CLS's WEEKLY 3

What You Need To Know About the Markets

OCTOBER 31, 2017

1. Did you know Americans now spend more money on Halloween than the GDP of 16 different countries?

2. The yield curve is changing - why this is important for investors to know.

3. Finally, it makes sense again to smartly manage cash balances.

CLS INVESTMENTS

Market Performance

Equities	LAST WEEK	QTD	YTD '17
Total U.S. Market[1]	+0.18%	+2.39%	+16.64%
Domestic Large-Cap Equity[2]	+0.23%	+2.55%	+17.16%
Domestic Small-Cap Equity[3]	-0.06%	+1.22%	+12.29%
International Equity[4]	-.054%	+1.23%	+22.62%
Developed International Equity[5]	-0.34%	+0.91%	+21.05%
Emerging Market Equity[6]	-0.84%	+2.67%	+31.20%
Fixed Income	**LAST WEEK**	**QTD**	**YTD '17**
U.S. Investment Grade Bonds[7]	-0.10%	-0.23%	+2.91%
Cash Equivalent[8]	+0.02%	+0.08%	+0.63%
Commodities	**LAST WEEK**	**QTD**	**YTD '17**
Commodity[9]	+0.72%	+1.75%	-1.17%

[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 10/27/2017

Week in Review

Despite a heavy slate of economic data releases last week, market performance was relatively muted making it a fairly quiet week. In the U.S., third quarter GDP surpassed analyst estimates at 3.0% versus an expected 2.6%. Other data points of note included Purchasing Managers' Index data, capital goods orders, and durable goods orders, which all beat estimates. Several large tech firms, including Amazon, Alphabet, Intel, and Microsoft, all released their third quarter earnings reports, which showed better-than-expected results.

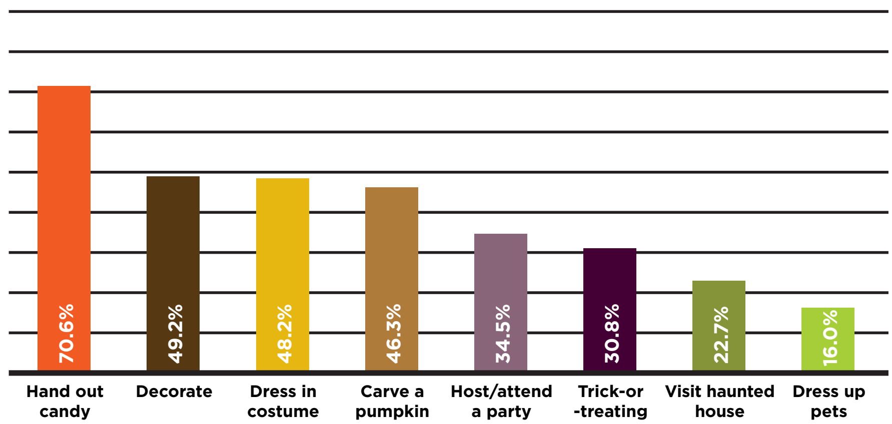
The domestic stock market was up alomst 0.2% on the week, with large-cap stocks outperforming small-caps on the back of the strong earnings data from a few tech giants. International markets were negative, with developed markets outperforming emerging. The U.S. bond market was down 0.10% for the week. Treasury yields were relatively volatile as the outlook for the next chair of the Federal Reserve shifted between Janet Yellen, John Taylor, and Jerome Powell. President Trump is expected to announce his selection by the end of this week. Overall, the top performing broad asset class was commodities.

Halloween is upon us, and Americans are prepared to celebrate in a big way. In fact, Halloween-related spending is expected to set a record in 2017. This will continue a trend that saw this ghoulish holiday seize the No. 2 slot for holiday spending, following Christmas and surpassing Valentine's Day.

According to the National Retail Federation's (NRF) annual survey, 71.7% of Americans are planning to celebrate this year, up from 69.1% in 2016, making it the highest percentage since the survey began in 2003. Celebration can occur in a variety of forms, the chart to the right provides a breakdown.

According to NRF data, total spending for 2017 is expected to reach $9.1 billion, up from $8.4 billion in 2016, the highest on record. The largest source of expenditures will be on costumes, with men planning to spend $96

How Respondents Expect to Celebrate Halloween



Sources: National Retail Foundation, as of September 2017

on average and women $77. Most of the remaining expenditures will be on candy and decorations.

To put this into perspective, the amount of money Americans expect to spend this year on Halloween exceeds the 2016 GDP of 61 out of 195 countries tracked by the World Bank. It makes you wonder why we do it. How did Halloween become such a deeply embedded tradition? A quick Google search shed some light on the matter.

The *genesis of Halloween* is a combination of Medieval and Christian traditions. Around 2000 years ago, the Celts living in what is now Great Britain, celebrated the ancient festival of Samhain

Josh Jenkins, CFA
Portfolio Manager

Joshua Jenkins manages CLS's moderate- to low-risk mutual funds and income-focused separate account strategies. He is a Portfolio Manager on the Milestone Treasury Obligations Fund, AdvisorOne CLS Growth and Income Fund, and AdvisorOne CLS Flexible Income Fund.

Mr. Jenkins joined CLS in 2013 as a Research Analyst and accepted the role of Portfolio Manager in 2015. Prior to joining CLS, he was an Analyst for Auriga, USA, LLC in New York City.

Mr. Jenkins received his Bachelor of Science degree in Finance from the University of Nebraska at Lincoln and holds the Chartered Financial Analyst (CFA) designation. He is a member of the CFA Society of Nebraska.

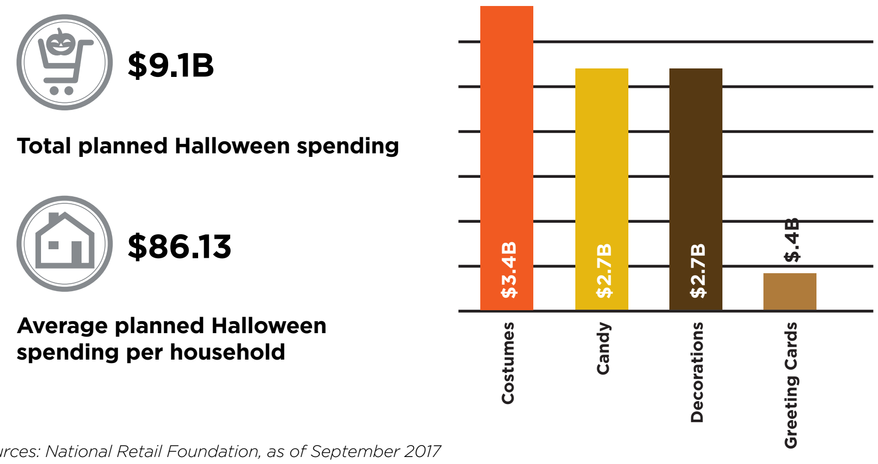
Did you know? Josh ran a 76-mile race for NorthStar.

(pronounced sow-in). October 31 represented the end of the harvest and beginning of the potentially deadly winter season. The Celts believed that on this day the boundary between the living and dead was at its thinnest and the dead could return to earth. Believers left food and wine on their doorsteps to ward off evil spirits, and they dressed up and wore masks outside hoping to be mistaken for fellow spirits.

In the eighth century, Pope Gregory III established November 1 as All Saints' Day, and the day after became All Souls' Day, a day to honor the dead. All Saints' Day was also referred to as All Hallows, with October 31 being All Hallows' Eve, eventually shortened to Halloween.

Trick-or-treating is believed to have its origins in the activities of "souling" and "guising." On All Souls' Day, poor individuals begged for pastries known as soul cakes,

Their Holiday Spending



Sources: National Retail Foundation, as of September 2017

and upon receipt they promised to pray for the provider's dead relatives. Guising was a practice in which children would dress up and receive food and money in return for singing or telling jokes.

Halloween festivities became widespread in the U.S. in the mid-1800s when waves of Irish immigrants fleeing famine brought these traditions with them. Initially, Halloween was more about parties and mischief, but by the 1950s it had transformed into the family-friendly, child-centric celebration it is today.

So, there are many people to thank for this spooky tradition that provides a night of fun and a helpful boon to our economy.

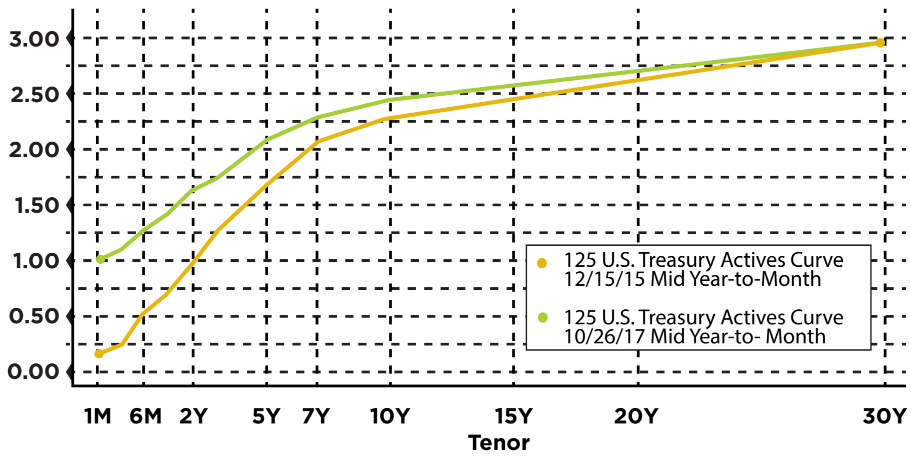
Watch the Yield Curve

The spread between short-term and long-term Treasury rates is near its lowest level since before the 2008 financial crisis. If this trend persists, it could have a profound impact on the future path of monetary policy and provide an advanced look at the direction of the economy.

The yield curve is a graphical representation of different bonds, in this case Treasury bonds, plotted out with term to maturity on the X-axis and yield on the Y-axis. The shape of the curve is generally described in one of three ways: normal, flat, or inverted. A normal curve shows the yield increasing as the term extends to maturity. This is considered normal because as the term is extended the risk associated with getting the principal back increases, and investors would therefore demand a higher yield to compensate for that increased risk. The Treasury yield curve has retained a normal shape for the last 10 years.

The curve's shape is not static; it changes as interest rates change. If rates increase or decrease by the same amount, regardless of maturity, it is referred to as a parallel shift. Alternatively, the curve could steepen if either long rates increase at a faster pace than short rates (bear steepening) or short rates fall at a faster pace than long rates (bull steepening). Finally, there may be a flattening of the curve. This occurs when short rates rise faster than long rates (bear flattening) or long rates fall faster than short rates (bull flattening). The curve has experienced a bear flattening since the Federal Reserve (Fed) began policy normalization in December 2015.

The Treasury Yield Curve



Sources: Bloomberg, as of October 26, 2017

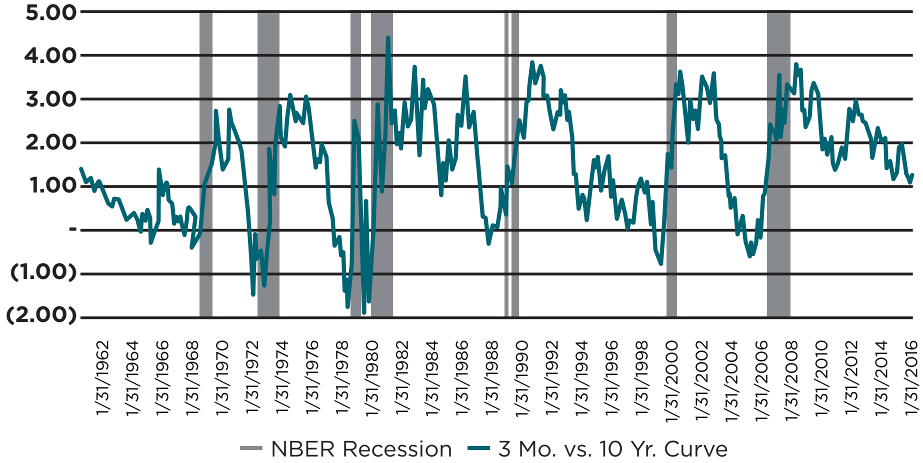
So, why does any of this matter? The shape of the yield curve is widely considered to be one of the best early predictors of a recession. More specifically, the signal flashes if the yield curve shape goes from normal to inverted. All of the last seven recessions have been preceded by an inverted yield curve.

A paper published by the Federal Reserve Bank of New York titled *"Monetary Cycles, Financial Cycles, and the Business Cycle"* provides a theory on the causal relationship between the shape of the yield curve and economic growth. The theory posits lending institutions generally borrow in the short term and lend in the long term. If the curve inverts, their cost to borrow exceeds the return on funds lent. This causes a contraction in the supply of credit and ultimately a contraction in output.

The front end of the yield curve is generally the most responsive to monetary policy, while the long end typically shifts based on expectations for long-term growth and inflation. Over the last two years, the Fed has increased its benchmark rate four times, while the outlook for growth and inflation has remained largely unchanged. This has contributed to the flattening evident in the top chart above.

If longer-term rates remain around current levels, reflecting unchanged expectations for future growth and inflation, the Fed may effectively be capped in how much it would continue to raise rates. Considering its theory on the causal relationship between the curve and economic output, the Fed would likely stop well short of excessive tightening that could put the current expansion in jeopardy.

Yield Curve vs. Recessions

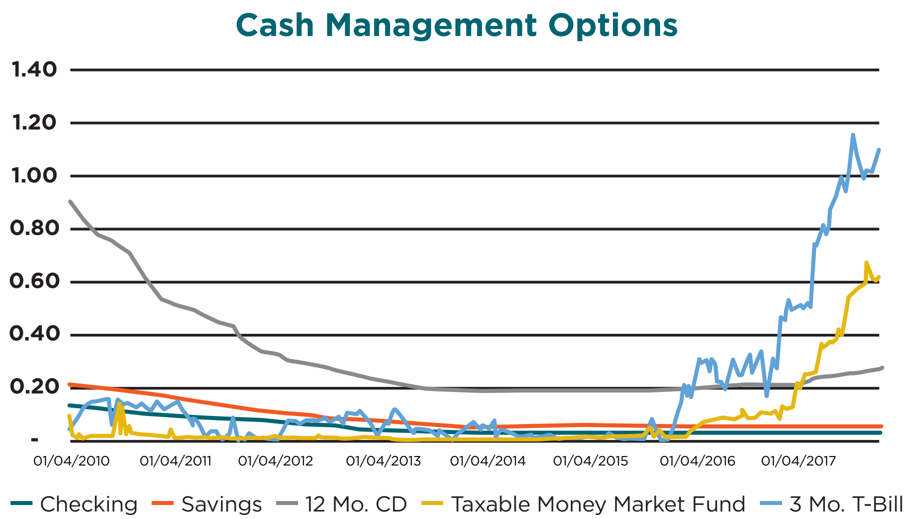


Sources: Bloomberg, FRED Database, as of October 23, 2017

Cash Management Matters Again

For much of the last 10 years, there has been little variance in cash yields. Money market funds, checking accounts, savings accounts, and Treasury bills, by and large, all yielded just a couple of basis points. Four rate hikes went into policy normalization, this is no longer the case. Cash instruments have come off the zero bound and are now generating some return, but not all options are created equal.

Despite the rise in rates, traditional checking and savings accounts continue to generate essentially nothing. According to the St. Louis Fed's Federal Reserve Economic Data (FRED) database, the national average rate on savings and checking accounts is 0.06% and 0.04%, respectively. Large-brokerage, cash-sweep accounts are generally in the same range. Some additional income can be picked up on 12-month certificates of deposit, but access to funds is generally lost and there are penalties for early withdrawals.



Sources: Bloomberg, FRED Database, and Morningstar, asOctober 23, 2017

Money market funds offer a meaningful boost in yield and daily liquidity. According to Morningstar, the average yield on taxable, non-prime funds is 0.63%, with some of the lowest-cost options yielding around 1%. Individuals with larger balances can purchase 3-month Treasury bills currently yielding about 1.10%. Finally, a few high-yield online savings accounts yield 1.20%-1.30%.

Whether it is an emergency fund, a rainy day fund, or dry powder waiting for a market pullback, cash should be working hard for investors. Previously, there was little difference in the income provided by the various options, but that is now changing. It may be worth it for investors to reassess whether their current cash vehicles are maximizing income and facilitating the appropriate level of liquidity and accessibility.

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 exchange-traded futures on physical commodities and represents 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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