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INVESTMENT CONCEPTS
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3rd Quarter 2017 in Review

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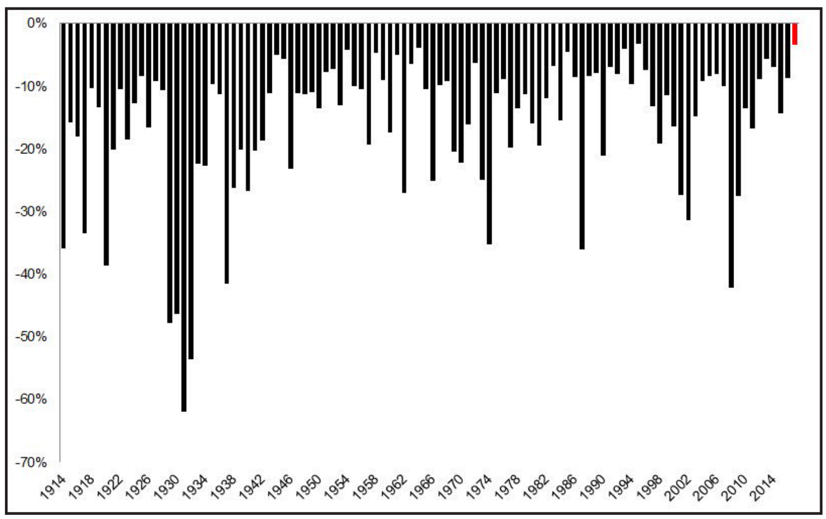
This past quarter our world experienced several events that challenged the human spirit. In the wake of devastating hurricanes, racially charged demonstrations, infuriating security breaches, and a sickening mass shooting, our hearts go out to those whose lives have been re-arranged as a result. At the same time, we stand up and cheer for those who have made the effort and sacrifice to stand in the gap and provide help during these times of crisis. This truly is a time to love your neighbor.

Meanwhile, it has been a very good quarter for investors as the S&P 500, as well as most market indexes, finished at all-time highs. That makes it 8 quarters in a row that the market has been positive. Not only have the markets been moving higher, they are doing so without many pullbacks along the way, which brings us to a term that we investment geeks call "max drawdown." Max drawdown refers to the amount of decrease from a high to a low over a certain period of time. The following chart created by Michael Batnick shows the max drawdown of the S&P 500 by calendar year for the past 100+ years. So far this year, the max drawdown is just under 3%, a level seen only once before (1995). Obviously we still have a quarter to go, but it's been a remarkable year so far.



Source: Created by Michael Batnick, tweeted by @ReformedBroker

Rational investors will realize that this is not a situation that is going to last forever. It is likely that when the market starts to smell the next recession, a deeper correction will ensue. But don't let the inevitability of an upcoming correction paralyze you with fear. As a client of Castle, your investment portfolio is designed not just to participate when markets are moving in your favor, but to meet your long-term objectives, which includes allowing diversification to smooth out the bumps that come along the way. The current batch of data continues to show that such recessionary signals are still off in the distance, but we will continue to be vigilant. After reviewing the index performance numbers, we will highlight some of the themes that are currently impacting the investment landscape.

Index	3rd Qtr 2017 Return	1 Year Return	3 Year Annualized Return	5 Year Annualized Return
S&P 500	2.1%	18.6%	10.8%	14.2%
Nasdaq Composite	1.1%	23.7%	14.4%	17.3%
Russell 2000 – Smaller Companies	6.2%	20.7%	12.2%	13.8%
MSCI EAFE – International	2.5%	19.1%	5%	8.4%
Barclays US Aggregate Bond	0.9%	0.8%	2.7%	2.1%

U.S. Economy

The United States Economy has been growing steadily for 8 years. While some questions have been raised about the economic impact of the recent hurricanes, it appears as though the drag that will occur from lower employment in these areas will be offset by the increased activity in construction and vehicle replacements, thus making the net impact not particularly significant to the overall economy.

Something that could impact the economy is the implementation of fiscal stimulus. A meaningful tax reform package, which is unlikely to be passed without a tax cut of some sort, would probably provide an economic boost at least for a year or so.

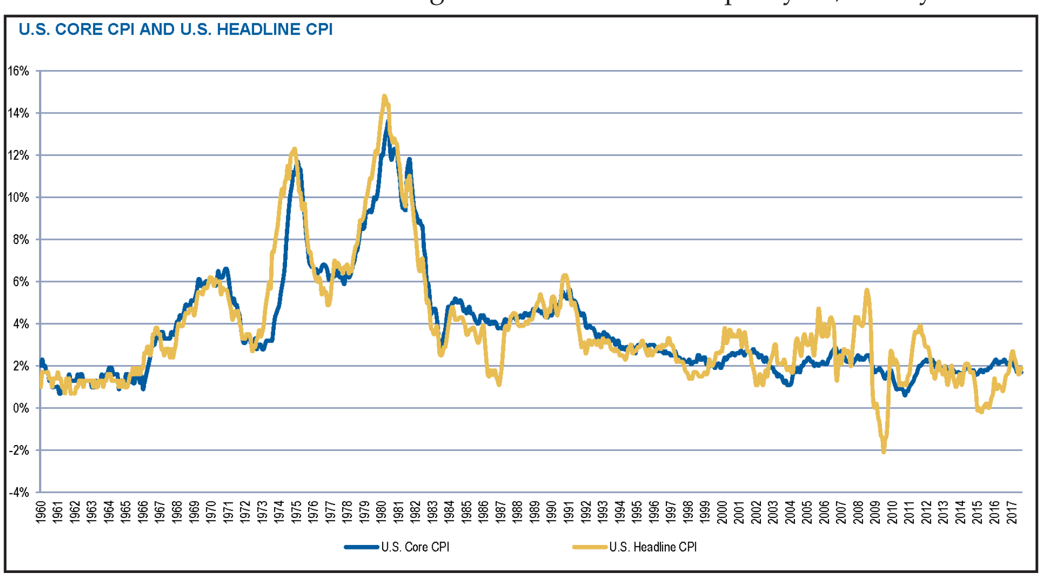
The Rest of the World

We often hear of the disasters that happen overseas, but maybe you didn't know that there is currently significant economic growth outside the U.S. Last quarter we mentioned the remarkable increases in the Global PMI index. This measure is now the highest it has been since 2011, indicating economic growth for every major developed and emerging country in the world. This growth is leading to the beginning of central banks moving rates back on the road toward a more normal level.

While earnings in the U.S. and Japan have eclipsed their all-time highs, European and Emerging Market countries still have a ways to go before returning to their previous peaks.

Inflation

Inflation remains quite low at under 2% and had been falling over the course of the past year, mostly due to the stabilization of medical costs and the lower cost of cell phone service. However, this trend appears to be reversing. With the worldwide growth that we just mentioned increasing demand for energy and driving lower the value of the U.S. Dollar, this has caused energy costs to rise along with the costs of imported goods. While not expecting runaway inflation, analysts are expecting to see an increase from these low levels.



Source: Neuberger Berman Deep Dive, 9.2017

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Federal Reserve

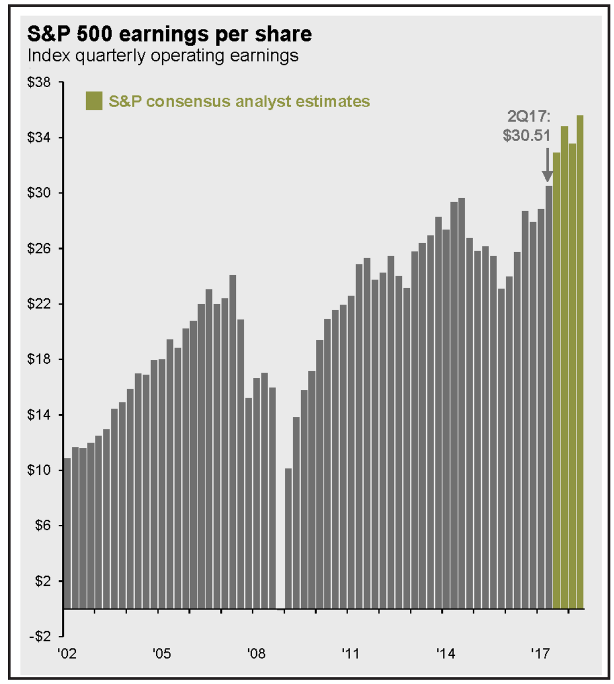
The Federal Reserve has announced a multi-year plan to reduce the size of its balance sheet. As part of the Quantitative Easing program that it implemented in an attempt to protect the economy following the Global Financial Crisis of 2008, the Fed accumulated trillions of dollars of bonds. As they now try to normalize, they will not replace these bonds as they mature. This combined with the gradual raising of their lending rate should have the impact of increasing interest rates, certainly those in the short-term and likely longer-term as well.

In addition, there is speculation about whether Chairwoman Yellen will be re-appointed when her term ends in early 2018. A change in leadership could make the trajectory of rising interest rates more aggressive.

Valuations

This past earnings season has been very good, keeping 2017 on pace to grow more than 10% from the past year, with double digit growth expected for the next few quarters.

Meanwhile, the stock market has become a little expensive, currently trading at a P/E of 17.7 compared with a 25 year average of 16. The higher this number goes, the more difficult future gains will be to obtain; this is another data point that deserves regular monitoring.



Source: JP Morgan Asset Management, 9.30.2017

Thanks for reading this quarter's update. We also hope you had a chance to check out the presentation we put together about what you can do, and we continually do, to keep your data safe. If you missed it, the file is available for download at http://bit.ly/2yaySaq. Along those lines, included with this newsletter is the annual disclosure of our privacy policy. Have a great fall.

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