Potential Opportunities For Income	Weaker Opportunities For Income
· Emerging Market Corporate Bonds	· International Sovereign Bonds
· High-Yield Municipal Bonds	· Treasurys
· International Real Estate	

MARKET REVIEW

Stocks Shake Off Short Lived Concerns

November is historically a strong month for stocks, which typically leads to the historically stronger month of December. Global stocks ended November with a gain of 1.94%, led primarily by U.S. and Japan, which increased by 3.07% and 2.99%, respectively. Europe and the emerging markets (EM) didn't fare as well, increasing by 0.22% and 0.20%, respectively. Small-cap U.S. stocks posted a strong month, increasing by 2.88%. November ended on a high note with nearly every major stock market hitting all-time highs on or within a week of 11/30. Market breadth was also strong, indicating a healthy bull market, as the advance-decline lines of most major stock markets coincidentally hit all-time highs in line with stock prices.

Bond markets had a very strange month as rates changed wildly, but ended with a nearly neutral -0.01% decline in the 10-year U.S. Treasury yield. Nearly all major bond asset classes declined as high-yield corporate bonds fell -0.26% and EM corporate bonds fell -0.04%. Treasurys also declined -0.14% for the month. However, global bonds increased by 1.11%, led by international sovereign bonds, which increased by 2.20%. Nearly all of that return can be attributed to gains in the euro and yen relative the U.S. dollar. We continue to believe that this trend isn't sustainable especially considering the increased likelihood of the passage of the tax bill currently making its way through Congress. We think investors should continue to be wary of this asset class.

STOCKS vs. BONDS

Another Look at Valuations

Nearly every investor is aware that stock valuations are high, but that doesn't seem to stop the buying frenzy. At the end of November, the S&P 500 Index was starting get into late-1990s levels of valuation with a median price-earnings ratio of 25.2x, roughly 1.5 standard deviations above the long-term median of 17.0x. Another favorite metric for valuation is market capitalization as a percentage of nominal gross domestic product (GDP). At the end of November, the S&P 500 was trading at 116% of GDP, again, in the same territory as the late 1990s and just shy of its 125% peak in March 2000. This high valuation is matched by a high level of confidence in the economy. The Conference Board Consumer Confidence Index reached 130, also in the same territory of the late 1990s, which peaked at 145 in January 2000. This data points to a high level of euphoria regarding stocks, but that isn't stopping buyers and they may be right to stay invested as valuation and sentiment are historically terrible timing mechanisms. For example, an investor who sold their S&P 500 position in 1998 (at a level similar to today's valuation) would have missed out on a 55% increase before the market corrected in a material way. On the other hand, valuation is great for long-term planning. At current multiples, it would be hard for new stock investments to expect double-digit annualized gains, so it is important to have in place a good risk management process to help determine when it is time to rotate away from stocks. However, we do not think that time is now.

One reason for the current bull market is the lack of any suitable alternative. At the peak of the market in Q1 2000, the 10-year Treasury was yielding 6.80%. Any prudent investor could have figured out that the long-term expected return for stocks at that point was below current Treasury yields. Meanwhile, today's yield of 2.42% is likely in line with the 10-year expected return of stocks and is therefore not attractive enough to pull investors out of the market. However, cash yields are going up and certain cash proxies are now yielding close to 1.80% with very little duration risk. It is likely that as the curve continues to flatten and cash approaches the 10-year Treasury yield, investors will become aware of the low expected return for stocks and the nearly risk-free option for cash income, which could kick off a serious correction. Only time will tell.

OUTLOOK

Just Some Thoughts

We started the year expecting emerging market stocks to lead the market and they are up 33.12% for the year while global stocks have increased 21.96%. We expected a positive return for stocks, but did not predict this type of rally. For bonds, we expected that credit would outperform. High-yield corporate bonds, EM corporate bonds, and high-yield muni bonds were our favorite asset classes for the year, and they have risen 7.20%, 9.27% and 8.54%, respectively, while global bonds have risen 7.28%. The surprise for bonds has been how robust the global bond market has been considering most global rates have increased for the year. As we have discussed in earlier commentaries this year, much of these gains have been driven by the increase of foreign currency prices relative the U.S. dollar, mostly the euro. In fact, when we account for currency, global bonds have only increased by 2.81%, putting them in line with U.S. bonds, which increased by 3.32% for the year. Those numbers make more sense given the economic backdrop. Moreover, from a purely fundamental standpoint, foreign bonds are on risky ground. Euro bonds are yielding 0.85% while Japanese government bonds are yielding 0.18%. At these levels, rates are more likely to go up than down and, given the strong economy, inflation is more likely than deflation. The final nail in the proverbial coffin is the current tax bill, which is expected to increase the deficit and will ultimately lead to increased value for the U.S. dollar relative other currencies. So where do we go from here? We think it is best to stick with the overall trend of the market and continue to overweight emerging markets and credit. Ultimately, we think the market will tell us where to go from here.

FUN FACT

A Story with a Twist

Astronomers in Hawaii spotted an alien visitor in our solar system. The object has been named Oumuamua, Hawaiian for “scout” or “messenger.” It is particularly odd because it is 10 times as long as it is wide, roughly 800 yards by 80 yards, and is red in color. These properties are not characteristic of any asteroids that make it into our solar system and so the object may be a visitor from very far away. The asteroid brightens and dims every seven hours or so, suggesting it is rotating on its short axis. It is likely from the solar system dominated by the star Lyra and would have taken 600,000 years to come to our solar system. Today, it is travelling nearly 40,000 miles per hour and will pass Jupiter next May as it exits our solar system.

Methodology

To learn more about the methodology visit the Salient Partners blog posting at www.salientpartners.com. You can also follow us on Twitter at @nrowader and @NicMillikan for live updates on the Income Report Card.

Asset Class Key

Bonds	
U.S. Treasurys	Bloomberg Barclays U.S. Treasury
U.S. Investment-Grade Credit	Bloomberg Barclays U.S. Credit Bond
Municipal Bonds	Bloomberg Barclays U.S. Municipal Bond
High-Yield Municipal Bonds	Bloomberg Barclays U.S. Municipal High Yield
U.S. High-Yield Corporate Bonds	Bloomberg Barclays U.S. Corporate High-Yield Bond
Emerging Market Corporate Debt	CS Emerging Markets Corporate Bond
Emerging Market Sovereign Debt	Bloomberg Barclays EM Sovereign Bond
International Sovereign Debt	Bloomberg Barclays Global Treasury ex-USD
Mortgages	Bloomberg Barclays U.S. MBS
Short-Term Treasurys (Cash Proxy)	Bloomberg Barclays U.S. Treasury Bond 1-3 Year Term

Stocks	
U.S. Stocks	S&P 500 Index
International Stocks	MSCI EAFE
Emerging Market Stocks	MSCI Emerging Markets
U.S. Real Estate	Dow Jones U.S. Real Estate
MLPs	Alerian MLP Infrastructure
Preferred Stocks	BofA Merrill Lynch Core Fixed Rate Preferred Securities
Utilities	S&P 500 Utilities Sector
International Real Estate	Dow Jones Global ex-U.S. Select Real Estate
EM Infrastructure	MSCI EM Infrastructure

Income Report Card: Stocks

Grades: Quintile rankings of asset classes
Downgrade Upgrade No Change

Trend: 12 month momentum
Carry: Current Yield / Current Std. Deviation

Risk: Based on 60-day std. deviation

U.S. Stocks

Yield: 1.90% **Risk:** 5.48%

TREND	CARRY	
B	D	U.S. stocks continue to outperform, eroding the income we are looking for. U.S. stocks remain one of the worst absolute level of income in our stock universe. We see U.S. stocks as a solid total return option and can be used as a good hedge against inflation and rising rates with regulatory changes on the horizon.

International Stocks

Yield: 3.07% **Risk:** 5.56%

TREND	CARRY	
A	B	Developed foreign markets have benefited greatly by the slowdown in bond purchases by the European Central Bank and the Bank Of Japan. Additionally, the U.S. dollar has seen a further decline relative to the euro and yen, significantly benefitting this asset class.

Emerging Market Stocks

Yield: 2.32% **Risk:** 10.02%

TREND	CARRY	
A	F	Emerging market stocks still produce low income, but the asset class offers strong diversification away from the U.S. economic environment. The strong trend, valuation and possible change in the long-term cycle all favor this asset class.

U.S. Real Estate

Yield: 4.12% **Risk:** 7.56%

TREND	CARRY	
D	B	The positive correlation with bonds should be taken seriously in this asset class, especially for any investor with a large position in fixed-rate bonds.

Master Limited Partnerships (MLPs)

Yield: 8.02% **Risk:** 18.30%

TREND	CARRY	
F	C	Volatility continues to rise. There was brief window where this asset class might have come back into favor. We are still waiting on an improving market for this asset class.

Preferred Stocks

Yield: 5.30% **Risk:** 2.18%

TREND	CARRY	
D	A	We see preferred stocks as the asset class to own for safe U.S.-based income. It does have a positive correlation to bonds, but the higher income stream should help protect it from changes in rates. The recent resurgence in bank stocks could find its way to preferreds in the near term.

Utilities

Yield: 3.25% **Risk:** 10.11%

TREND	CARRY	
C	D	As rising rates continue, we see downgraded carry as earnings multiples and long-term growth prospects continue to be weak in this asset class. We think preferred stocks are a better option for an income portfolio.

International Real Estate

Yield: 3.98% **Risk:** 6.54%

TREND	CARRY	
C	A	Volatility has been declining and the carry is looking very attractive at this point. The asset class has also lagged other international assets so there should be some relative value that could provide some good capital appreciation as well.

EM Infrastructure

Yield: 3.74% **Risk:** 7.48%

TREND	CARRY	
B	C	If EM stocks are too volatile, we believe this asset class is a great way to access to the economic growth of the emerging markets with some decent income and lower volatility. Additionally, most of these stocks are backed with hard assets and positive cash flow.

Income Report Card: Bonds

Grades: Quintile rankings of asset classes
Downgrade Upgrade No Change

Trend: 12 month momentum
Carry: Current Yield / Current Std. Deviation

Risk: Based on 60-day std. deviation

U.S. Treasurys

Yield: 2.15% **Risk:** 2.59%

TREND F CARRY F

Treasurys may be the purest way to express an interest rate position. As a result, this asset class represents the tip of the spear on the future of interest rates. If you must hold Treasurys, we believe short duration/cash-like or muni bonds are best.

U.S. Investment Grade Credit

Yield: 3.20% **Risk:** 2.76%

TREND C CARRY D

There has been an uptick in buying of investment grade credit. However, the strong economy still favors more credit risk, so we prefer high-yield over investment-grade credit.

Municipal Bonds

Yield: 2.47% **Risk:** 1.74%

TREND D CARRY D

Muni bonds offer an attractive yield relative Treasurys. However, the low likelihood of recession favors taking more credit risk. We think it is prudent to look to high-yield municipal bonds instead. But, if you must have a high-safety asset class, we prefer this asset class over Treasurys.

High-Yield Municipal Bonds

Yield: 5.39% **Risk:** 2.58%

TREND B CARRY B

This asset class is riskier than rated muni bonds, but, barring a recession (which seems unlikely at this juncture), we believe high-yield municipal bonds are a good alternative to any investment-grade holding. If you are looking for safe cash flow, we think this asset class is likely the best opportunity.

U.S. High-Yield Corporate Bonds

Yield: 5.68% **Risk:** 1.90%

TREND B CARRY B

The spread on high yield is very tight and investors have a right to be cautious. This asset class is still a good source for current income given the strength of the economy, but if you have to choose, EM corporate debt appears stronger.

Emerging Market Corporate Debt

Yield: 5.87% **Risk:** 1.36%

TREND A CARRY A

EM corporate debt has also been one of our favorite asset classes for 2017. The low price volatility and high current income makes this asset class very attractive. We don't expect this asset class to deliver total return like it did last year, but higher income may offset any increased rates.

Emerging Market Sovereign Debt

Yield: 4.99% **Risk:** 3.05%

TREND A CARRY C

If you absolutely need government bonds, we see this as your best bet. However, spreads are now at pre-crisis levels and the great returns here might not warrant the risk. Again, we'd suggest credit over sovereign bonds.

International Sovereign Debt

Yield: 0.66% **Risk:** 5.84%

TREND C CARRY F

This asset class has been a great performer this year, but its volatility is similar to stocks and it has a yield that offers very little cover in the case of rising interest rates, which have been going up. A pullback in currency values could lead to a very sharp decline, such as the near 4% drawdown in September.

Mortgages

Yield: 2.94% **Risk:** 1.74%

TREND D CARRY C

Mortgages continue to struggle in a rising rate environment. We have seen a downgrade in trend as the course of interest rate increases becomes more visible. Due to this macro trend, mortgages most likely do not belong in an income portfolio.

Short Term Treasurys (Cash Proxy)

Yield: 1.80% **Risk:** 0.54%

TREND F CARRY A

Right now we would prefer credit risk over short duration, but cash is starting to look very attractive as protection in the event of recessionary environment.

Definition of Terms

10-year U.S. Treasury is a debt obligation issued by the U.S. Treasury that has a term of more than one year but not more than 10 years.

Advance-decline line is a technical indicator that plots changes in the value of the advance-decline index over a certain time period.

Alerian MLP Infrastructure Index is the leading gauge of large- and mid-cap energy master limited partnerships (MLPs). The float-adjusted, capitalization-weighted index includes some of the most prominent companies and captures approximately 75% of available market capitalization.

Bloomberg Barclays EM Sovereign Bond Index is a rules-based market-value weighted index engineered to measure the fixed-rate local currency sovereign bonds issued in emerging markets as identified by Bloomberg.

Bloomberg Barclays Global Treasury ex-USD Index is an unmanaged index composed of those securities included in the Barclays Global Aggregate Bond Index that are Treasury securities, with the US excluded while hedging the currency back to the US dollar.

Bloomberg Barclays U.S. Aggregate Bond Index represents securities that are U.S. domestic, taxable and dollar denominated. The index covers the U.S. investment-grade, fixed-rate bond market, with index components for government and corporate securities, mortgage pass-through securities and asset-backed securities.

Bloomberg Barclays U.S. Corporate High-Yield Bond Index covers the USD-denominated, noninvestment-grade, fixed-rate, taxable corporate bond market. Securities are classified as high yield if the middle rating of Moody's, Fitch and S&P is Ba1/BB+/BB+ or below.

Bloomberg Barclays U.S. Credit Index is an index composed of corporate and non-corporate debt issues that are rated investment grade (Baa3/BBB) or higher.

Bloomberg Barclays U.S. Mortgage Backed Securities (MBS) Index tracks the mortgage-backed pass-through securities of Ginnie Mae (GNMA), Fannie Mae (FNMA) and Freddie Mac (FHLMC).

Bloomberg Barclays U.S. Municipal Bond Index covers the USD-denominated, long-term tax-exempt bond market. The index has four main sectors: state and local general obligation bonds, revenue bonds, insured bonds and pre-refunded bonds.

Bloomberg Barclays U.S. Municipal High Yield Index measures the noninvestment-grade and nonrated U.S. dollar-denominated, fixed-rate, tax-exempt bond market within the 50 United States and four other qualifying regions (Washington D.C., Puerto Rico, Guam and the Virgin Islands).

Bloomberg Barclays U.S. Treasury Index is an unmanaged index of public obligations of the U.S. Treasury with a remaining maturity of one year or more.

Bloomberg Barclays U.S. Treasury Bond 1-3 Year Term Index is an unmanaged index of public obligations of the U.S. Treasury includes public obligations of the U.S. Treasury with a maturity between 1 and up to (but not including) 3 years.

BofA Merrill Lynch U.S. Core Fixed Rate Preferred Stock Index consists of investment-grade, fixed and fixed-to-floating rate U.S. dollar-denominated preferred securities.

CBOE Volatility Index is a popular measure of market risk and is constructed using the implied volatility of S&P 500 index options.

Consumer confidence index (CCI) is a measure of consumer confidence, defined as the degree of optimism on the state of the economy that consumers are expressing through their activities of savings and spending.

Consumer price index (CPI) is an index number measuring the average price of consumer goods and services purchased by households. The percentage change in the CPI is a measure of inflation.

Credit Suisse Emerging Market Corporate Bond Index consists of U.S. dollar-denominated fixed-income issues from Latin America, Eastern Europe and Asia.

Dow Jones Global ex-U.S. Select REIT Index measures the performance of equity real estate investment trusts (REITs) and real estate operating companies (REOCs) traded globally, excluding the U.S.

Dow Jones U.S. Real Estate Index measures the performance of the real estate industry of the U.S. equity market.

JPMorgan Global Manufacturing Purchasing Managers' Index is a composite index that serves as a global economic indicator by measuring different business conditions in 24 countries, including global manufacturing output, new orders and employment across the global manufacturing sector.

MSCI EAFE (Europe, Australasia and Far East) Index is a stock market index that is designed to measure the equity market performance of developed markets outside of the U.S. and Canada.

MSCI Emerging Markets Index is a free float-adjusted market capitalization index that is designed to measure equity market performance in the global emerging markets.

MSCI Emerging Markets Infrastructure Index captures the global opportunity set of companies that are owners or operators of infrastructure assets.

MSCI Emerging Markets Index is a free float-adjusted market capitalization index that is designed to measure equity market performance in the global emerging markets.

MSCI Emerging Markets Infrastructure Index captures the global opportunity set of companies that are owners or operators of infrastructure assets.

MSCI World Index is a free float-adjusted market capitalization index designed to measure equity market performance in the global developed markets.

Max drawdown is the percentage of loss that an asset incurs from its peak net asset value to its lowest value.

NASDAQ-100 is a modified capitalization-weighted index that includes the largest nonfinancial U.S. and non-U.S. companies listed on the NASDAQ stock market across a variety of industries, such as retail, healthcare, telecommunications, wholesale trade, biotechnology and technology.

NYSE Advance/Decline Indicator is a technical indicator that charts the difference between the number of advancing stocks and declining stocks on the NYSE in a given market on a given day.

NYSE New Hights/Lows is a technical indicator that charts the highest and lowest prices over 52 weeks of NYSE stocks in a given market on a given day.

Russell 2000 Index measures the performance of the 2,000 smallest companies in the Russell 3000 Index. The Russell 3000 Index represents approximately 98% of the investable U.S. equity market.

S&P 500 Index is an unmanaged index of 500 common stocks chosen to reflect the industries in the U.S. economy.

S&P 500 Financials Index comprises those companies included in the S&P 500 that are classified as members of the GICS® financials sector.

Sharpe ratio is a ratio developed by Nobel laureate William F. Sharpe to measure how a fund performs relative to the risk it takes.

Standard deviation measures the degree to which a fund's return varies from its previous returns or from the average of all similar funds.

Valuation is the process of determining the value of an asset or company based on earnings and the market value of assets.

VIX (the ticker symbol for the Chicago Board Options Exchange Volatility Index) is a popular measure of market risk and is constructed using the implied volatility of S&P 500 index options.

Yield is the interest or dividends received from a security and is usually expressed annually as a percentage based on the investment's cost or on the U.S. government's debt obligations.

Salient®

4265 San Felipe
8th Floor
Houston, TX 77027

800-994-0755

www.salientpartners.com

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