index	7.50	6.35	5.78	8.03
Bloomberg Barclays US Aggregate Bond Index	3.54	2.24	2.10	4.01
Bloomberg Barclays US TIPS Index	3.01	2.05	0.13	3.53
Citi World Government Bond Index 1-5 Years (hedged to USD)	1.13	1.21	1.23	2.13
ICE BofAML 3-Month US Treasury Bill Index	0.86	0.41	0.27	0.39
ICE BofAML 1-Year US Treasury Note Index	0.57	0.49	0.38	0.90

Note: Data as of December 31, 2017. One basis point equals 0.01%. Past performance is not a guarantee of future results. Indices are not available for direct investment. Index performance does not reflect the expenses associated with the management of an actual portfolio.

Bull Markets & Bitcoins

The lengthy but shallow economic expansion, along with one of the longest bull markets in modern history, has investors feeling anxious. During 2017, few market observers expected stocks to deliver double-digit gains in the face of enduring geopolitical tensions, massive natural disasters, political gridlock, and tighter monetary policy. That said, recessions, rapid commodity price appreciation, aggressive monetary policy actions and extreme valuations typically precede or accompany major bear markets (see below). Using this framework to assess the current landscape, we see none of the typical flashing red lights that suggest a market downturn is imminent.

U.S. economic growth has averaged just 2.2% per year over the last five years, but during the last two quarters the economy has picked up momentum and grown over 3% on an annualized basis. With strong readings from consumer and business confidence, along with the potential benefits from tax reform, the economy appears to be stable and showing no signs of a looming recession.

Many consider oil as one of the most important commodities that affect the global economy since oil is a primary source of energy and is an essential input into a vast array of products. The current crude oil prices are about 45% below the highs reached in 2013 and unless a significant change disrupts oil production or demand, oil prices could remain at a reasonable level to support further global economic growth.

Since December 2015, the Federal Reserve has been raising the federal funds rate in 0.25% increments and has more recently begun reducing the size of its balance sheet that stems from the dark days of the financial crisis. The Fed's slow and transparent approach towards a more normalized monetary policy has kept markets relatively calm.

Characteristics of Bear Markets [5]

Market Corrections	Market Peak	Bear Market Return	Recession	Commodity Price Spike	Aggressive Fed	Extreme Valuations
Crash of 1929: Excessive leverage, irrational exuberance	Sep 1929	-86%	◆			◆
1937 Fed Tightening: Premature Policy Tightening	Mar 1937	-60%	◆		◆	
Post WWII Crash: Recession fears	May 1946	-30%	◆			◆
Flash Crash of 1962: Flash crash, Cuban Missile Crisis	Dec 1961	-28%				◆
Tech Crash 1970: Economic overheating, civil unrest	Nov 1968	-36%	◆	◆	◆	
Stagflation: OPEC oil embargo	Jan 1973	-48%	◆	◆		
Volcker Tightening: Whip Inflation Now	Nov 1980	-27%	◆	◆	◆	
1987 Crash: Program trading, overheating markets	Aug 1987	-34%				◆
Tech Bubble: Extreme valuations	Mar 2000	-49%	◆			◆
Global Financial Crisis: High leverage, Lehman collapse	Oct 2007	-57%	◆	◆	◆	

Note: Past performance is not a guarantee of future results.

Bull Markets & Bitcoins (cont'd)

Many market commentators believe the current U.S. equity bull market is in bubble territory, created by some combination of easy monetary policy, Trump-induced euphoria, irrational exuberance and the exceptional performance of Facebook, Amazon, Netflix, and Google. When examining valuations on multiple measures, the S&P 500 trades modestly above long-term averages. However, to provide some historical context, at the height of the tech bubble, the forward P/E multiple of the S&P 500 in March 2000 stood at 27.2 times earnings, 33% higher than the current multiple.

S&P 500 Valuation Measures as of 12/31/17 [6]

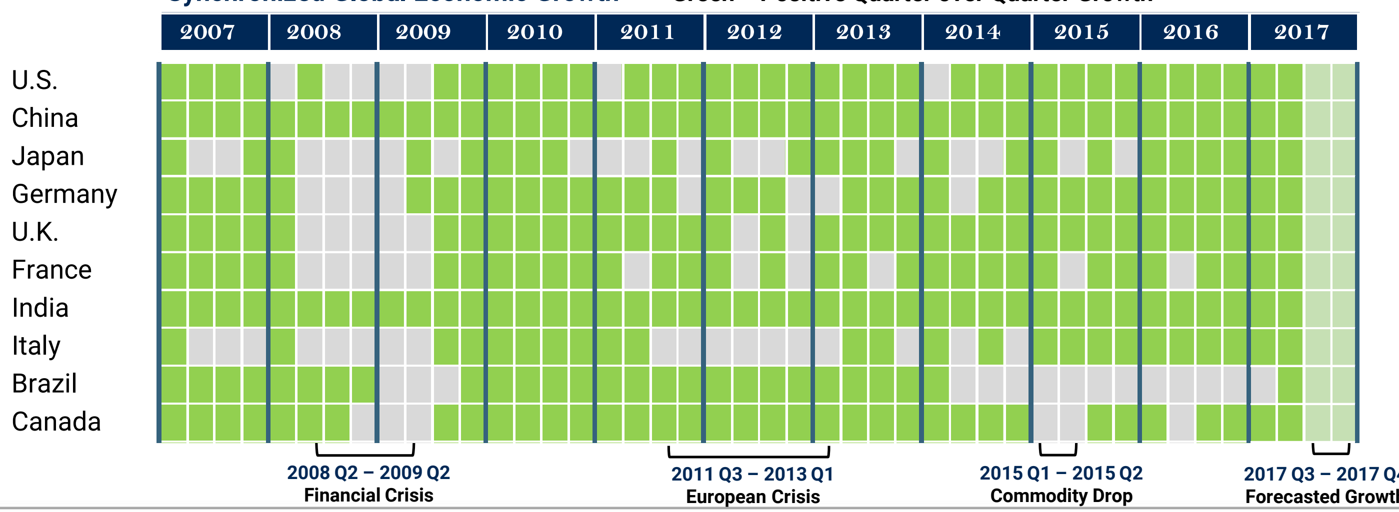
Valuation Measure	Description	Latest	25-Year Average
P/E	Forward P/E	18.2x	16.0x
Div. Yield	Dividend Yield	2.0%	2.0%
P/B	Price to Book	3.1x	2.9x
P/CF	Price to Cash Flow	12.8x	10.7x

It is also wise to view current valuation levels within the context of corporate earnings. The primary driver of U.S. stocks has been relatively consistent earnings growth since the great financial crisis. The current S&P Dow Jones Indices outlook suggests earnings could continue to grow by double-digit levels through 2018. While those estimates may be too aggressive, we believe earnings growth could remain positive and provide a solid foundation to support stock market valuations. While current valuations appear elevated, from a historical perspective they are not excessive or at levels that would prevent the opportunity for further stock market gains.

However, the returns on both U.S. and foreign large stocks have appreciated each month over the last year, which is extremely rare. Virtually every calendar year features at least one, and often several, significant declines of 5% or more; whether caused by some headline event or other circumstance. Armed with this knowledge, investors should be prepared for more volatility going forward and seek to maintain a globally diversified portfolio to weather the inevitable fluctuations.

Synchronized Global Economic Growth [7]

Green = Positive Quarter over Quarter Growth

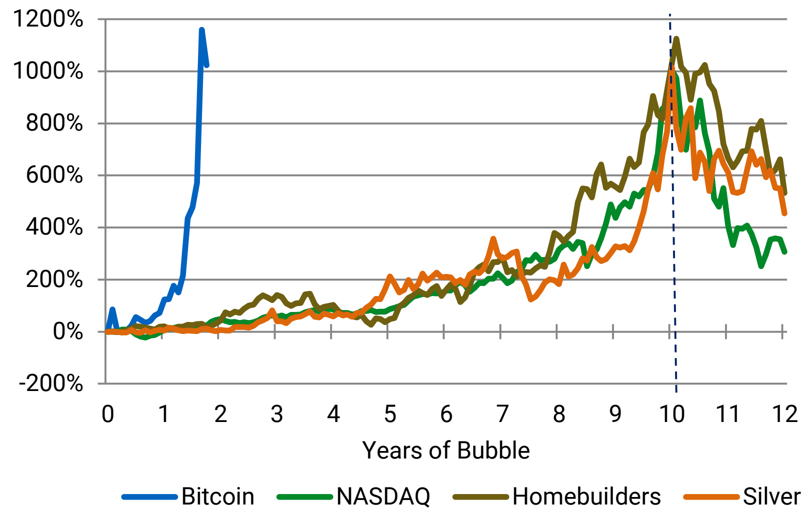


Further underpinning global stock prices is a 2017 resurgence in synchronized global growth across most of the developed and emerging world. Remarkably, on a global basis, 179 of 192 economies in the International Monetary Fund's (IMF's) World Economic Outlook posted economic growth last year, and the IMF forecasts 2018 will have the fewest countries in recession ever.[8] Many countries are finally benefitting from accommodative monetary policies, and in some cases, greater political stability, which in turn have supported earnings growth of foreign corporations. Many international economies are also in much earlier phases of their economic cycles that - in our opinion - could provide return and diversification benefits for globally diversified portfolios.

Fear of Missing Out

Bitcoin and other "cryptocurrencies" are receiving widespread media attention, prompting many investors to wonder if digital currency deserves an allocation in a diversified portfolio. Quite simply, a cryptocurrency is a digital or virtual currency that uses complex computer algorithms to track and store the digital currency while also maintaining security. The technology underlying cryptocurrencies (blockchain) could have a revolutionary impact on numerous industries, particularly in banking and financial services. However, the timing of a commercially viable application is highly uncertain. An investor contemplating a digital currency investment could select one of over 1,400 cryptocurrencies available with an aggregate market value of over $700 billion. To provide some context, the cryptocurrency aggregate market value is a bit higher than the market capitalization of the Indian stock market. Behaviorally, humans are prone to getting caught up in speculative investment crazes and operate from the "Fear of Missing Out" on the next great money making opportunity. The cryptocurrency mania reminds us of the euphoria surrounding the tech bubble with investors seeking to identify the next "big thing" like the Netscape browser or companies like eToys.com or Pets.com. When evaluating returns of Bitcoin in particular, this digital currency appears to be in a bubble. Historical data suggests that bubbles often form when an asset appreciates 1,000%, or 10x, in a span of ten years. When a comparison is made between Bitcoin and other asset bubbles in market history, Bitcoin appreciated over 1,000% in the span of fifteen months! Our value oriented investment discipline seeks to build a fundamental case for each investment in a portfolio, which implies an asset provides some sort of cash flow that can generate a positive expected return. A currency investment does not provide any form of cash flow return, so an investor would need to rely on speculative hope that the next investor will pay a higher price in the future. Currently, given the fickleness of human behavior, cryptocurrencies are best viewed as speculative endeavors using play money that an investor can afford to lose and not appropriate for a long-term investment portfolio.

Blowing Bubbles [9]



Bull Markets & Bitcoins (cont'd)

Concluding Thoughts

The overall economic landscape currently remains balanced with a generally positive long-term outlook. There are always known and unknown risks on the horizon that have short-term impact on the markets. What is known is that stocks and other growth investments have historically been cyclical, and as a result, there may be frequent periods of negative short-term returns. It is wise to remember that most portfolios serve long-term needs, and as a result, the focus should be upon long-term trends and outcomes. By taking the long view, it becomes easier to avoid the temptation of being swayed by the popular press and trends, which is often driven by emotion, rather than knowledge and discipline.

We hope our thoughts are helpful and informative. As always, please contact The Milestone Group if your objectives change and with any questions or comments. We appreciate your confidence in our team as we help grow and protect your financial security.

- The Milestone Group

Note: Past performance is not a guarantee of future results.

Disclosures/Endnotes

Asset class returns illustrated on page 1 are provided by Bloomberg and Ibbotson and utilize the following index or investment fund returns: U.S. Large Stocks: S&P 500 Index; U.S. Large Value Stocks: Russell 1000 Value Index; U.S. Small Stocks: Russell 2000 Index; U.S. Small Value Stocks: Russell 2000 Value Index; U.S Micro Stocks: DFA U.S. Micro Cap Fund; Foreign Large Stocks: MSCI EAFE Net Div. Free Equity Index; Foreign Large Value Stocks: DFA International Value Fund; Foreign Small Stocks: DFA International Small Company Fund; Foreign Small Value Stocks: DFA International Small Cap Value Fund; Emerging Market Foreign Stocks: IFC Emerging Markets Equity Index; U.S. Real Estate Stocks: NAREIT Investment Trust Index; Foreign Real Estate Stocks: Dow Jones Wilshire ex-U.S. International Real Estate Index; Master Limited Partnerships: Alerian MLP ETF; Others include: NASDAQ Composite; Cash: U.S. 90-Day Treasury Bills Index; U.S. Government Bonds: Bloomberg U.S. 1-3 Yr. Govt. Bond Index, Bloomberg U.S. 3-5 Yr. Govt. Bond Index, Bloomberg U.S. 10+ Yr. Govt. Bond Index; Inflation-Hedged Bonds: Barclays U.S. Inflation Linked Bond Index; Corporate Bonds: Lehman Brothers U.S. Corporate Index; High Yield Bonds: CSFB High Yield Bond Index; Foreign Government Bonds: JP Morgan GBI; Commodities: Goldman Sachs Commodity Index; Municipal Bonds: Barclays Capital Municipal Bond Index; Consumer Price Index.

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ENDNOTES:

1 MSCI ACWI Index (USD) [net div.]. MSCI data © MSCI 2017, all rights reserved.
2 Federal Reserve.
3 State and local bonds are from the S&P National AMT-Free Municipal Bond Index. AAA-AA Corporates represent the Bank of America Merrill Lynch US Corporates, AA-AAA rated. A-BBB Corporates represent the Bank of America Merrill Lynch US Corporates, BBB-A rated.
4 Bloomberg; US long-term bonds, bills, inflation, and fixed income factor data © Stocks, Bonds, Bills, and Inflation (SBBI) Yearbook™, Ibbotson Associates, Chicago (annually updated work by Roger G. Ibbotson and Rex A. Sinquefield). Citi fixed income indices copyright 2017 by Citigroup. The BofA Merrill Lynch Indices are used with permission; © 2017 Merrill Lynch, Pierce, Fenner & Smith Incorporated; all rights reserved. Merrill Lynch, Pierce, Fenner & Smith Incorporated is a wholly owned subsidiary of Bank of America Corporation. The S&P data are provided by Standard & Poor's Index Services Group.
5 J.P. Morgan Asset Management.
6 J.P. Morgan Asset Management, December 31, 2017
7 DoubleLine Capital L.P.; BMO Global Asset Management.
8 Goldman Sachs.
9 Charles Schwab & Co, Inc.; Morningstar Direct; MVIS CryptoCompare Bitcoin PR USD; NASDAQ Composite PR USD; S&P 500 Sub/Homebuilding TR; S&P GSCI Silver Spot.

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