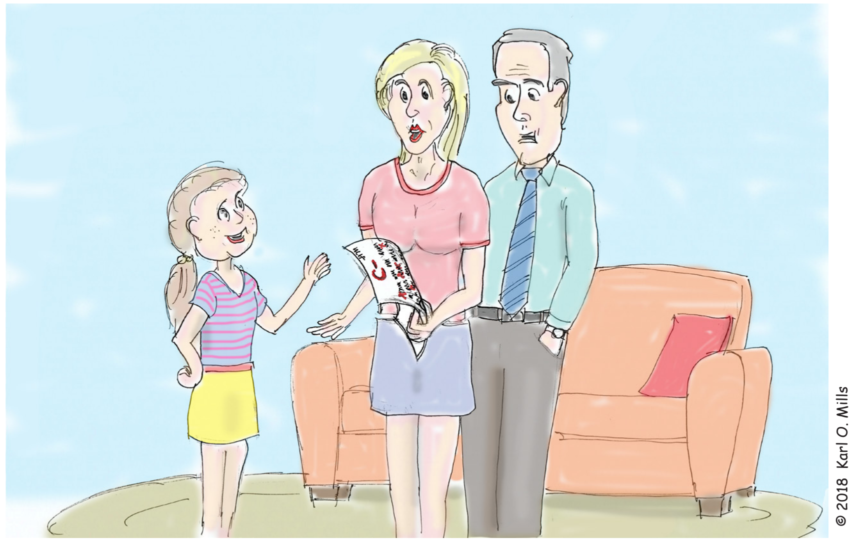
COUNTER | POINT

The Quarterly Commentary of Jurika, Mills & Keifer LLC



It's a totally fake grade. I am probably the most successful student in the history of the 2nd grade. I give myself an A Plus!

Fourth Quarter: October, 2018

In this issue:

"A Plus"

According to a recent Tweet, the economy and stock market are the best they have ever been, in the history of America, and deserve an A Plus. What else do you need to know?

For the moment, perhaps not much more. Against the backdrop of painful political theater and challenging geopolitics, the U.S. Economy and stock market continue to move onward and upward, with a full head of steam. If the political news is distressing, the economic news, at least here in the United States, is currently very good.

This stands in growing contrast to what is happening outside the U.S.

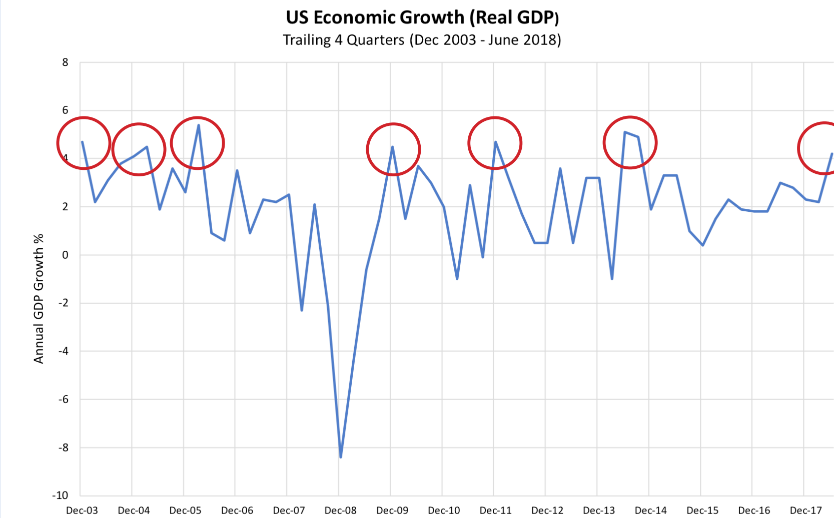
Summary:

- Despite constant political bluster and dysfunction, the U.S. economy and markets continue to power onward and upwards.
- This stands in contrast to the rest of the world where economic growth is softening, at least for the time being and markets are generally down.
- The U.S. economy is large, diverse and well insulated from the rest of the world. A $19 trillion economy growing at 4% has a lot of momentum to it.
- Current trends likely continue into next year. The U.S. economy may grow stronger for longer and stocks may move higher, but risks are elevated and expected returns are lower.
- We therefore think it makes sense to maintain a more defensive allocation to risk assets.

where economies and markets are struggling.

U.S. Economic Growth topped 4% last quarter and should remain elevated for another quarter or two as fiscal stimulus from last year's tax reform works its way through the economy. It may not be the best growth in recorded history (**Chart I** shows we have achieved this seven times since 2003) but it is a good thing and sure beats the alternative.

Chart I



Source: Bureau of Economic Analysis, YCharts & Jurika, Mills & Keifer LLC

As the chart also shows, growth spurts above 4% tend to be short-lived. In the current case, some of the stimulus is one-time in nature, such as the repatriation of foreign cash reserves by U.S. corporations. Some of the benefits of tax reform will be ongoing, such as the reduction in overall corporate and individual tax rates, but it remains to be seen how much of these tax savings will result in higher levels of ongoing capital investment and consumer spending.

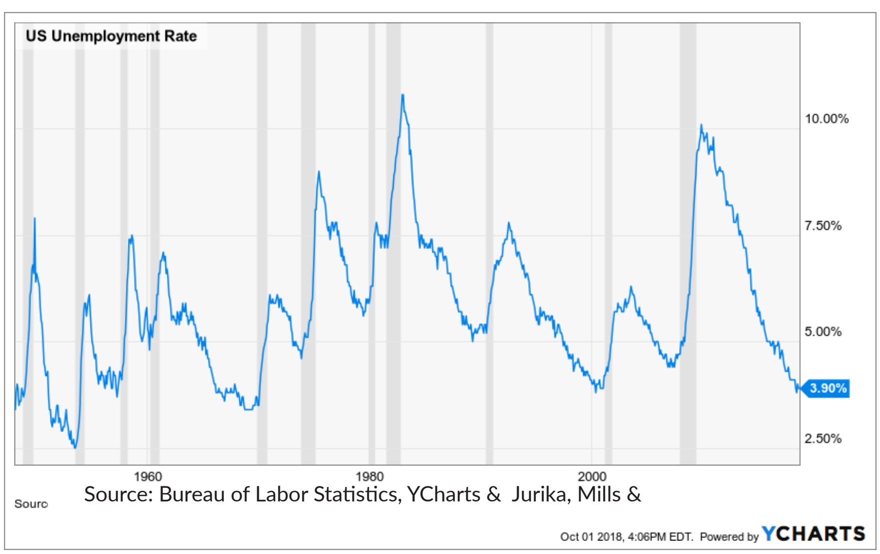
It is also important to note that much of the tax reform will be financed by higher deficits –many economists estimate the net cost in excess of $1 trillion - which should drive up government borrowing costs and tend to make future government investment costlier and more difficult.

There are other basic economic forces that are likely to weigh on growth in the coming quarters including tight employment and higher interest rates.

The unemployment rate is currently 3.9% **(Chart II)**. This is the lowest level since April of 2000 and near historical trough levels. Skilled labor is becoming increasingly scarce and expensive and we are starting to see increasing upward pressure on wages.

Meanwhile interest rates are on the rise and the Federal Reserve just increased the Federal

Chart II



Funds Rate another 0.25% to 2%. The 10-year, US Treasury Bond rate recently topped 3%. We think interest rates will continue to head higher and more so than investors are currently anticipating.

These are all reasons why economic growth will naturally moderate in the coming quarters, but not reasons for it to suddenly fall off a cliff.

By contrast, throughout much of the rest of the world the economic picture looks more challenging and growth appears to be slowing.

One cause for this slowing is China. Chinese GDP growth has declined from over 10% a few years ago to just over 6%, its lowest level since the Credit Crisis. The Chinese economy has experienced massive credit growth and is now awash in debt and excess capacity. The government is currently more focused on wringing excess out of the system than stimulating new growth. This has an impact on countries throughout Asia and Europe for whom exports to China represent an important source of economic growth.

This is much less the case with the United States, where exports to China represent less than 1% of US GDP. By contrast, Chinese Exports to the U.S. represent 4% of Chinese GDP. China is more dependent on trade with the United States than the United States is dependent on trade with China. The current trade skirmish between the U.S. and China impacts both economies but impacts China considerably more.

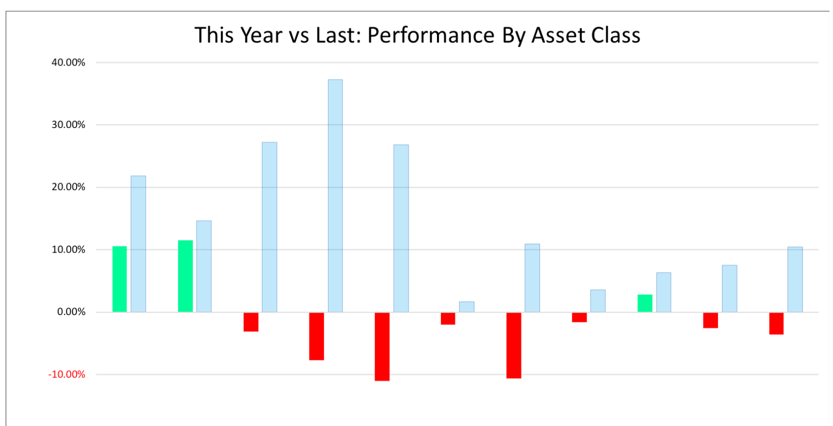
Many Emerging economies have also been affected by the strong U.S. Dollar. According to BCA Research, 80% of Emerging Market foreign-currency debt is denominated in U.S. dollars and Emerging Market debt levels are at the highest level since the late 1990s. The stronger the dollar gets, the harder it is for these economies to service their debt and the less money is available for other government spending to support growth and stability.

And finally, in Europe, after a more hopeful 2017, economic indicators have softened. GDP growth in the Eurozone is wavering around 2% and concerns about Brexit and Italian budget deficits are adding additional drag on business and investor sentiment. Meanwhile, The European Central Bank is maintaining short term interest rates around 0%.

Markets:

The global financial markets grade on a curve, and relative to other markets and asset classes,

Chart III



	S&P 500 TR USD	Russell 2000 TR USD	MSCI ACWI Ex USA NR USD	MSCI EM NR USD	MSCI Frontier Emerging Market NR USD	Bloomberg Commodity TR USD	Bloomberg Sub Precious Metals TR USD	Bloomberg Barclays Agg Bond Index TR	Markit iBoxx Liquid High Yield TR USD	FTSE WGBI USD	JPM EMBI Global Core TR USD
Year to Date	10.56%	11.51%	-3.09%	-7.68%	-11.05%	-2.03%	-10.66%	-1.60%	2.81%	-2.55%	-3.62%
2017	21.83%	14.65%	27.19%	37.28%	26.79%	1.70%	10.94%	3.54%	6.34%	7.49%	10.46%

Source: Morningstar & Jurika, Mills & Keifer LLC the U.S. stock market indeed gets an A Plus this year.

Chart III above shows the performance – this year and last - of various asset classes including U.S. and Non-U.S. stocks, commodities, precious metals, and various domestic and non-domestic bonds. Whereas last year optimism about synchronized global recovery and growth was a tide that floated all asset classes, this year there is a stark contrast between U.S. stocks and almost everything else.

Through the third quarter, U.S. stocks as measured by the S&P 500 are up over 10% and small cap stocks are up over 11%. By contrast, non-US developed market equities are down 4% and emerging and frontier market stocks are down 7.8% and 11.1% respectively. commodities are down, precious metals are down 10.7% and most bonds, other than U.S. high yield are down.

Too Much of a Good thing?

Regardless of what one thinks of the current political situation, the U.S. economy is in an enviable position relative to the rest of the world. As we have written in the past, our economy is large, broad, diverse, insulated and resilient. Although we are a major force in global trade, we are not overly reliant upon it, with exports representing about 14% of our GDP. We can grow the food to feed ourselves and generate all the energy we need to power our lives. We have a large, well-educated ethnically diverse population, friendly and very tolerant neighbors to the North and South, thousands of miles of water protecting us to the East and West, and the largest and most sophisticated military on the globe. We have well established rule of law, the world's reserve currency, the deepest and most liquid capital markets and the finest research Universities. With a strong culture of innovation and risk-taking, the U.S. is still ***the*** leading source of innovation and disruption and the home of most of the World's most dynamic and successful companies.

"It is important to bear in mind that a $19 trillion economy growing at 4% with a trillion dollars of turbocharged stimulus running through its system has a lot of momentum...it does not slow quickly of its own accord."

Moreover, our banking system is currently very well capitalized, corporate debt levels are manageable. The housing market is stable and household debt levels are below average. The economy is healthy, without any major imbalances or bubbles, other than the overall level of government debt. Relative to the rest of the world, our economy is in very good shape.

Some of these advantages will fade or be eclipsed by other countries in time, especially if we focus on short-term economic gains at the expense of long-term investment in education, infrastructure, healthcare and the important public institutions that undergird our society.

As Michael Lewis points out in his new book ***The Fifth Risk***, while government institutions are an easy target for ridicule, many of them perform essential functions and are staffed by highly professional and competent people who work for the public good. Without them, many services that we take for granted would stop functioning.

We can also likely bully our way into improved trade deals with other countries, with friends and foes alike, but our long-term prosperity is linked to the long-term stability of the global economy, which in turn is dependent on trusted relationships, principled leadership, and common purpose.

In the near term however, the U.S. economy is not as fragile as it may seem on television, and many of the headlines regarding trade are more noise than substance. It is important to bear in mind that a $19 trillion economy growing at 4% with a trillion dollars of turbocharged stimulus running through its system has a lot of momentum to it. Like a steaming locomotive barreling down the track, it does not slow quickly of its own accord.

Investment Strategy: *More than you might think*

The bottom line is that current trends may continue longer than most people expect. Our economy may grow stronger for longer, the dollar may continue to strengthen, and the Federal Reserve may need to raise interest rates higher than most people think before they actually take hold. And markets may rise higher than they rationally should before finally succumbing to the laws of economic gravity. Historically, markets tend to overshoot rational valuation levels on the way up and the way down. We do not see a reason why this time would be any different.

Although an overshoot of the US economy and markets higher would not surprise us, and in our view is the most probable case, our investment stance has become increasingly defensive and valuation focused. As markets and valuation levels rise, risks rise as well, and expected returns decline.

"The bottom line is that current trends may continue longer than most people currently expect."

We have therefore been doing some selective pruning of our higher growth positions, where we think the valuation risks are the highest.

We are still long-term believers in technology and innovation and are maintaining a strategic allocation to investments focused on technology, biotechnology and healthcare, but these areas have become very crowded as investors have flocked to them, chasing short term performance.

Another area of strategic focus has been emerging markets. Although we are primarily focused on the consumer companies in the developing world, most all assets tied to emerging markets have been painted by the same brush. As long as the Federal Reserve is the only major central bank in the world raising interest rates, the dollar should remain strong. Barring a new round of fiscal stimulus by the

Chinese Government, emerging economies and markets should continue to struggle in the near term.

We remain focused on the long-term however, where the prospects for the developing world are better. We are therefore maintaining our positions and will likely increase them when we see a meaningful change in the direction of the dollar, and/or a new round of stimulus by the Chinese government.

Although diversification has not worked this year, and may not for a while longer, we are firm believers in its long-term benefits. We continue to like alternative strategies that have low correlation to current equity markets or hedge against the risks inherent in the more highly valued portions of our portfolios.

Finally, given our forecast for higher interest rates, we have an underweight position in traditional longer-maturity bonds, but are using short-term and flexible mandate bond-funds as a parking place for cash that we can reinvest when compelling opportunities present themselves.

Over the long-term we continue to invest with a global focus; balancing investments targeted at areas of long-term growth and innovation - such as technology and biotechnology - with more defensive equity, alternative, and fixed income strategies aimed at mitigating volatility and risk. As always, we welcome your comments, questions and referrals.

Jurika, Mills & Keifer, LLC
October, 2018

JMK Jurika · Mills & Keifer
Private Wealth Management

Jurika, Mills & Keifer is a private wealth management firm serving a limited group of individuals and families.

Our firm is built on a core set of values and investment principles that have been central to our identity and success for over 30 years.

Our objective is to preserve and build the purchasing power of our clients' capital over time through forward-looking investment management and smart financial planning and counsel.

Our offices are in San Francisco, California. We welcome your inquiries.

Jurika, Mills & Keifer, LLC
Private Wealth Management
One Ferry Building, Suite 255
San Francisco, California, 94111
415-677-5430 Phone
www.jmkadvisors.com

Important Disclosures

Opinions expressed are those of Jurika, Mills & Keifer, LLC, and are subject to change.

Source for Data: Bloomberg, Morningstar, BCA Research, YCharts, U.S. Government.

Investments in securities involve the risk of loss. There can be no assurance that investment strategies referenced will be successful, or that investment objectives will be achieved. Past performance is no guarantee of future results. One cannot invest in an index.

This communication is neither an offer to sell nor the solicitation of an offer to buy a security or advisory services, which can only be made by the appropriate offering document.

Jurika, Mills & Keifer is registered with the Securities Exchange Commission.

v.10-2018