WEEKLY MARKET REVIEW

JULY 25, 2017

In This Edition

- *Financials weren't so bad after all.*
- *Policy movement in Washington stalled.*
- *What's next for the markets?*

CLS INVESTMENTS

Market Performance

Equities	LAST WEEK	QTD	YTD '17
Total U.S. Market[1]	+0.57%	+2.03%	+11.15%
Domestic Large-Cap Equity[2]	+0.56%	+2.13%	+11.67%
Domestic Small-Cap Equity[3]	+0.50%	+1.49%	+6.55%
International Equity[4]	+0.73%	+3.19%	+17.74%
Developed International Equity[5]	+0.47%	+2.38%	+16.51%
Emerging Market Equity[6]	+1.33%	+5.33%	+24.74%
Fixed Income	**LAST WEEK**	**QTD**	**YTD '17**
U.S. Investment Grade Bonds[7]	+0.56%	+0.64%	+2.93%
Cash Equivalent[8]	+0.01%	+0.05%	+0.35%
Commodities	**LAST WEEK**	**QTD**	**YTD '17**
Commodity[9]	+0.36%	+0.53%	-4.76%

[1]Russell 3000 [2]S&P 500 Index [3]Russell 2000 Index [4]MSCI ACWI ex-U.S. Index [5]MSCI EAFE Index [6]MSCI Emerging Markets Index [7]Bloomberg Barclays Capital U.S. Aggregate Bond Index [8]Bloomberg Barclays Capital 1-3 Month U.S. Treasury Bill Index [9]Bloomberg Commodity

As of 7/21/2017

Week in Review

Equity and fixed income markets saw another week of strong performance. New record highs were achieved in the S&P 500 and Russell 2000. Emerging markets led the way again (up over 1%) and are up nearly 25% so far this year. Even commodities performed well, up 0.3%, and the Barclays U.S. Aggregate Bond Index was up 0.5% as inflation concerns continue to abate. Fears about the balance sheet and the debt ceiling appeared in the short-term fixed income market by the week's end.

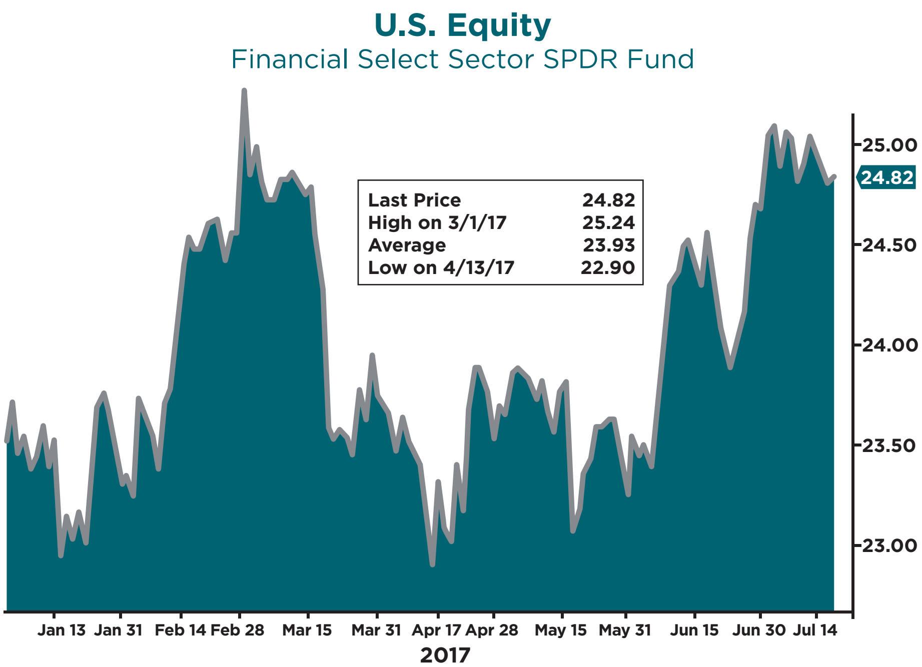
The Difference Half a Year Makes

At the beginning of 2017, market expectations were quite different from what they are today. A new president was taking office, and many expected significant policy changes. Infrastructure spending, deregulation in the financial industry, reduced taxes, and the repeal of Obamacare topped the list. In addition, the Federal Reserve (Fed) was expected to hike rates aggressively as lending increased.

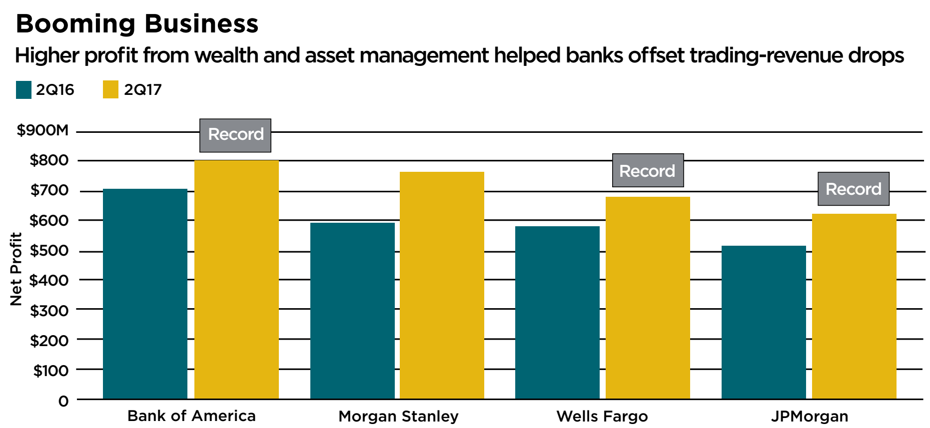
Needless to say, all of these expected events are now questionable.

So, what does that mean for CLS portfolios? We emphasize the financial sector in portfolios as it falls under the CLS Investment Theme, Global Value. Using the Financial Select Sector SPDR Fund (XLF) as a proxy, this sector has seen a return of more than 7% so far this year. That would seem pretty good most years — and it is especially positive this year when almost everything that *could* go wrong with financials, *has* gone wrong. Long-term interest rates are lower, the yield curve has flattened, trading volumes have slowed significantly, commodities have been in the dump, and deregulation efforts haven't gone anywhere.

On the positive side, the largest banks saw revenue climb to a record $18.4 billion in the second quarter, according to Bloomberg. And, as CNBC reported, profits at divisions of JP Morgan Chase and Bank of America saw record highs, while investment banking businesses scored a boon as fees rose at the biggest firms. This success comes at a time when the financial sector is navigating new fiduciary rules and surges in robo-advising and passive investing.



Source: Bloomberg Finance L.P., July 19, 2017



Source: Bloomberg

See You in December?

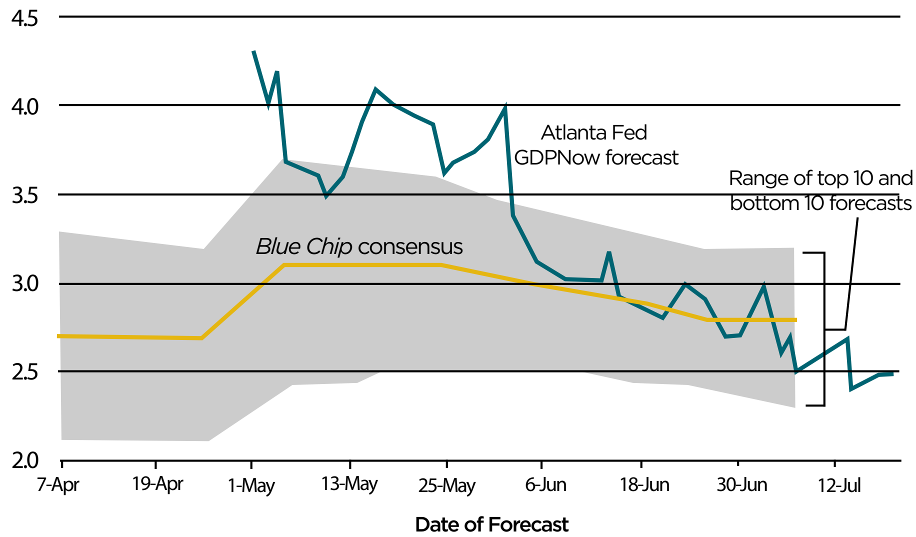
There is clearly a tug of war right now between inflation and deflation. Earlier this year, it appeared the Fed was falling behind on its inflation mandate as energy prices rebounded, housing prices increased, and wages rose well above 2%. But, core Consumer Price Index (CPI) readings over the last three months have been -0.12%, +0.07%, and +0.06% respectively. Certainly the trend has now gone the other way.

Further, policy movement in Washington seems to have stalled. Healthcare, tax reform, and even some infrastructure projects appear on hold, which is giving the Fed a pause in taking short-term rates higher. Meanwhile, inflation-adjusted GDP was only 1.5% in the first quarter, although it picked up in the second quarter, and employment, household wealth, and business fixed investment have all turned higher in 2017.

As seen on the charts to the right, while the data is improving, there is no reason for the Fed to act now. In fact, I would contend there is a good chance the Fed doesn't do anything further in 2017. However, December offers the most likely scenario for any possible change.

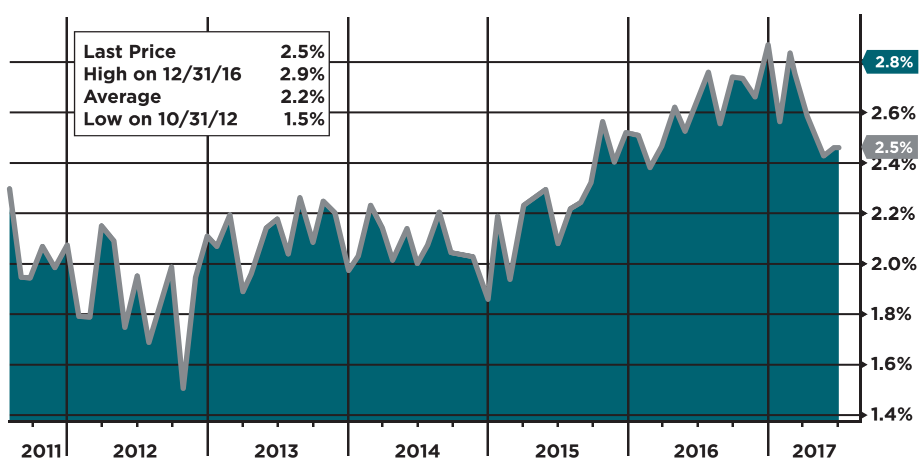
In the meantime, enjoy the nice weather.

GDPNow Model Forecast for Real GDP Growth 2017: Q2



Sources: Blue Chip Economic Indicators and Blue Chip Financial Forecasts. GDPNow as of 7/19/2017
Note: The top (bottom) 10 forecast is an average of the highest (lowest) 10 forecasts in the Blue Chip Survey, and is represented by the gray shaded area

U.S. Average Hourly Earnings All Employees
Bureau of Labor Statistics



Source: Bureau of Labor Statistics, June 31, 2017

What's Next for the Markets?

While the Fed may be on hold with respect to short-term interest rates, the stock market continues to hit new highs, interest rates remain well-behaved, and volatility is nowhere to be found.

But, that doesn't mean there can't be fireworks just because the fourth of July has passed.

Government policies that have stalled so far can easily be reignited. Healthcare, tax reform, and infrastructure spending can all resume at any time. Concerns about the debt ceiling have already surfaced in the short-term Treasury bill market. With three months to go before Congress's deadline to raise the debt ceiling and avoid defaulting on its bills, yields on T-bills maturing after October 19 increased by approximately 10 basis points (bps) from midweek on, according to Bloomberg. The last bout of angst when this happened saw an increase of approximately 50 bps when some T-bill rates were virtually zero.

Disruptions in bill supply over the next few months will cause increased volatility and could put a crimp in the Fed's plan to start unwinding its balance sheet. That may begin as soon as September. Investors will have to navigate between finding a place to stash money and avoiding certain maturity dates that could tie up liquidity until the debt ceiling issue is resolved. While the resolution may be last minute, I don't see any chance investors will not receive their money back in a timely manner on these securities.

With that said, as we have seen before, the potential disruptions could spill over into the credit and equity markets.

Marc Pfeffer
Managing Director, Institutional Fixed Income, Senior Portfolio Manager

Marc Pfeffer joined CLS in 2011, continuing as Senior Portfolio Manager for the Milestone Treasury Obligations Fund, which CLS incorporated into its fund family in January 2012. Mr. Pfeffer has over 30 years of investment management experience, including time spent as the Chief Investment Officer at Milestone. He also worked previously at Goldman Sachs and Bear Stearns.

Mr. Pfeffer is a Portfolio Manager on the CLS Flexible Income Fund and CLS Global Growth Fund portfolio management teams, in addition to being a Portfolio Manager of the CLS Active Income X Strategy and CLS's ETF strategies. He also manages individual municipal bond portfolios for the CLS Master Manager Strategy, and is a senior member of the CLS Investment Committee.

Mr. Pfeffer graduated from the State University of New York with a Bachelor of Science degree, and from Fordham University with a Master of Business Administration degree. He holds his FINRA Series 7, 63, and 65 licenses.

Investor Fears

The Bank of America Merrill Lynch July Fund Manager Survey showed some interesting trends among investors, who are showing a high appetite for risk, while fund managers appear to be anticipating a bear market. Here's an overview, as pulled from a recent CNBC article that summarizes the findings.

- *While the average cash balance has dipped to 4.9 percent from 5 percent last month, the 10-year average remains above 4.5 percent.*
- *While 28 percent of those surveyed fear a crash in bond markets the most, another 27 percent are concerned a central bank mistake is most likely to leave markets in troublesome waters.*
- *Fund managers are taking out more protection and cash positions. When asked why, 45 percent of investors that responded highlighted a bearish view on markets.*
- *One potential trigger could be the Fed reducing its balance sheet. "Although 48 percent of investors see it as a non-event, a notable minority, 31 percent, thought any decrease would be risk-off pushing bond yields higher and equities lower," the survey said.*
- *There was a slight reduction in equities in July and increase into bonds. Equities, however, remain the most owned asset class even though they are considered expensive.*

The survey also found that the banking sector has been favored over technology, noting banks are considered undervalued, while tech is overvalued. This trend is in line with CLS's Value Investment Theme.

Along with our other investment themes, we continue to have a significant weighting (considerably higher than industry averages) in both smart beta and actively managed ETFs. Specifically in fixed income, we expect this trend to continue as the amount of active fixed ETFs has lagged before their equity counterparts, and I believe they offer a greater chance of outperformance.

Stay balanced, and thanks for reading.

The Russell 3000 Index is an unmanaged index considered representative of the U.S. stock market. The index is composed of the 3,000 largest U.S. stocks. The S&P 500® Index is an unmanaged composite of 500-large capitalization companies. This index is widely used by professional investors as a performance benchmark for large-cap stocks. The Russell 2000® is an index comprised of the 2,000 smallest companies on the Russell 3000 list and offers investors access to small-cap companies. It is a widely recognized indicator of small capitalization company performance. The MSCI All-Countries World Index, excluding U.S. (ACWI ex US) is an index considered representative of stock markets of developed and emerging markets, excluding those of the US. The MSCI EAFE Index is a composite index which tracks performance of international equity securities in 21 developed countries in Europe, Australia, Asia, and the Far East. The MSCI Emerging Markets Index is a composite index which tracks performance of large and mid-cap firms across 21 countries classified as emerging market countries. The Barclay's Capital U.S. Aggregate Bond® Index measures the performance of the total United States investment-grade bond market. The Barclay's Capital 1-3 Month U.S. Treasury Bill® Index includes all publicly issued zero-coupon U.S. Treasury Bills that have a remaining maturity of less than 3 months and more than 1 month, are rated investment grade, and have $250 million or more of outstanding face value. The Bloomberg Commodity Index is made up of 22 exchange-traded futures on physical commodities and represents 20 commodities that are weighted to account for economic significant and market liquidity. An index is an unmanaged group of stocks considered to be representative of different segments of the stock market in general. You cannot invest directly in an index.

The graphs and charts contained in this work are for informational purposes only. No graph or chart should be regarded as a guide to investing. While some CLS portfolios may contain one or more of the specific funds mentioned, CLS is not making any comment as to the suitability of these, or any investment product for use in any portfolio. This material does not constitute any representation as to the suitability or appropriateness of any security, financial product or instrument. There is no guarantee that investment in any program or strategy discussed herein will be profitable or will not incur loss. This information is prepared for general information only. It does not have regard to the specific investment objectives, financial situation, and the particular needs of any specific person who may receive this report. Investors should seek financial advice regarding the appropriateness of investing in any security or investment strategy discussed or recommended in this report and should understand that statements regarding future prospects may not be realized. Investors should note that security values may fluctuate and that each security's price or value may rise or fall. Accordingly, investors may receive back less than originally invested. Past performance is not a guide to future performance. Individual client accounts may vary. Investing in any security involves certain non-diversifiable risks including, but not limited to, market risk, interest-rate risk, inflation risk, and event risk. These risks are in addition to any specific, or diversifiable, risks associated with particular investment styles or strategies.

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