January 2018

About Beacon Financial Advisors Ltd.

Beacon is an independent fee-only advisor with a clear mission statement: To provide our clients long-term value-added financial counsel and investment performance with *exceptional service.* **Beacon** is a Registered Investment Advisor with the US Securities and Exchange Commission.

Beacon's Advisors

MARCEL HEBERT has a B.S. in Finance, an M.B.A., and is a Certified Financial Planner (CFP) licensee and a Chartered Financial Analyst (CFA) charterholder.

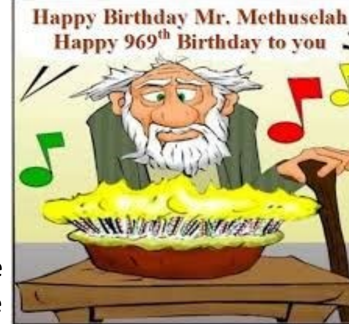
JOSH HEBERT has a B.S. in Accounting, an M.B.A., and is a Certified Internal Auditor (CIA) and a Certified Financial Planner (CFP) licensee.

Please remember to contact Beacon Financial Advisors, Ltd. if there are any changes in your financial situation or investment objectives, or if you wish to impose, add, or modify any reasonable restrictions to our investment management services. A free copy of our FIRM BROCHURE (Form ADV, Part 2) is always available upon request.

An important note: Where reference is made in VIEW to Beacon's relative performance, or individual mutual fund performance, it applies to fully invested portfolios for the period including reinvestment of income. Actual results vary among clients, as risk tolerance levels and the timing of asset purchases & sales are unique to each of our clients. Each client's unique results are revealed in the performance reports inside their Portfolio Review. Clients are urged to compare the custodians (Charles Schwab et al) account statements with Beacons reports.

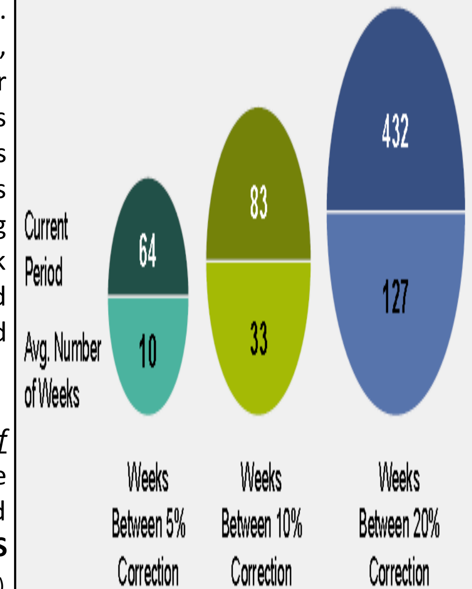
March 9, 2009—December 31, 2017: The METHUSELAH MARKET

"When Methuselah had lived 187 years he became the father of Lamech. And after he became the father of Lamech, Methuselah lived 782 years and had other sons and daughters. Altogether, Methuselah lived 969 years, and then he died." **(Genesis 5:25-27, NIV)**



Today's bull stock market reminds us of an aged-Methuselah—quite old, yet not dead. After all, from March 2009 lows we're nearing the bull's 9th birthday. As **BEACON** wrote last April in our 2017 Q1 VIEW regarding the time-duration of this bull market—it is indeed a very long period by historical measures. If for no other reason than time-duration some observers have declared stock prices have peaked or, are overvalued. Yet, there is no "rule" dictating the time-duration of the business/economic cycle or to stock market phases. Historically, bull markets have usually ended due to major inflection points like when interest rates increase faster than expected due to inflation-pressure, or geopolitical shocks like oil supply disruptions and the like. Other times stocks retreat due to policy mistakes by politicians or regulators—the US Federal Reserve ("FED") has a big task in 2018 of monetary reversal (removing much of the liquidity pumped into the financial sector after the 2008 "Great Recession"). Are stock and bond investors correctly reading FED signals about rate hike timing and frequency, bond repurchases, etc., or will the FED "surprise" the markets? As for the stocks-are-overvalued argument, corporate earnings have been a tailwind and supportive of prices of stocks (see p. 2).

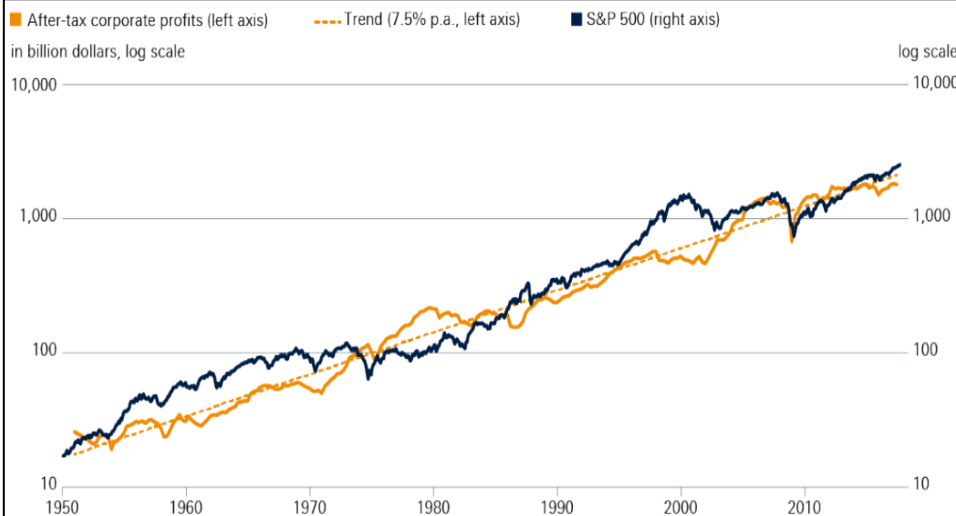
One consideration not in dispute is we are overdue for a price *correction—a reverse in stock prices of 5%-20% in an up-trending market*. As the chart on right depicts, US stocks have gone way past the norm without a correction. Will that change in 2018? Perhaps so. Tax reform is constructive, and perhaps "animal spirits" are unleashed. But the FED bears watching (see above). What is **BEACON'S** approach for your portfolio?—rebalance as needed and remain thoughtfully diversified. (continued p. 2)



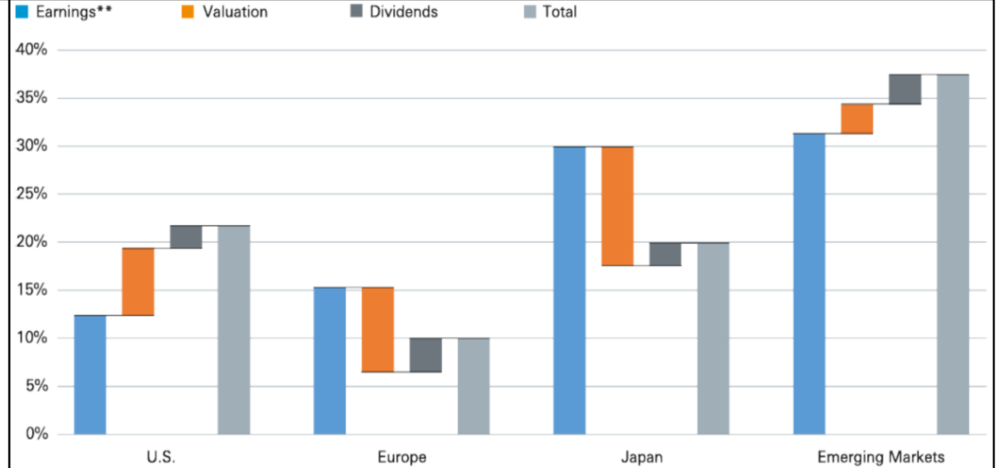
March 9, 2009—December 31, 2017: The METHUSELAH MARKET

Are stocks, notably US large company stocks, overvalued? It depends in large part on earnings—that is, *future* earnings. After all, every financial analyst and MBA student knows the value of a stock today is the discounted *present* value of *future* earnings (or operating, recurring cash flows). Said simpler—buying a stock means acquiring a claim on *future* profits. As the *future* is unknowable, analysts' make estimates. Also, as every value manager knows markets often "price" a stock at a level higher or lower than it's "value". Today's F.A.A.N.G. stocks (Facebook, Amazon, Apple, Netflix, Google) have high prices, and the *future* earnings will determine which direction prices for those tech-darlings go (or, in the case of Amazon, how they execute their growth strategy).

As we begin 2018, we'll venture **two** useful observations informed by the charts below. **First**, based on corporate earnings (and today's low interest rates), our stock partners contend good values can be had as dispersion is elevated—some stocks expensive, others more attractive. On the lower-left is the relationship between US corporate profits and US stock prices. The past 70+ years from 1945 US corporate after-tax profits have risen by 7.5% annually compared to the S&P 500 rise of 7.3% annually. While there've been times stock price gains weren't justified by corporate earnings, such as late 1990's tech-mania, overall there is a close correlation. Today's elevated stock prices appear to be supported by historically high corporate earnings. **Second**, international stock prices appear relatively attractive to those in the US. The chart on he lower-right depict the drivers* of stock returns in 2017 across the globe. In the US and Emerging Markets, stock returns included increases beyond earnings and dividends—that is, P/E multiples increased—meaning investors bid up prices beyond earnings and dividends (*positive* **ORANGE BAR**). In contrast, European and Japanese stock P/E multiples actually decreased (*negative* **ORANGE BAR**) even while earnings and dividends were quite good. [*We recommend **BEACON'S** August 2016 white paper Rates (&Weights) of Investment Return (Part 2) wherein we describe the components/drivers of stock returns as earnings growth, dividend yield and valuation (i.e. Price/Earnings) expansion (http://www.bfaltd.com/files/RATES%20and%20WEIGHTS%20OF%20INVESTMENT%20RETURN%20PART%202.pdf).]



Sources: Bloomberg Finance L.P., Board of Governors of the Federal Reserve System, Deutsche Asset Management Investment GmbH; as of 10/10/17



Sources: Bloomberg Finance L.P., Deutsche Asset Management Investment GmbH, as of 1/3/18
*U.S.: S&P 500, Europe: Euro Stoxx 50, Japan: MSCI Japan Index, Emerging Markets: MSCI Emerging Markets Index
** Basis: last 12-months earnings

Asset Allocation (aka diversification) divides your funds into different asset types that typically provides exposure to the period *best* and *worst* returners, generating a blended return designed to achieve your financial goals. The matrix chart below is instructive. Over a decade and a half from 2003-2017—a notable period including the "Great Recession" of 2007-2009—a 60/40 **Asset Allocation** returned 8.3% annualized (see **RED CIRCLE** below). Indeed **Asset Allocation's** solid return rivaled the returns of the worlds' developed stock markets, nearly 7X greater than **Cash** (i.e. money in the bank), with risk (volatility) about half that of stocks. In 2017 **Asset Allocation** returned over 14% as the *best* returner was **Emerging Market Equity** at nearly 38% versus the *worst* **Cash** at 0.8%. 2017 witnessed positive returns in all major asset classes following a solid 2016. 2017 witnessed reversal of a multi-year trend—the **US Large Cap** and **US Small Cap** conceded top-billing to non-US stocks **Emerging Market Equity** and **Developed Market Equity**. Restated, effective diversification (aka Asset Allocation) means always owning some of the *best* performers while limiting exposure to the *worst*. The white **Asset Allocation** boxes connected with the black line-graph clearly produced that *smoothing* result across the full length of the turbulent 2003-2017 years. Sometime ago a wise fellow named King Solomon wrote:

"Divide your investments among many places, for you do NOT know what risks might lie ahead." Ecclesiastes 11:2 (New Living Translation)

2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2003 - 2017 Ann.	Vol.
EM Equity 56.3%	REITs 31.6%	EM Equity 34.5%	REITs 35.1%	EM Equity 39.8%	Fixed Income 5.2%	EM Equity 79.0%	REITs 27.9%	REITs 8.3%	REITs 19.7%	Small Cap 38.8%	REITs 28.0%	REITs 2.8%	Small Cap 21.3%	EM Equity 37.8%	EM Equity 12.7%	EM Equity 23.0%
Small Cap 47.3%	EM Equity 26.0%	Comdty. 21.4%	EM Equity 32.6%	Comdty. 16.2%	Cash 1.8%	High Yield 59.4%	Small Cap 26.9%	Fixed Income 7.8%	High Yield 19.6%	Large Cap 32.4%	Large Cap 13.7%	Large Cap 1.4%	High Yield 14.3%	DM Equity 25.6%	Small Cap 11.2%	REITs 22.3%
DM Equity 39.2%	DM Equity 20.7%	DM Equity 14.0%	DM Equity 26.9%	DM Equity 11.6%	Asset Alloc. -25.4%	DM Equity 32.5%	EM Equity 19.2%	High Yield 3.1%	EM Equity 18.6%	DM Equity 23.3%	Fixed Income 6.0%	Fixed Income 0.5%	Large Cap 12.0%	Large Cap 21.8%	REITs 11.1%	Small Cap 18.8%
REITs 37.1%	Small Cap 18.3%	REITs 12.2%	Small Cap 18.4%	Asset Alloc. 7.1%	High Yield -26.9%	REITs 28.0%	Comdty. 16.8%	Large Cap 2.1%	DM Equity 17.9%	Asset Alloc. 14.9%	Asset Alloc. 5.2%	Cash 0.0%	Comdty. 11.8%	Small Cap 14.6%	Large Cap 9.9%	Comdty. 18.8%
High Yield 32.4%	High Yield 13.2%	Asset Alloc. 8.1%	Large Cap 15.8%	Fixed Income 7.0%	Small Cap -33.8%	Small Cap 27.2%	Large Cap 15.1%	Cash 0.1%	Small Cap 16.3%	High Yield 7.3%	Small Cap 4.9%	DM Equity -0.4%	EM Equity 11.6%	Asset Alloc. 14.6%	High Yield 9.6%	DM Equity 18.4%
Large Cap 28.7%	Asset Alloc. 12.8%	Large Cap 4.9%	Asset Alloc. 15.3%	Large Cap 5.5%	Comdty. -35.6%	Large Cap 26.5%	High Yield 14.8%	Asset Alloc. -0.7%	Large Cap 16.0%	REITs 2.9%	Cash 0.0%	Asset Alloc. -2.0%	REITs 8.6%	High Yield 10.4%	DM Equity 8.6%	Large Cap 14.5%
Asset Alloc. 26.3%	Large Cap 10.9%	Small Cap 4.6%	High Yield 13.7%	Cash 4.8%	Large Cap -37.0%	Asset Alloc. 25.0%	Asset Alloc. 13.3%	Small Cap -4.2%	Asset Alloc. 12.2%	Cash 0.0%	High Yield 0.0%	High Yield -2.7%	Asset Alloc. 8.3%	REITs 8.7%	Asset Alloc. 8.3%	High Yield 11.3%
Comdty. 23.9%	Comdty. 9.1%	High Yield 3.6%	Cash 4.8%	High Yield 3.2%	REITs -37.7%	Comdty. 18.9%	DM Equity 8.2%	DM Equity -11.7%	Fixed Income 4.2%	Fixed Income -2.0%	EM Equity -1.8%	Small Cap -4.4%	Fixed Income 2.6%	Fixed Income 3.5%	Fixed Income 4.1%	Asset Alloc. 11.0%
Fixed Income 4.1%	Fixed Income 4.3%	Cash 3.0%	Fixed Income 4.3%	Small Cap -1.6%	DM Equity -43.1%	Fixed Income 5.9%	Fixed Income 6.5%	Comdty. -13.3%	Cash 0.1%	EM Equity -2.3%	DM Equity -4.5%	EM Equity -14.6%	DM Equity 1.5%	Comdty. 1.7%	Cash 1.2%	Fixed Income 3.3%
Cash 1.0%	Cash 1.2%	Fixed Income 2.4%	Comdty. 2.1%	REITs -15.7%	EM Equity -53.2%	Cash 0.1%	Cash 0.1%	EM Equity -18.2%	Comdty. -1.1%	Comdty. -9.5%	Comdty. -17.0%	Comdty. -24.7%	Cash 0.3%	Cash 0.8%	Comdty. -0.3%	Cash 0.8%

CHART FROM J.P. MORGAN ASSET MANAGEMENT 2018 Q1 GUIDE TO THE MARKETS - PAGE 60

"Asset Allocation" portfolio assumes the following index weights: 25% S&P 500, 10% Russell 2000, 15% MSCI EAFE, 5% MSCI EMI, 25% Barclays Capital Aggregate, 5% Barclays 1-3m Treasury, 5% Barclays Global High Yield, 5% Bloomberg Commodity Index, 5% NAREIT Equity REIT Index.

(NOTE: An investor cannot invest directly in an index, and its performance does not reflect investing costs).

Our STOCK and BOND Fund Partners for 2017: Green Lights all the way!

STOCKS enjoyed robust returns in US and international markets led by non-US companies. As the chart on right reveals, the S&P 500 Index (**Large Cap**) had a total return (including dividends) of 21.8%. But, the asset class stars of 2017 were **Emerging Market Equity** and **Developed Market Equity**—the results supported **BEACON'S** contention that international stock prices/valuations were comparatively attractive [to US counterparts] as we maintained a full-to-slight overweight in that asset class. **BEACON'S** stock partners acquitted themselves well as almost all had double-digit returns for 2017.

Our top-performing US stock partner in 2017 was Jensen Quality Growth Inst'l (JENIX) with a 23.5% return—the 2018 Jensen Outlook:

Similar to this time last year, we maintain a constructive view of U.S. equity markets due to improving global economic growth, the combination domestically of strong employment and manageable inflation, and expectations of prudent U.S. Fed tightening actions. As a result, our 2018 outlook remains favorable. It is underscored by expectations of mid-teens S&P 500 Index earnings growth, stable economic conditions in large countries worldwide, and the likelihood of domestic tax reform. Potential threats to this view include a meaningful uptick in inflation, more-hawkish-than-expected U.S. Fed Policy, and unexpected global geopolitical turmoil.

It's widely reported that recent year's fund flows have favored "passive" indexes in mutual funds and exchange traded funds (ETFs), and "active" managers like **BEACON'S** partner Dodge & Cox are viewed by many as passé . **We disagree**. And so does Morningstar and The New York Times. In Dodge & Cox: Built to Last analyst Andrew Daniels of Morningstar reinforces that patient investors (like **BEACON**) have benefited from Dodge & Cox's steadfast commitment to put it's shareholders first (i.e. aligned interests). In Wealth Built Quietly With Old-School Ways NYT journalist Landon Thomas Jr. reminds that Dodge & Cox's "old school" methods never really go out of style. [NOTE: click on the blue hyperlink's above to read articles at www.dodgeandcox.com].

BONDS produced above-inflation gains with the broad US market Bloomberg/Barclays (US) Aggregate (**Fixed Income**) returning 3.5%. However, there was wide variance between bond sectors as **High Yield** corporate bonds gained 10.4% while **Cash** returned 0.8%. Dodge & Cox Income (DODIX) returned over 4.3% outpacing the broad market, while MetWest Total Return (MWTIX) gained 3.4%. Our global bond returns ranged from 3.1% AB Global Bond (ANAYX-currency hedged) to 8.3% Dodge & Cox Global Bond (DODLX-currency unhedged).

Tax-exempt municipal bonds enjoyed splendid returns reversing a late 2016 post-election **muni-bond Trump-SLUMP*** (*expectation individual tax rates will be lowered, making tax-exempt municipal bonds relatively less attractive). As many of our taxable client accounts hold municipal bonds, this asset class plays a pivotal role in our portfolios. As **BEACON** predicted in our 2016 Q4 VIEW about the **muni-bond Trump-SLUMP**, municipals found firmer footing in 2017 as investors correctly surmised tax-reform would produce only modest decreases in the top individual rate. Our municipal managers at AB Global and Fidelity generated solid returns with AB High Income Municipal (ABTYX) gaining over 10%. As always in **BEACON'S** clients' balanced, global portfolios, the primary portfolio-goals of bonds are income generation and stabilizing shock-absorbers for more volatile stocks—the diversifying "anchor to windward" in our portfolio construction.

2017
EM Equity 37.8%
DM Equity 25.6%
Large Cap 21.8%
Small Cap 14.6%
Asset Alloc. 14.6%
High Yield 10.4%
REITs 8.7%
Fixed Income 3.5%
Comdty. 1.7%
Cash 0.8%

Overall 2017 was a robust year for our balanced, global portfolios. Clients' total returns ranged from 9%-11% for conservative client-portfolios up to 16%+ for moderate-aggressive client-portfolios. Accounts holding municipal bonds fared better than those holding taxable bonds as the tax-free sector proved durable even with tax-reform.