CLS's WEEKLY 3

What You Need To Know About the Markets

SEPTEMBER 19, 2017

In This Edition

1. The Fed's meeting scheduled to touch on the FOMC balance sheet, "dot plots," and the federal funds rate.
2. The future of bitcoin remains cloudy.
3. Is inflation dead or on the rebound?

CLS INVESTMENTS

Market Performance

Equities	LAST WEEK	QTD	YTD '17
Total U.S. Market[1]	+1.70%	+3.39%	+12.62%
Domestic Large-Cap Equity[2]	+1.63%	+3.64%	+13.33%
Domestic Small-Cap Equity[3]	+2.35%	+1.40%	+6.46%
International Equity[4]	+0.73%	+6.08%	+21.04%
Developed International Equity[5]	+0.56%	+4.70%	+19.15%
Emerging Market Equity[6]	+1.05%	+9.87%	+30.12%
Fixed Income	**LAST WEEK**	**QTD**	**YTD '17**
U.S. Investment Grade Bonds[7]	-0.50%	+1.10%	+3.40%
Cash Equivalent[8]	+0.02%	+0.21%	+0.51%
Commodities	**LAST WEEK**	**QTD**	**YTD '17**
Commodity[9]	+0.53%	+3.37%	-2.06%

[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 Index

As of 9/15/2017

Week in Review

Stocks rose sharply last week as Hurricane Irma caused less damage than initially feared. The U.S. markets led the way as the Russell 3000 Index rose 1.7%. Small-caps were up sharply as the Russell 2000 Index was up 2.35%. International markets, while positive, lagged as the MSCI ACWI Index was up 0.73%. Bonds sold off last week led by a stronger-than-expected Consumer Price Index (CPI) report on Thursday. The Bloomberg Barclays U.S. Aggregate Bond Index was down 0.5%. Investors fled the safety of U.S. Treasuries as the yield on the 10-year rose 15 basis points to close the week at 2.20%.

The Federal Reserve (Fed) begins its two-day meeting on Tuesday, September 19, which will conclude with a press conference led by Fed Chair Janet Yellen. Several key items will come up with a lot of moving parts:

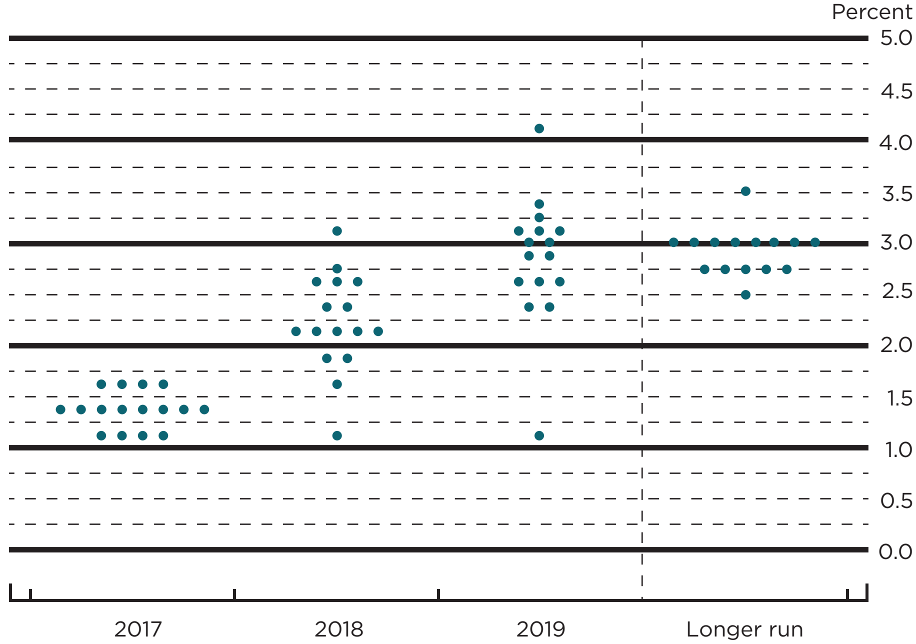
1. The Federal Open Market Committee (FOMC) is likely to take its first step to normalize its balance sheet as it has already outlined.
2. The "dot plot," which charts individual FOMC members' expectations regarding short-term interest rates over the next several years, will be updated as it is every quarter.
3. There may be a change in the federal funds rate.

Let's delve a bit deeper into these three items.

For months, the FOMC has said it will take the first step in normalizing its balance sheet at this meeting. Even after Congress kicked the can down the road on the debt ceiling and two massive hurricanes hit the U.S., the committee seems eager to begin this process. What it means for investors is that interest payments and principal from maturing securities will no longer be reinvested in the bond market. This process will take years to complete and is not intended to cause major market disruptions. However, the Fed's initial tapering, which was also telegraphed, caused what became known as the "taper tantrum" and pushed long-term interest rates much higher over the following months. So, we will see.

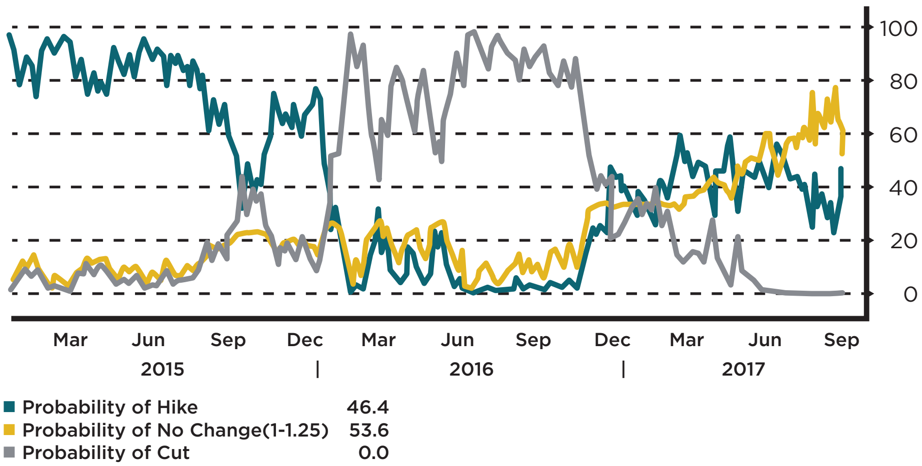
FOMC Participants' Assessments of Appropriate Monetary Policy:

Midpoint of target range or target level for the federal funds rate



*Source: The Federal Reserve. As of June 14, 2017 - *see disclosures*

Current Implied Probabilities



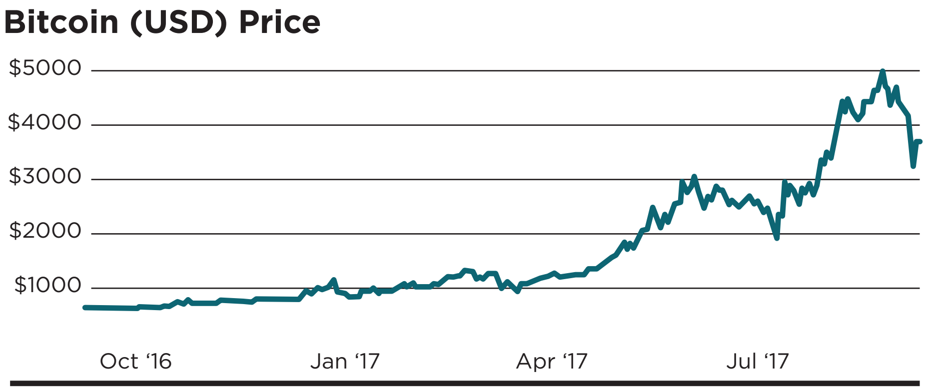
Source: Bloomberg Finance L.P. As of September 15, 2017

The dot plot is where it gets interesting. Until the latest CPI report, the market had essentially priced out further rate increases in 2017. That goes totally against the dot plot, as well as the anticipated quarter rate hikes through 2018.

Finally, there could be significant changes to the federal funds rate — especially considering comments made by several Fed officials about delaying rate hikes for now. However, no immediate change is expected at this meeting.

The Rise (and Fall?) of Bitcoin

During the technology craze and eventual bust in the late 1990s, investors — myself included — didn't know what they were buying; they just knew the stock symbols. It was irrelevant whether the companies made money or not, or what the price-to-earnings ratios were. It was a matter of buying a stock, holding on to it for even just a few minutes, and then selling it, hopefully at a profit. Companies opened up as much as 10 times their initial public offering (IPO) price.



Source: Coindesk. As of September 17, 2017

Bitcoin is starting to remind me of that boom-and-bust time. When I talk to people on the street, whether it's an Uber driver or my shoe-shine guy, I hear bitcoin being discussed with enthusiasm. And, as a father of a daughter who recently got engaged, it's hard not to jump on the bandwagon and try to trade some bitcoin to fund the wedding I know is coming. But, I am older now and hopefully a little wiser — at least enough to know I shouldn't trade something I know little about.

So, let's start with the basics. Bitcoin is a cryptocurrency, which is a type of digital token that relies on cryptography to chain together transactions and control the creation of additional units of the currency. Bitcoin became the first decentralized cryptocurrency in 2009.

Well, where I come from currencies don't swing 20% or so in a day. Imagine if the U.S. dollar swung like that!

Just last week, the Chinese government and financial regulators officially requested Chinese bitcoin exchanges and trading platforms to shut down by the end of September. While the initial news brought the purchase price of one bitcoin down from approximately $5,000 to $3,000, it has since rebounded. Many speculators remain optimistic since the Chinese bitcoin exchange only accounted for approximately 10%-13% of global bitcoin trades.

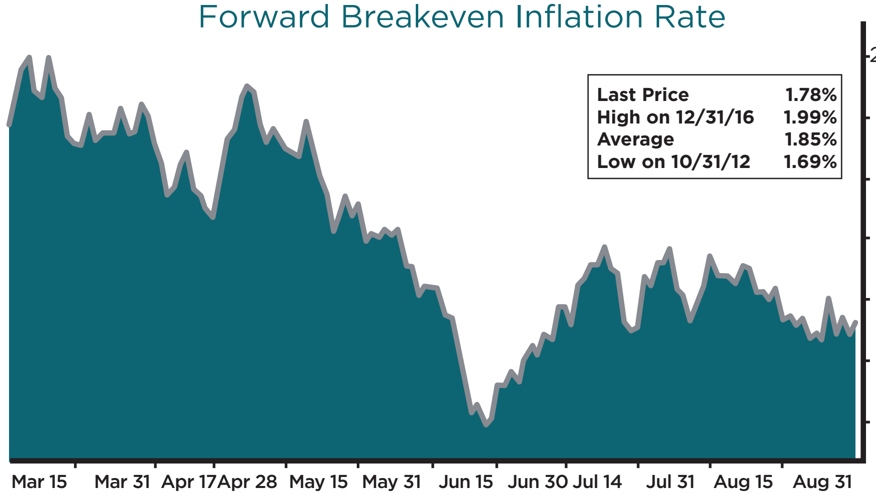
Also last week, Mohamed El-Erian, a recognized global thinker and Chief Economic Adviser at Allianz, suggested the value of bitcoin should be cut in half, citing the crackdown in China and his belief that current prices assume mass adoption. Meanwhile, JPMorgan Chase CEO, Jamie Dimon, called the digital currency a fraud.

So, what does all this mean? It's still pretty unclear. As for me, I will keep watching the rise — and possible fall — of bitcoin, while sticking to investments I know and understand that will help me grow wealth over the long term. And, maybe fund a wedding in the short term.

Is Inflation Dead Or On the Rebound?

Fed's 5-Year Index

Forward Breakeven Inflation Rate



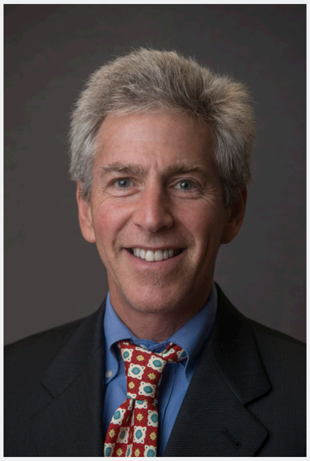
Source: Bloomberg Finance L.P. As of September 17, 2017

Coming into 2017, higher inflation was seen as a key risk in the market. So far, that has not materialized despite a synchronized global expansion and tight domestic labor market.

However, that may have started to change as we finally received a decent inflation report this past week. The CPI rose 0.4% in August. Core CPI came in at 0.2%, which was arguably an upside surprise given the string of disappointments in recent months. The CPI is up 1.9% from a year ago. A large part of the increase was in housing and shelter. Shelter increased 0.5% in August for the largest gain since 2005 and owners' equivalent rent was up 0.4%. Gasoline prices were also up sharply.

Further, while the recent storms will distort data over the next several months, the rebuild is likely to be massive and could certainly put upward pressure on several commodities as this occurs. Specifically, lumber and metals are likely to see a price hike as the rebuild commences.

Our Portfolio Management Team continues to believe in the inflation story in the medium and long term. As mentioned in my earlier section on the Fed, while we don't expect a rate increase at this meeting, market expectations of a rate hike before the end of 2017 have increased.



Marc Pfeffer

Managing Director, Institutional Fixed Income, Senior Portfolio Manager

Marc Pfeffer specializes in fixed income strategies. He is a Portfolio Manager on the CLS Flexible Income Fund team and manages 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 joined CLS in 2011, continuing as Senior Portfolio Manager for the Milestone Treasury Obligations Fund. The Fund was incorporated into CLS's fund family in January 2012. Mr. Pfeffer has more than 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 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.

Did you know? Marc is also an avid poker player.

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 Bloomberg Barclay's Capital U.S. Aggregate Bond® Index measures the performance of the total United States investment-grade bond market. The Bloomberg 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.

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*Note: Each shaded circle indicates the value (rounded to the nearest 1/8 percentage point) of an individual participant's judgment of the midpoint of the appropriate target range for the federal funds rate or the appropriate target level for the federal funds rate at the end of the specified calendar year or over the longer run. One participant did not submit longer-run projections for the federal funds rate.

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