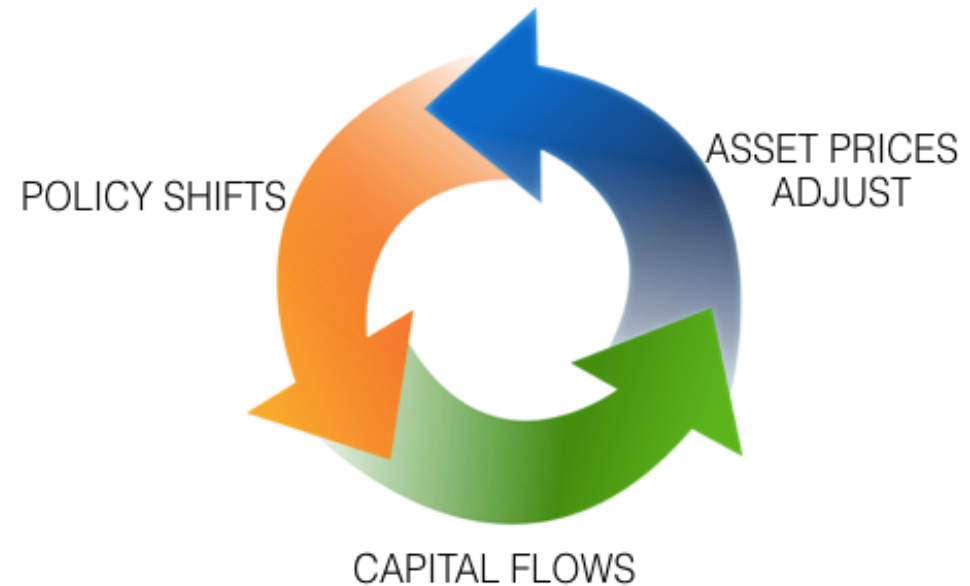

CAPITAL POURS INTO GROWTH

Macro investing can be simplified into a very logical, three step process.

1. Policy Shift: A policy shift occurs changing the “rules of the game.” When the rules change, players (investors) change their behavior which impacts global...
2. Capital Flows: Capital flows to where it is treated best (earns the highest after tax returns). Pro-growth policies attract capital. Anti-growth policies repel capital. Capital flows in/out of asset classes, countries, sectors and industries determine...
3. Asset prices: Capital flows change the supply/demand for assets causing market prices to adjust.



Investors should view this asset allocation process as a circular system. Meaning, one can observe what is happening in any step and make logical assessments about the future. One can start by studying policy changes and try to anticipate capital flows. Or one can look at how asset prices are adjusting to capital flows and try to identify the durable policy shift that caused the move. Or one can do both, as we do. We analyze policy to make predictions about how policy shifts will alter future capital flows and asset prices. But we also work in reverse using asset price trends to reveal how capital is already flowing in an effort to reveal the policy reasons why.

POLICY BASED INVESTING

by Russell Redenbaugh & James Juliano

Monday, March 4, 2019

There are four main, global asset classes that dominate the flow of capital around the world: stocks, bonds, real estate & commodities. Each asset class performs best under different economic conditions, over or under performing based on the current mix of economic growth expectations coupled with currency valuation expectations. The intersection of rising or fall growth and currency results in our 2x2 matrix “Investing Map.”

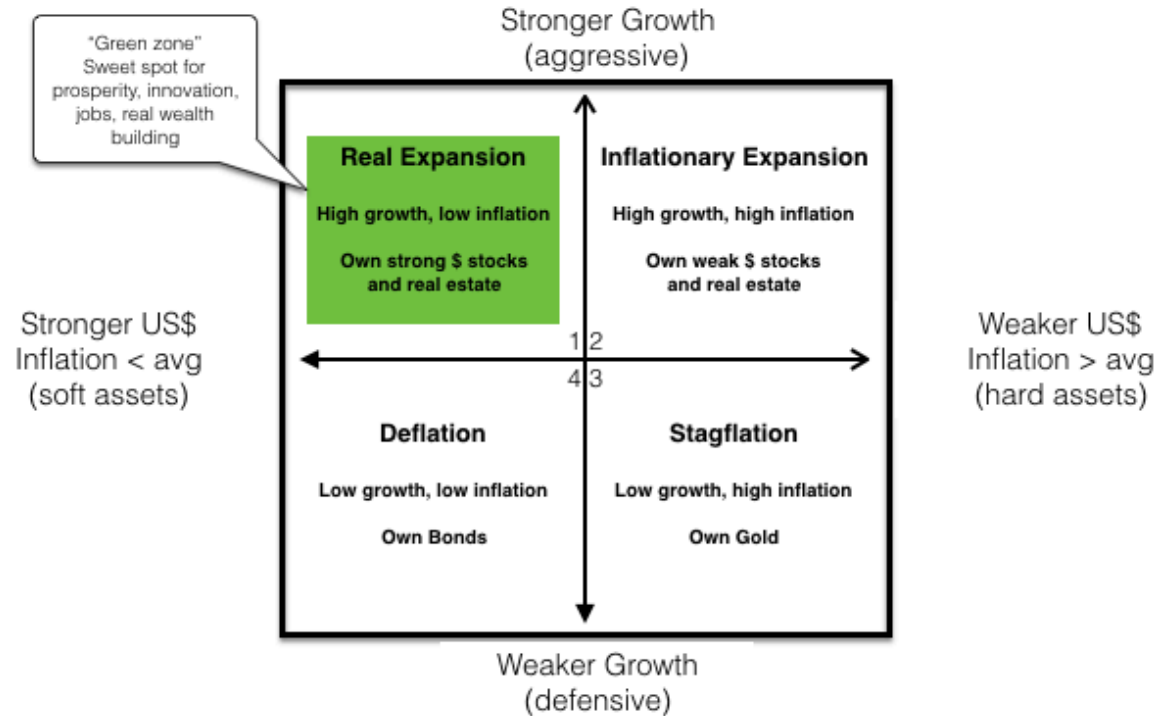
Assets in the North of the map (stocks, real estate & growth commodities) do best under rising growth expectations. Capital flows into these “aggressive” asset classes when strong growth is on the menu.

Assets in the South of the map (Bonds & Gold) do best under falling growth expectations.

Capital flows into these “defensive/safe-haven” asset classes when weak growth is on the menu.

One powerful way we view the investment universe is by monitoring the relative performance of rising growth versus falling growth asset class prices. We look for inflection points when global capital shifts from pro-growth to anti-growth or vice versa. If that capital flow is caused by a durable policy shift then portfolios need to be adjusted.

In this context, we examine the “panic” of Q42018. Remember, just a few short months ago pundits and investment professionals were declaring the definitive end to the bull market. A 2008-style repeat was assured, and the only place to hide was in the safety of cash, bonds and gold. As usual, those calls were loudest just as growth assets like stocks bottomed in late December. What few are now saying (certainly none of the gloom and doom prognosticators of



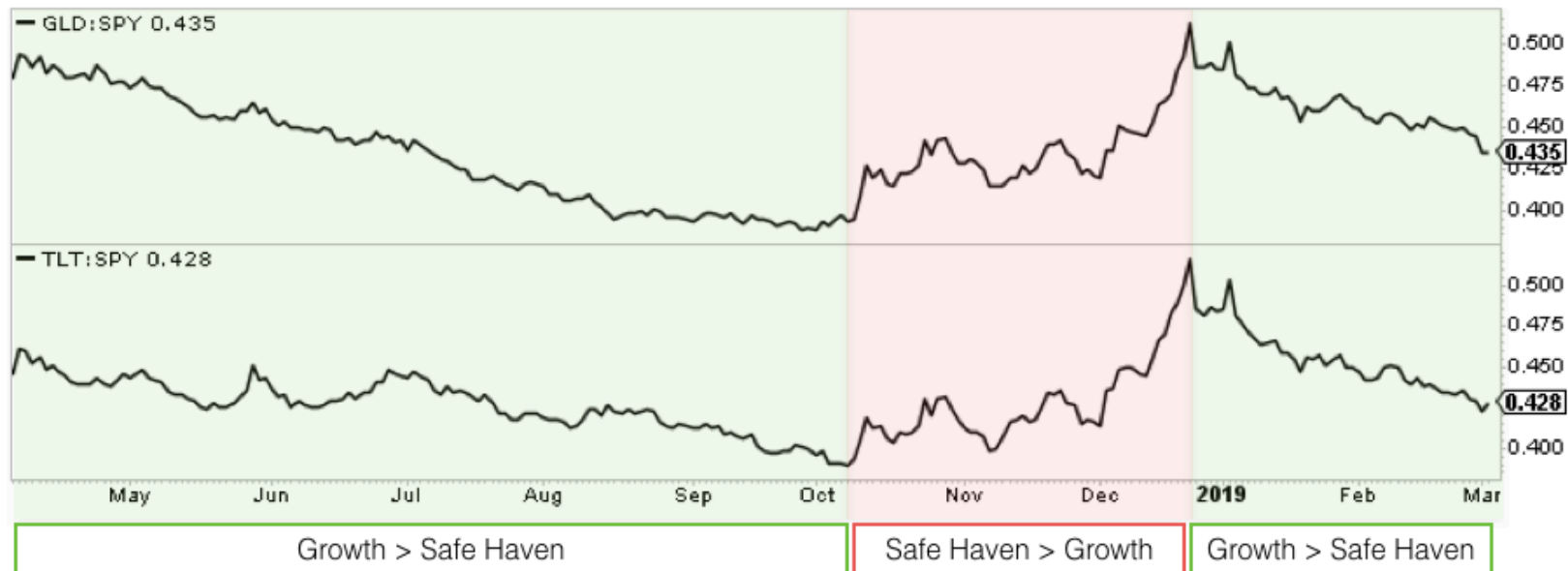
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December) is just how short lived the global capital flow into safe have assets was and how quickly the “growth trade” has resumed.

The charts below show the relative performance of both”defensive/safe-haven” assets classes (bonds & gold) versus an “aggressive/pro-growth” asset class (stocks.) From April-October 2018 stocks dominated both gold and bonds. Beginning October 4, 2018 capital reversed course. Recall, October 4th was the day Fed Chairman Powell made his arrogant comments about interest rates being far below neutral. Over the following weeks Powell continued to inject deflationary fear into markets, refusing to walk back his comments that monetary policy tightening was set in stone. But a few short months later, in late December, Powell finally caved into the reality markets were revealing. On December 24th, global capital reversed back into growth (stocks) from havens (bonds/gold). Days later on January 4th Powell attended a roundtable discussion with former chairs Greenspan and Yellen, officially walking back the deflationary language that caused the panic. Since then, with the Fed no longer blindly committed to tightening monetary policy unless the data warrant, the growth trade is back with a vengeance. Stocks have been dominating both bonds and gold since December 24th. Anyone recommending being “defensive” since Christmas Eve isn't follow the data or doesn't have a repeatable process to interrogate global capital flows. With the Fed’s deflationary mismatch threat behind us, investors should expect this trend to continue. The monetary policy scare warranting owning defensive assets was extremely short lived and has been over since Christmas Eve 2018.



ALLOCATOR

Fixed Income

Bonds are an asset class that does well in a deflationary policy environment (Low Growth & Strong Currency)

We have long said the Treasury bond bubble will pop again as it did from May2013-Jan2014 when long term Treasury bonds fell 18%. With voters choosing Trump's pro-growth agenda to ignite growth, we believe the this is even more likely. Treasury bond prices are at risk to fall 30-50%, and we expect any moves higher in bond prices (lower in yields) to be short-lived. Since most other bonds price off of Treasury yields, fixed income in general is a risky asset class.

Asset	ETF	Action Date Red Sell/Green Buy		Current Price	% Gain/Loss	Policy Notes
Investment Grade	LQD	9/9/2016	\$119.00	\$115.73	-2.7%	
Aggregate Bond	AGG	9/9/2016	\$109.00	\$106.76	-2.1%	2017 rise in Treasury bond prices (decline in yields) due to inflation expectation falling while growth expectation flat. This is a positive combination for future economic growth. Bonds remain a risky asset class that could decline 30-50% as real growth normalizes higher.
Municipal	MUB	9/9/2016	\$111.00	\$109.66	-1.2%	
TIPS	TIP	9/9/2016	\$114.00	\$110.82	-2.8%	
Extended Duration	EDV	9/9/2016	\$128.00	\$111.24	-13.1%	
US Treasury 3-7 yr	IEI	9/9/2016	\$124.00	\$121.26	-2.2%	
US Treasury 7-10 yr	IEF	9/9/2016	\$109.00	\$103.89	-4.7%	
US Treasury 20+ yr	TLT	9/9/2016	\$133.00	\$119.59	-10.1%	
International Total Bond	BNDX	9/9/2016	\$54.40	\$54.83	0.8%	
High Yield	HYG	4/12/2016	\$77.00	\$85.48	11.0%	Act more like equities than bonds, benefit from improving growth

ALLOCATOR

Commodities

A change in the price of gold is a change in the value of the currency. When gold rises, the currency's value falls and vice versa. Commodities are an asset class that does well when the currency is weak.

If growth is slowing while the currency weakens, there is stagflation. Own precious metals.

If growth is accelerating while the currency weakens, there is an inflationary expansion. Own agriculture, industrial and energy commodities.

Commodities suffered heavy losses in the strong US Dollar environment 2012-2015. In 2016 Dollar weakness was caused by election uncertainty and commodities rallied. That weak Dollar trend was reversed by Election2016. The demand for transactional and asset based Dollars will rise if Trump's pro-growth policies are implemented and fall if his policy agenda fails. Gold's recent decline back below \$1,300/oz is a confirmation of better policy and rising growth rates. Capital is beginning to leave safe haven asset classes as policy uncertainty diminishes.

Asset	ETF	Action Date Red Sell/Green Buy		Current Price	% Gain/Loss	Policy Notes
Gold	GLD	10/2/2017	\$120.77	\$121.55	0.6%	
Silver	SLV	10/2/2017	\$15.67	\$14.15	-9.7%	
Energy	DBE	8/13/2014	\$28.97	\$14.58	-49.7%	
Oil	USO	7/30/2014	\$37.00	\$11.80	-68.1%	
Agriculture	DBA	9/13/2011	\$32.50	\$16.33	-49.8%	
Broad Comm. Index	GSG	8/5/2011	\$33.00	\$15.61	-52.7%	
Base Metals	DBB	6/17/2011	\$23.00	\$16.49	-28.3%	

ALLOCATOR

Real Estate

Real Estate is an asset class that performs well when growth is accelerating. When rising growth is coupled with a strong currency, own real estate tied to business activity (like commercial REITS). When rising growth is coupled with a weak currency, own real estate tied to commodities (farmland).

Commercial RE will be helped by improving real economic growth. RE properties leveraged to businesses & economic growth are preferred under pro-growth US policies.

Asset	ETF	Action Date Red Sell/Green Buy	Current Price	% Gain/ Loss	Policy Notes	
Residential	REZ	12/21/2016	\$61.00	\$68.75	12.7%	Real estate assets have declined as higher interest rates expectations lower the perceived attractiveness of housing demand and real estate's dividend yield.
Building/Construction	ITB	12/21/2016	\$28.00	\$34.95	24.8%	
Mortgage REIT	REM	4/1/2016	\$35.00	\$43.23	23.5%	
REIT	VNQ	3/7/2016	\$75.50	\$84.11	11.4%	

ALLOCATOR

US Equity

We have been waiting for a 1980s/90s type of policy driven equity bull market for sixteen years. The 2014 midterm House/Senate/gubernatorial election shifts put us on the path as pro-growth candidates propelled the GOP to majorities. It was a repudiation of anti-growth economic policies and a big step toward a Reagan/Clinton type of equity bull market. Despite the voters' growth signal, Obama doubled down on his tax/spend/regulatory (EPA) agendas in 2015 causing stocks to be range bound and volatile. As 2016 began, policy uncertainty ahead of November's elections became the biggest threat to equities. The ebb and flow of the presidential political season moved markets in both directions as investors waited to learn which policy theme would prevail in November – growth vs. redistribution. Voters decisively made their choice in Election2016, and growth won. Trump's pro-growth policy agenda beat Hillary's anti-growth policy agenda in landslide fashion. Republicans retained control of the Senate, House and increased their control of governorships by three. The policy stage is now set for Trump and Congress to keep delivering pro-growth tax, regulatory and monetary policies. As they do, a bull market in U.S. equities will ignite to rival the 1980s/90s

US Equity - Cap Size

Asset	ETF	Action Date Red Sell/Green Buy		Current Price	% Gain/Loss	Policy Notes
Micro	IWC	7/11/2016	\$72.00	\$95.92	33.2%	Most tied to domestic policy / growth
Total Market	IWV	5/19/2016	\$117.00	\$165.35	41.3%	
Large	IWB	5/19/2016	\$111.00	\$155.58	40.2%	Large caps should underperform smaller caps as domestic economic growth accelerates
Small Cap	IJR	5/19/2016	\$54.00	\$79.65	47.5%	Most tied to domestic policy / growth
Mid Cap	IWR	4/6/2016	\$38.57	\$53.69	39.2%	More tied to domestic policy / growth

US Equity - Style

Asset	ETF	Action Date Red Sell/Green Buy		Current Price	% Gain/Loss	Policy Notes
Large Growth	IWF	7/11/2016	\$101.00	\$148.03	46.6%	Growth outperformed value in 2017 across all cap sizes. Trend will continue as tax cuts get implemented.
Small Growth	IWO	7/11/2016	\$140.00	\$199.44	42.5%	
Small Value	IWN	5/19/2016	\$92.00	\$124.03	34.8%	
Mid Growth	IWP	5/9/2016	\$90.00	\$133.59	48.4%	
Large Value	IWD	4/6/2016	\$95.00	\$123.55	30.1%	
Mid Value	IWS	4/6/2016	\$68.00	\$87.13	28.1%	

US Equity - Sector

Asset	ETF	Action Date Red Sell/Green Buy		Current Price	% Gain/Loss	Policy Notes
Staples	XLP	6/5/2017	\$57.00	\$54.15	-5.0%	Defensive sector hurt by rising growth
Utilities	XLU	6/5/2017	\$54.00	\$57.23	6.0%	Defensive sector hurt by rising growth
Metals/Mining	XME	5/8/2017	\$29.00	\$30.95	6.7%	Tied to commodity prices, hurt by strong Dollar
Energy	XLE	3/13/2017	\$69.00	\$66.57	-3.5%	Tied to commodity prices, hurt by strong Dollar
Healthcare	XLV	2/8/2017	\$71.00	\$91.69	29.1%	
Discretionary	XLY	11/14/2016	\$79.00	\$110.75	40.2%	Consumer strong w/ rising growth expectations
Financial	XLF	7/18/2016	\$19.00	\$26.52	39.6%	Helped by Trump deregulation (Dodd Frank) & rising interest rates
Materials	XLB	4/6/2016	\$44.00	\$55.23	25.5%	Global growth
Industrial	XLI	3/14/2016	\$52.00	\$76.07	46.3%	Global growth
Technology	XLK	3/7/2016	\$41.00	\$71.07	73.3%	Repatriation tax reform huge plus for tech companies

Foreign Equity

Country	ETF	Action Date	Red Sell/Green Buy	Current Price	% Gain/Loss	Policy Notes
Mexico	EWX	10/1/2018	\$51.23	\$43.06	-15.95%	Freer and fairer trade agreements are pro-growth for all parties involved
Canada	EWC	10/1/2018	\$28.78	\$27.65	-3.93%	
Denmark	EDEN	7/2/2018	\$63.89	\$62.28	-2.52%	European polices not improvng despite anti-austerity movements across the Euro Zone. Capital is fleeing. A zero trariff trade deal with the U.S. would reverse course and be very pro-growth for European economies.
Switzerland	EWL	7/2/2018	\$32.58	\$34.75	6.66%	
Netherlands	EWN	7/2/2018	\$30.51	\$29.70	-2.65%	
Sweden	EWD	7/2/2018	\$30.51	\$30.16	-1.15%	
Eurozone	EZU	7/2/2018	\$41.01	\$38.67	-5.71%	
Spain	EWP	7/2/2018	\$30.35	\$28.86	-4.91%	
Poland	EPOL	7/2/2018	\$21.78	\$23.30	6.98%	
France	EWQ	7/2/2018	\$30.52	\$29.51	-3.31%	
Germany	EWG	7/2/2018	\$29.98	\$27.37	-8.71%	
Italy	EWI	7/2/2018	\$28.89	\$27.11	-6.16%	
Austria	EWO	7/2/2018	\$22.65	\$20.20	-10.82%	
Israel	EIS	2/26/2018	\$52.41	\$54.27	3.55%	
Vietnam	VNM	10/9/2017	\$14.99	\$16.87	12.54%	Demographic leverage to US economic growth policies
Indonesia	EIDO	7/24/2017	\$26.78	\$25.86	-3.44%	Demographic leverage to US economic growth policies
Ireland	EIRL	1/26/2017	\$39.00	\$41.82	7.23%	
Singapore	EWS	1/11/2017	\$21.00	\$23.70	12.86%	
China	FXI	1/6/2017	\$35.50	\$44.42	25.13%	Strong Dollar emerging market, tied to US growth
World Ex US	VEU	11/15/2016	\$43.50	\$49.96	14.85%	Global growth reset higher after US Election2016
Norway	ENOR	8/20/2016	\$20.00	\$25.26	26.30%	
UK	EWU	8/4/2016	\$30.50	\$32.55	6.72%	Brexit was a vote for growth
Finland	EFNL	7/26/2016	\$33.00	\$39.51	19.73%	

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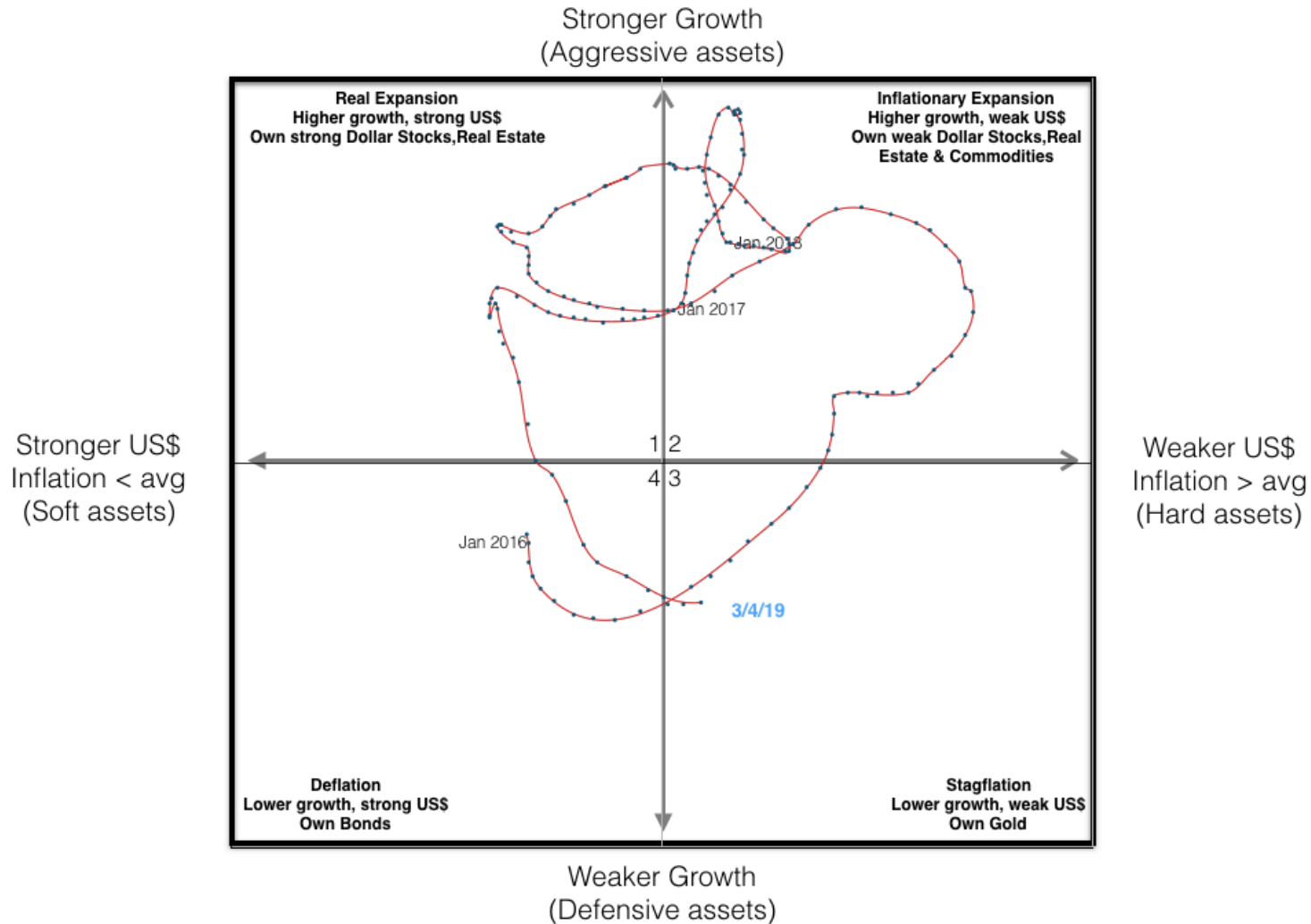
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Japan	EWJ	7/15/2016	\$47.00	\$54.35	15.64%	
South Korea	EWY	7/13/2016	\$52.00	\$62.55	20.29%	
Hong Kong	EWH	7/6/2016	\$19.00	\$25.88	36.21%	
Frontier Mkts	FRN	7/5/2016	\$10.50	\$13.58	29.33%	Highly levered to Eurozone growth movement
Peru	EPU	6/29/2016	\$30.50	\$38.75	27.05%	
South Africa	EZA	6/29/2016	\$51.00	\$52.97	3.86%	
India	EPI	6/27/2016	\$19.00	\$23.96	26.11%	Strong Dollar emerging market, tied to US growth
Taiwan	EWT	6/21/2016	\$27.00	\$33.32	23.41%	
Thailand	THD	5/20/2016	\$64.00	\$87.59	36.86%	
Belgium	EWK	3/16/2016	\$16.50	\$18.33	11.09%	
New Zealand	ENZL	3/5/2016	\$36.00	\$50.01	38.92%	
Philippines	EPHE	8/5/2015	\$37.00	\$33.23	-10.19%	
Qatar	QAT	12/1/2014	\$24.00	\$18.25	-23.96%	
Malaysia	EWM	10/3/2014	\$41.00	\$30.38	-25.90%	
Australia	EWA	9/16/2014	\$22.50	\$21.32	-5.24%	
Greece	GREK	7/14/2014	\$20.00	\$7.83	-60.85%	
Portugal	PGAL	6/4/2014	\$15.00	\$10.93	-27.12%	
Columbia	ICOL	6/27/2013	\$21.00	\$13.31	-36.64%	
Turkey	TUR	6/1/2013	\$58.00	\$27.65	-52.33%	
UAE	UAE	5/20/2013	\$23.00	\$14.48	-37.04%	
Russia	RSX	8/7/2011	\$30.00	\$19.97	-33.43%	Weak Dollar emerging market
Brazil	EWZ	7/14/2011	\$60.00	\$42.37	-29.38%	Weak Dollar emerging market
Chile	ECH	3/1/2011	\$61.00	\$44.56	-26.95%	
Egypt	EGPT	2/23/2004	\$64.00	\$32.78	-48.78%	

POLICY MAP

Growth increased versus last week (-.81 to -.80): Despite pro-growth tax and regulatory policy improvements since 2016, growth has tipped into negative territory over fears of a 2008-style, deflationary monetary policy mistake.

Value of US\$ decreased versus last week (0.10 to 0.20): Dollar had been stable between gold \$1,300-\$1,375/oz, and recently strengthened to \$1,230/oz. This strong Dollar signal gave the Fed room to pause rate hikes until economic and market data calm down.



BOND YIELD COMPONENT ANALYSIS

Nominal Yield: 2.76% (+4%) **Inflation Expectation Component: 1.96% (+3%)** **Real Growth Component: 0.80% (+8%)**

Bond market became less pessimistic about pro-growth policy outcome in 2017. After 2017 tax cut bill real growth exited the range of .30-.70 to the upside. Growth expectations are holding near 1%, while inflation expectations have drifted down over the past five years and are now below 2%. Rising growth with falling inflation is the perfect recipe for prosperity.

