Alhambra Investment Partners

Q4 2016

Review & Outlook

OCTOBER 2016

Executive Summary

- Markets are generally moving as we expected based on our outlook at the beginning of the year.
- The strength of the dollar this year has been the only surprise but it hasn't affected our expectations of a gold/commodity rally or a nascent shift to international leadership.
- US economic growth has continued to disappoint and we don't expect that to change materially.
- Inflation protected bonds are outperforming.
- The election is causing a lot of angst but the effects probably won't be long lasting. One party control though is not factored into current market prices.
- Emerging markets are outperforming but the dollar will likely need to fall for that to continue.
- The valuation bears are being vindicated by low US stock returns.
- Our model portfolios have performed very well due to gold and EM exposures.
- The Fed may hike in December but the market is saying one and done.

Review

Performance YTD (as of 9/30/16)*:

	YTD 2016
Alhambra Aggressive Allocation	**9.59%**
Alhambra Moderately Aggressive Allocation	**9.64%**
Alhambra Moderate Allocation	**8.02%**
Alhambra Moderately Conservative Allocation	**6.70%**
Conservative	**6.86%**
S&P 500	7.84%
World Stock	6.60%
US Small Cap Stocks	11.46%
MSCI EAFE	1.73%
Aggregate Bond	5.80%
Global Aggregate Bond	9.85%
US High Yield Bond	15.11%
US Corp. High Grade Bond	9.20%
DJ US Real Estate	11.01%
MSCI Emerging Mkts.	16.02%
Gold	24.20%
CRB Commodity Index	5.70%

At the beginning of the year we laid out our expectations for markets:

- US economic weakness persists, moving toward recession
- Interest rates continue to fall
- The US dollar weakens further
- Gold and other weak dollar investments outperform
- Gold stocks outperform the metal
- International stocks outperform the US

In the spring we updated the outlook:

- US economic growth continues to fall. We would not expect to see obvious recession signs before the second half of the year if then. We may well be headed for a stagnation, a la Japan, that persists but doesn't turn into a deep recession.

- Nominal interest rates could continue to fall but rising inflation expectations may mean that TIPS are the better option. We may well see a rise in nominal growth expectations coupled with a fall in real growth expectations.

- The dollar may see a short term rally from oversold conditions but the trend is down. Keep your eye on real interest rates for clues about a reversal.

- If the dollar does rally short term, gold will correct at the same time but long term momentum for gold has broken out to the upside. For those with an aggressive urge, silver is likely to outperform gold from here on.

- Gold stocks and other commodity type stocks continue to outperform but again, a short term correction should not be a surprise.

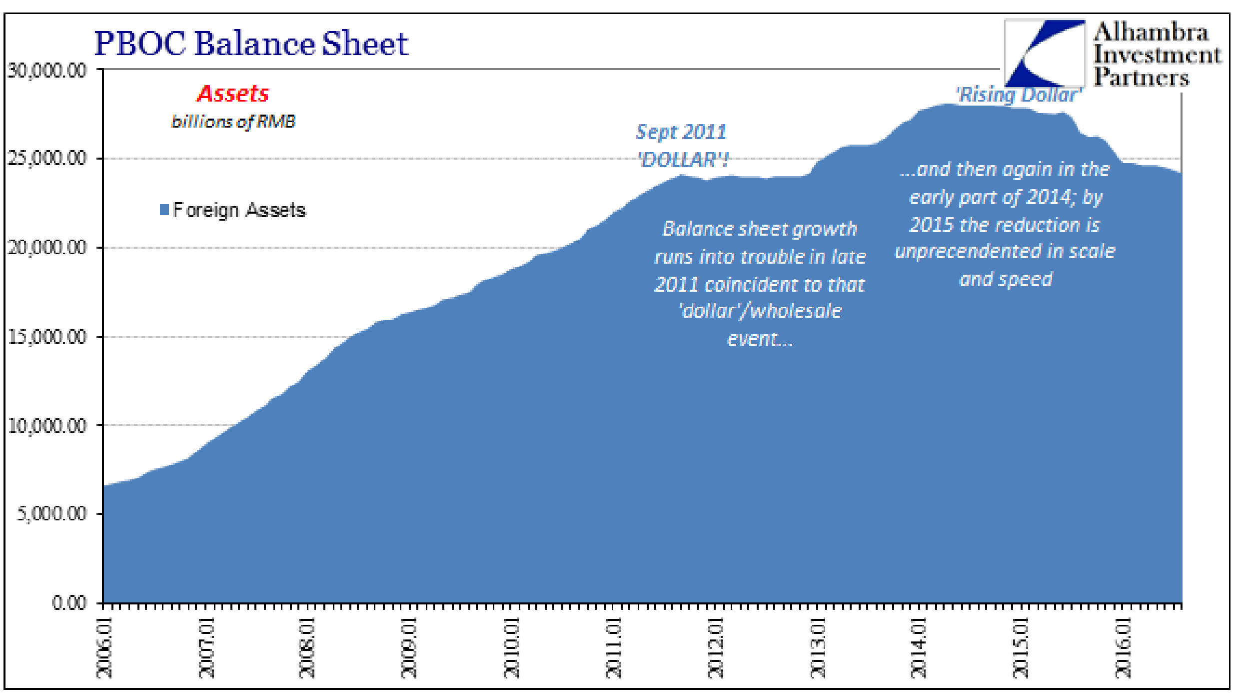
- International stock outperformance spreads from EM to developed markets. EM will likely correct at some point, again likely with any dollar rally.

Of those six original points, the only one that doesn't seem to be panning out is the dollar which is basically flat on the year and up slightly since the spring update. The rest is still on track and in some ways points to a weak dollar outcome.

- The US economy has continued to weaken on a year over year basis. The rebound in Q2 was a disappointment and Q3 is tracking under 2% as well.
- Interest rates are considerably lower than the start of the year and per the spring update, TIPS have outperformed.
- Gold has outperformed the S&P 500 by a wide margin although, as predicted, it has corrected with the rally in the dollar. I expect the dollar to peak soon and gold to resume its uptrend.

- Gold stocks and commodity type stocks – particularly oil stocks – have outperformed. In addition, long term commodity index momentum has turned positive bolstering the trend. The only thing that could derail this move is a further rally in the dollar.
- EM is still outperforming but EFA has outperformed the S&P since late June. EM stocks did correct some with the rising dollar but not much.

We see no reason to change the outlook unless the dollar continues to move higher. The risk of that is not insignificant and is to some degree something over which the Fed has little control. The Chinese have been attempting a controlled devaluation of their currency for well over a year. The market turmoil in August of 2015 was driven by a Yuan devaluation that appeared to be getting out of control. Their ability to control that process is constrained by their rapidly dwindling foreign reserves and there is certainly the possibility of another disruptive move in the Yuan that drives the dollar higher. And a rising dollar has the same effect as tightening monetary policy except the Fed would in that case have no control over the rate of change. Jeff Snider monitors those markets for us and hopefully we'll get some warning if the Chinese start to lose control of the process. For now, we do not expect the dollar rally to move beyond the previous high.



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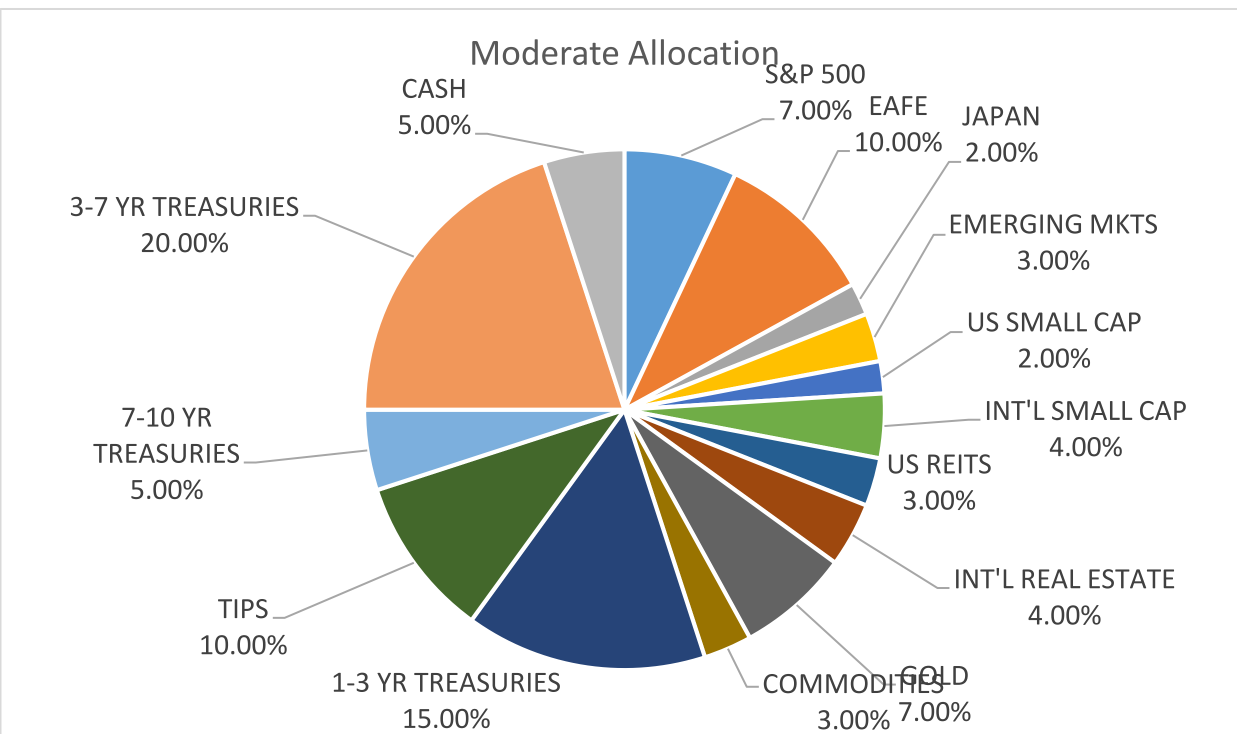
As I’ve mentioned before we use a four box matrix in our investment process:

Rising dollar, rising growth	Rising dollar, falling growth
Falling dollar, rising growth	Falling dollar, falling growth

We have tried to identify assets that perform well under each set of conditions. We believe we are moving toward the southeast quadrant of falling growth and a falling dollar. We know what assets have performed well in that environment in the past but each period is unique. There is a difference, for instance, between falling growth and recession. If the US is able to continue to grow, even at a slowing rate, we could easily see foreign stocks extend their recent outperformance. The same is true of the general commodity indices and gold. But if falling growth turns into US recession then we’ll have to adjust. The US is still the dog that wags the tail of the global economy.

Our Moderate Risk Allocation reflects our outlook:

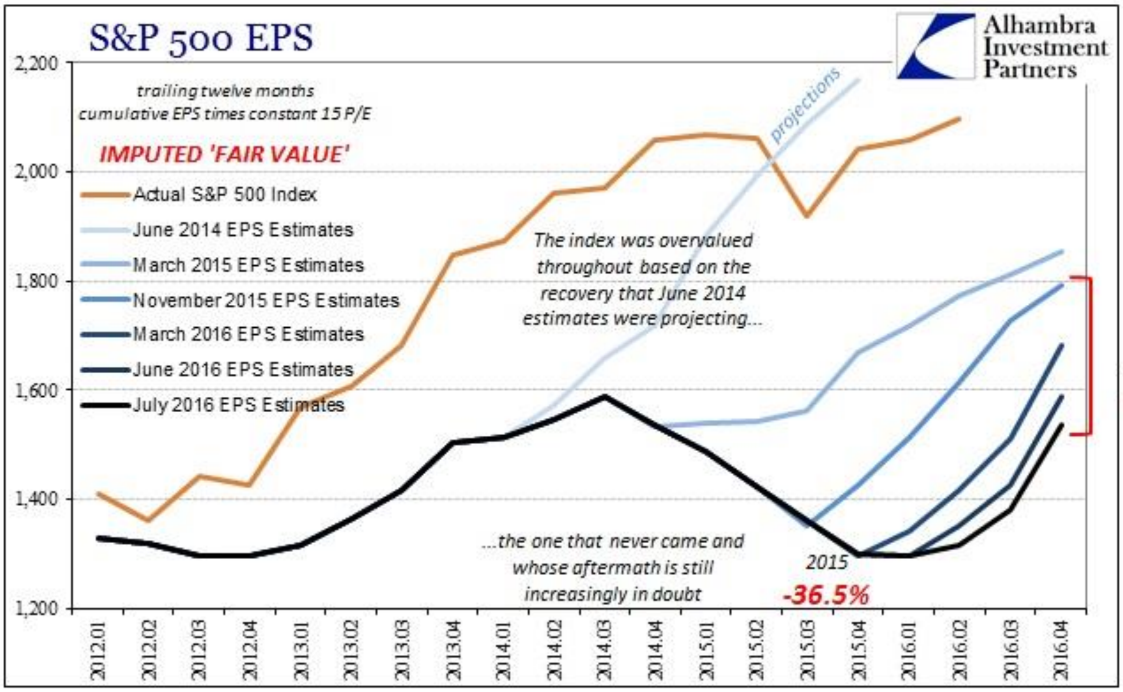


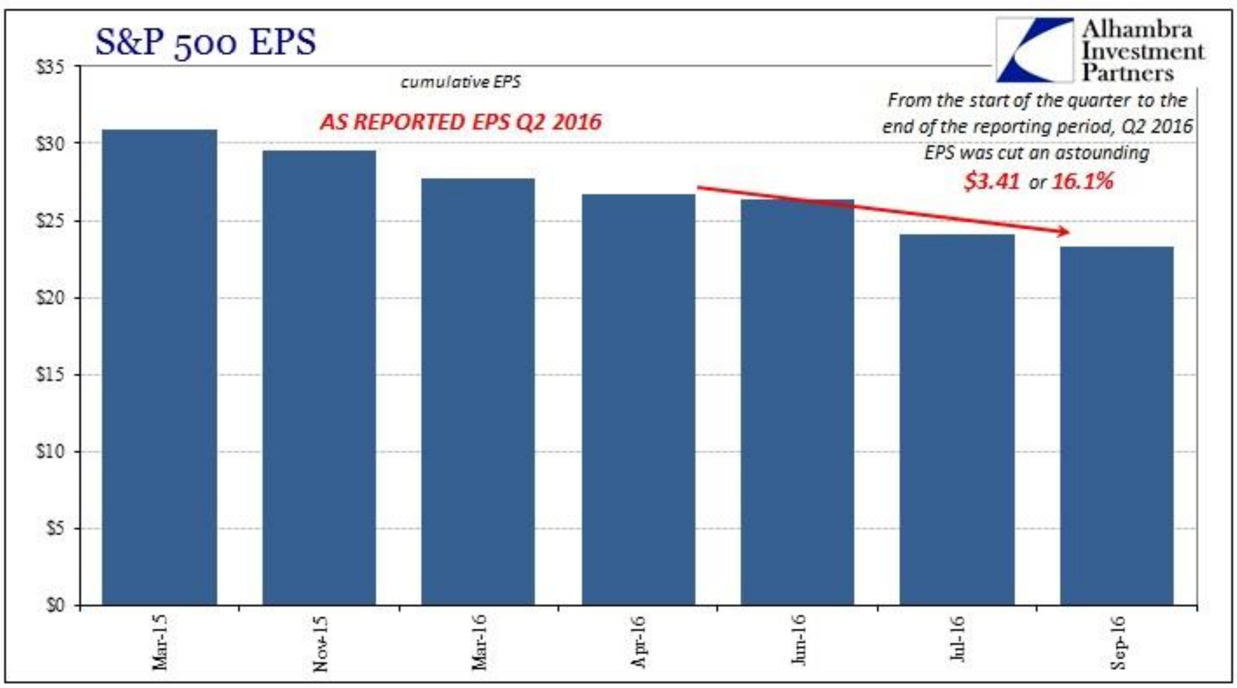
Just looking at the performance review above one might conclude that the last year has been a pretty easy time for investors, a conclusion that is based on some calendar quirks (and would likely be disputed by anyone tasked with navigating the market). The stock market sold off last August and September so the 1 year numbers are measuring from the low of that year to basically the high this year. Look at a longer time frame and the true picture emerges. The S&P 500 is up just about 4% annually since the end of 2014 so we're closing in on 2 years of minimal gain. And while it has been a good year for global stocks and bonds, it has been a more volatile ride than more recent years. The S&P 500 has suffered three significant drops since the fall of 2014, one of nearly 10% and two others that cracked double digits.

Momentum Shifts

The US stock market has been leading the pack basically since the 2008 crisis but there are some signs that might be ending and not surprisingly we might add. The last few years it has been fashionable to make fun of those of us who cited valuation as a risk factor. A plethora of articles were written about why the Shiller P/E or any other metric cited as showing an overvalued market were wrong, a new century version of "it's different this time". Ridicule was heaped on those investment Malthusians who had the temerity to point out that there was a finite amount of future returns that could be brought forward, a limit to multiple expansion. The idea that profit margins were mean reverting was disputed, a new era of permanently high profits proclaimed, Irving Fisher resurrected.

Well, it turns out the valuation bears – and you can certainly include Alhambra in that group - had a point. Profit margins have peaked and started to come down, earnings contracting for well over a year now. We have had some multiple expansion but due to falling earnings rather than rising stock prices. More importantly, returns have stagnated while volatility has picked up. The valuation argument was, all along, that high valuations today imply - indeed demand, unless something very fundamental has changed – lower returns in the future. Most who argued caution in the face of high valuations have stressed repeatedly – to deaf ears apparently – that we have no idea the future path of those returns. Of course, past experience says that it is more likely to be a bumpy ride than a smooth one but the gradual incline – or decline - is certainly within the realm of possibility.



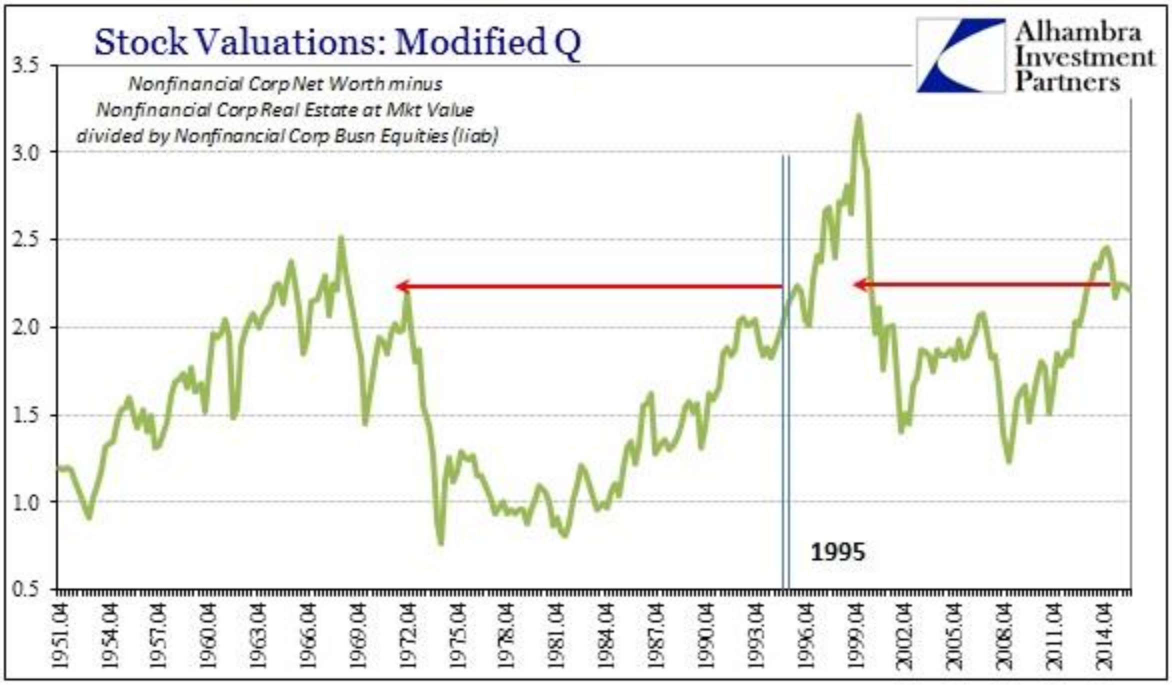


It is also interesting, from a fractal point of view, to consider the much longer term secular bear market within which we think we still reside. The returns since the valuation peak of 2000 are a mere 2.5% annually which most people would agree is pretty puny when one considers the two 50%+ bear markets one had to endure to make it. Returns since the valuation peak of 2007 are slightly better at about 4.5% but achieving that return required navigating through the crash of 2008 without wavering in one's commitment to the market. Measuring from trough to peak gives a different picture of course. From 2003 to 2007 the S&P 500 returned a little over 10% annually. From 2009 to today the market has delivered about 12.5% per year. But returns are slowing over the last few years. The 3 year return is down to 7%. Since mid-2014 the return is 5% and since the beginning of 2015, 4.4%.

The valuation argument has always been about risk. Are those puny predicted future returns worth the risk one has to incur to achieve them? If one asks that question today it seems hard to answer, especially with the 10 year Treasury, the risk free alternative over the next 10 years, yielding a mere 1.75%. But we can certainly answer the question retroactively; we know what happened from 2000 to today and from 2007 to today. Since 2000 the 10 year Treasury has returned 4.1% per year, higher than the return of the S&P 500 over the same period. Obviously, the risk incurred by owning stocks was not rewarded. From November 2007 to today the 10 year Treasury has returned 3.9% annually, only slightly less than the 4.5% of the stock market with no crashes along the way.

Recent history also favors the Treasury. Since mid-2014 the 10 year Treasury has returned 5.7% annualized versus the 5% of stocks with no double digit drawdowns to worry you into selling. And since the beginning of 2015 the 10 year has returned 3.3%, 75% of the S&P 500 return with a fraction of the volatility.

And so today we are faced with the same question. Are future returns high enough to justify owning a full allocation of stocks? With valuations near their peak for this cycle (depending on what metric you use), expected future returns are low. Estimates of forward 10 year real returns, depending on methodology and metric, range from negative single digits to low positive single digits. In other words, not significantly different than one can achieve by purchasing a 10 year TIP with a real yield of 0.13%. And the TIP is essentially riskless over that time frame.

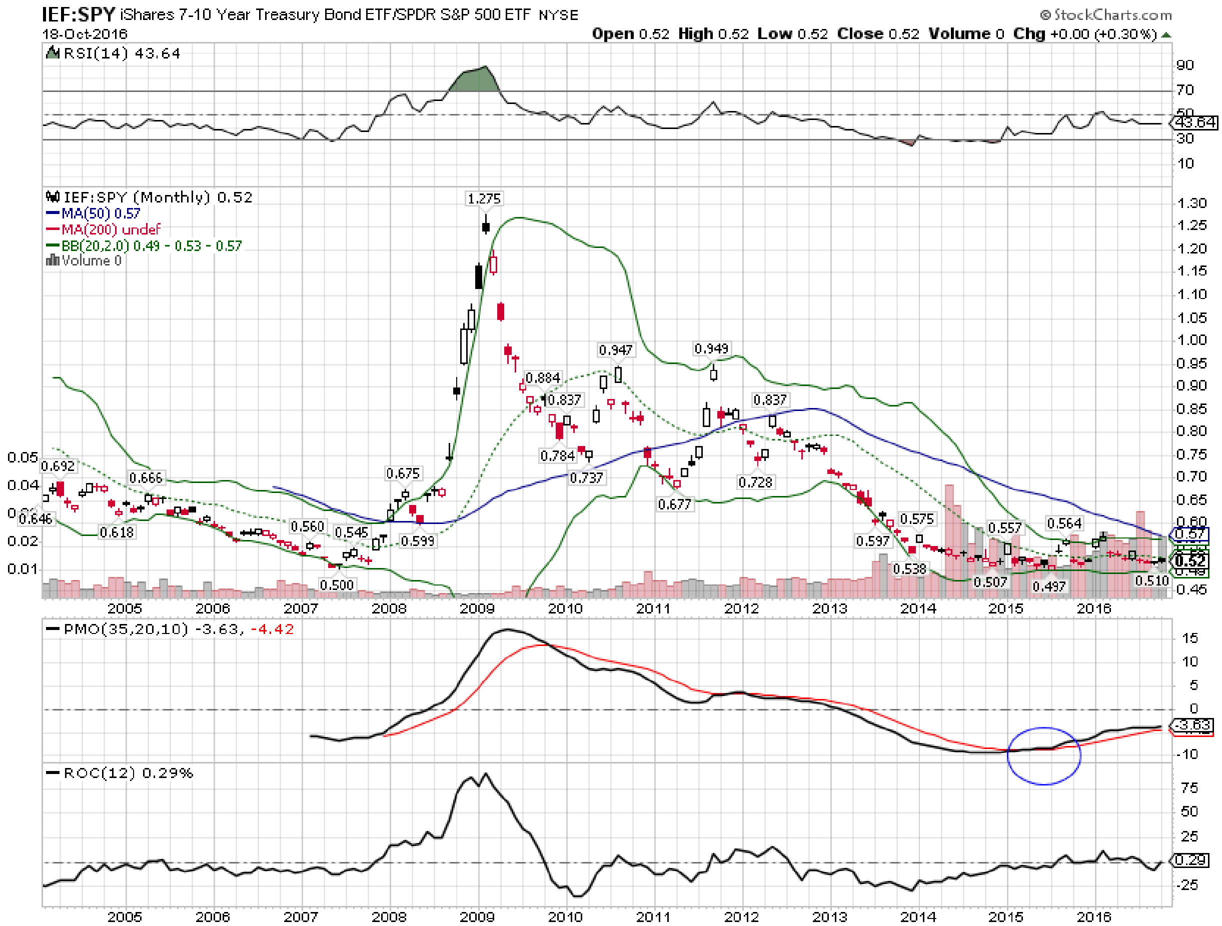


Our answer for the last couple of years to the valuation question posed above has been no and we've adjusted our asset allocation accordingly. That doesn't mean, as so many of the bulls seem to think, that we own no stocks. We are not so arrogant that we place a 100% probability on the low returns predicted by high valuations. Sure things are no more likely in the market than at the track. What it does mean is that we have reduced our stock allocation to reflect the risk of holding stocks at high valuations. At the same time, we've raised our allocation to bonds and other non-US stock assets. As you can see from the chart of recent returns, moving away from US stocks is starting to pay dividends. Gold and commodities are producing positive returns for the first time in years. Stocks outside the US are starting to outperform with EM leading the way.

We don't know yet whether these short term shifts will be sustained, if the dominance of US stocks is coming to an end. But there have been some long term momentum shifts recently that point in that direction. Long term momentum shifts don't happen very often so we pay attention when they do.

The first is gold which has strongly outperformed the S&P 500 this year:

Another long term momentum shift occurred in mid-2015. Momentum shifted to Treasuries (the 7-10 year ETF) last year and that momentum has carried over to this year.



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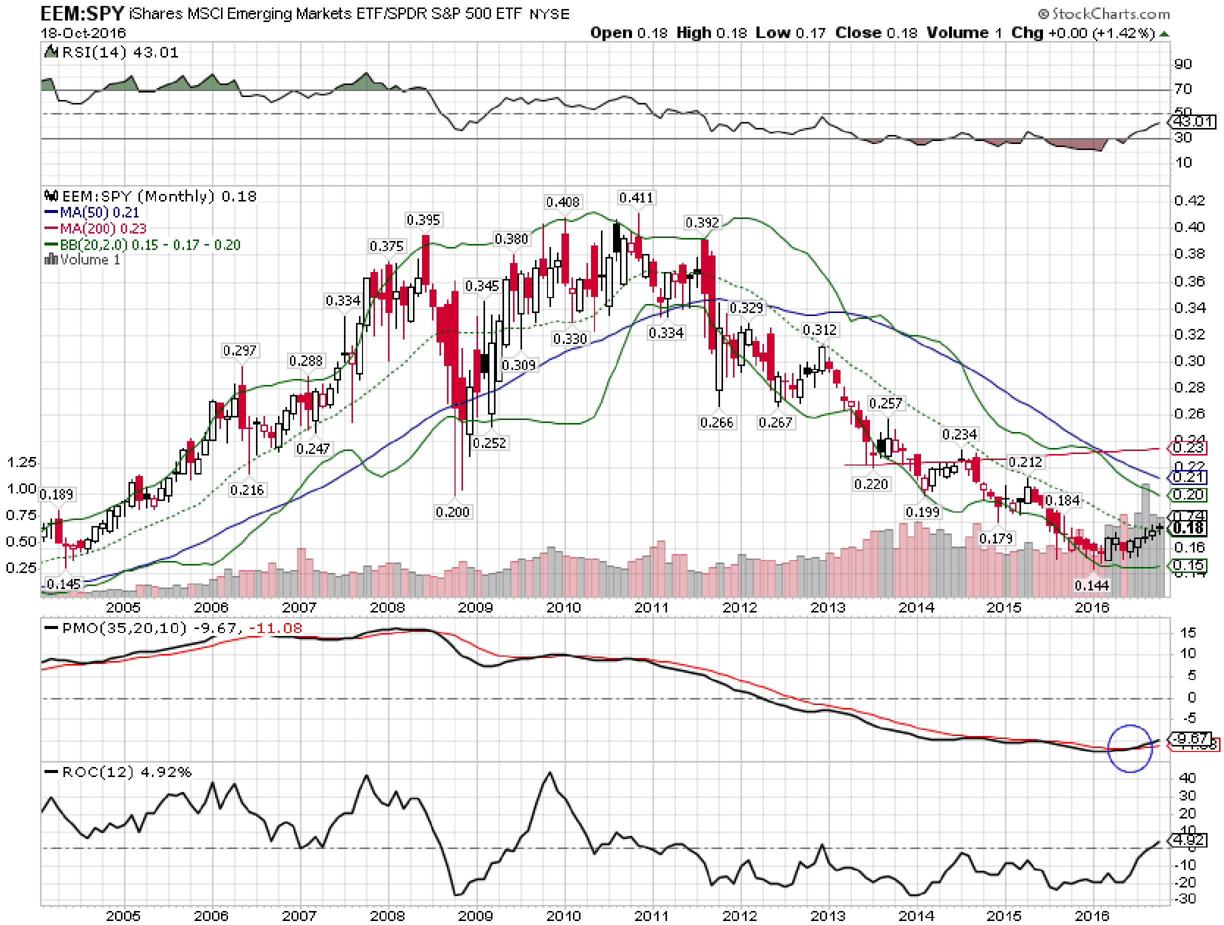
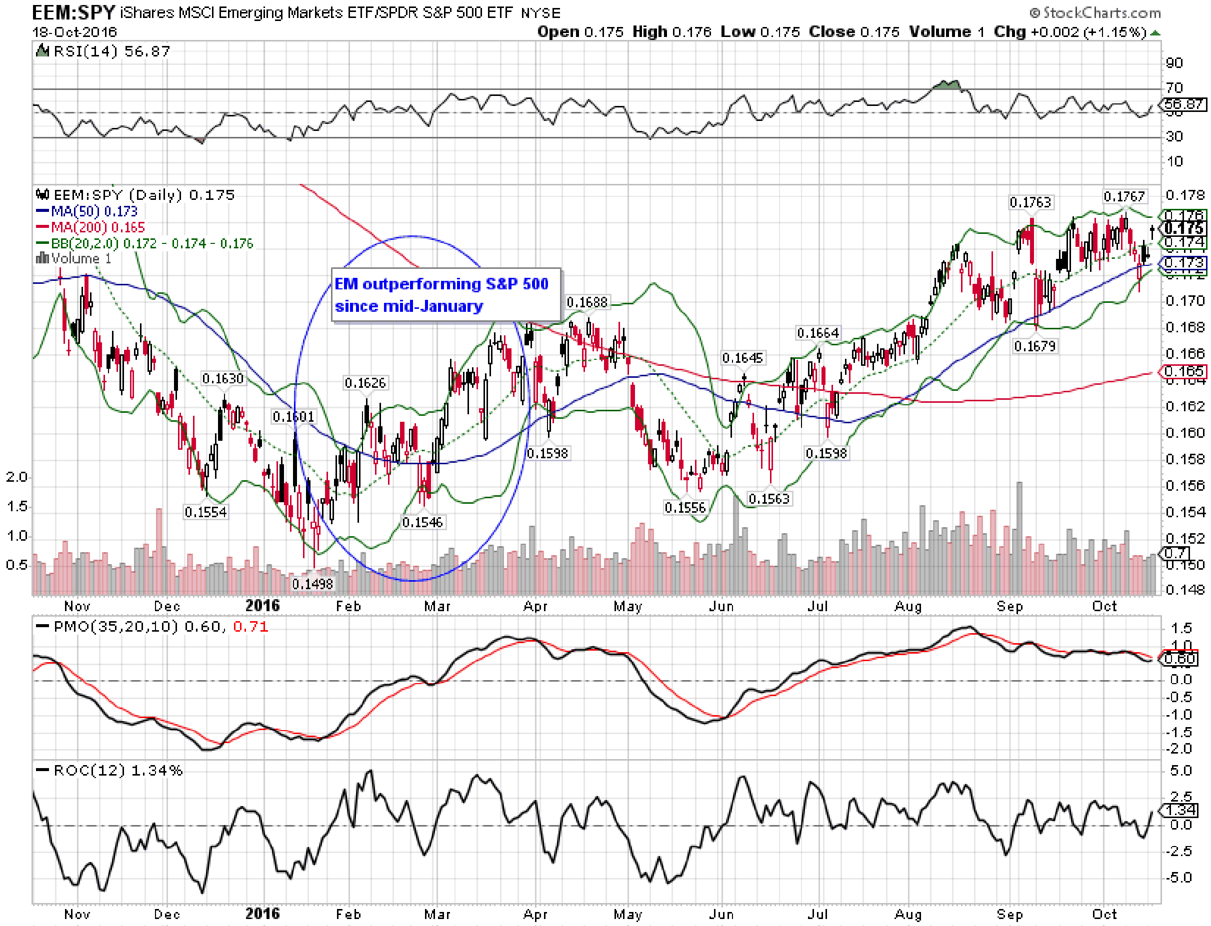
A long term shift to non-US stocks also started this year with Emerging Markets leading:



You can see that more clearly on the daily chart:



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The latest long term momentum shift is to the general commodity index from the S&P 500:

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Perhaps the most important – or potentially most important – change in momentum came in the US dollar index earlier this year. Indeed if the other shifts are to be anything more than short term events, the dollar will likely have to fall. Instances of international stock and commodity outperformance during rising dollar periods are rare indeed. If the dollar's recent strength is extended, momentum shifting once again to favoring a stronger dollar, the other trends will likely prove short lived.

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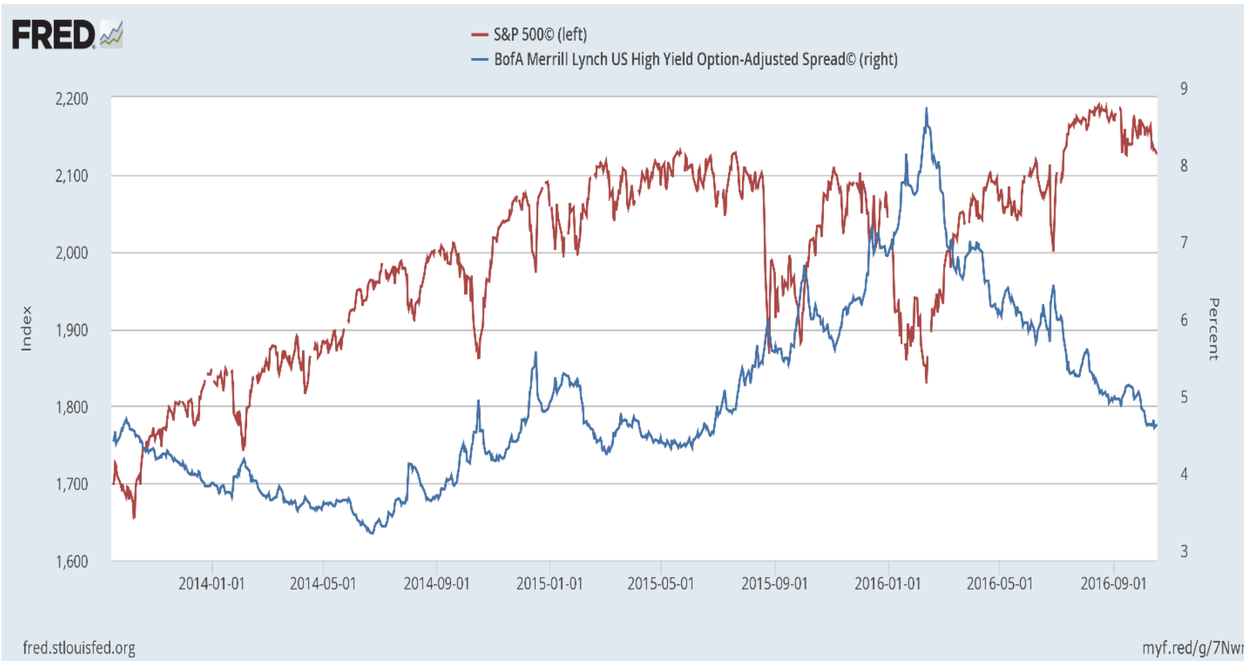
The other major event this year so far is the return to favor of high yield – junk – bonds, up 15% this year so far. The corrections we've seen the last couple of years have been accompanied by a widening of credit spreads as junk bonds were sold and Treasuries bought. The reversal this year has seen the opposite effect with stocks rising strongly out of the February lows in lock step with narrowing credit spreads.



The widening of spreads was blamed on falling oil prices and the subsequent impact on the fracking industry. As oil prices have moved back higher, credit spreads have responded positively. It will be interesting to see if this trend is extended back to the lowest spreads of the cycle. The credit cycle is turning with delinquencies and defaults rising, not all of it energy related. If the economy remains weak, it seems more likely that spreads will widen again at some point. Indeed, history says that spreads will lead the way, widening before we reach the recession point.

One last potentially significant observation in the bond market. TIPS have outperformed nominal bonds this year and long term momentum has shifted in favor of inflation protected bonds. That is a phenomenon normally associated with the late part of the business cycle. It is also consistent with rising concern about inflation another market indicator that points to a weaker dollar.

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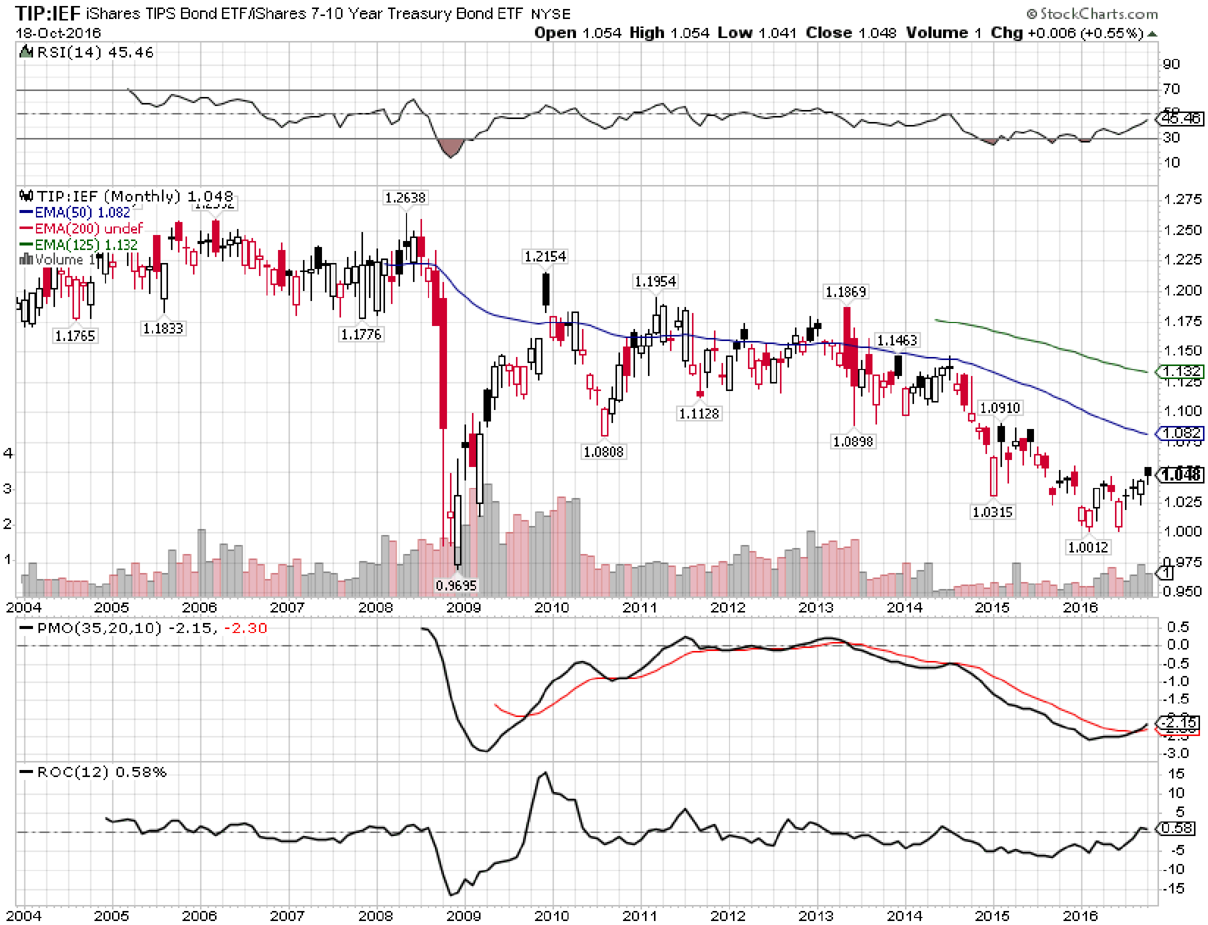


Political Observations

We really hate to do it, but we're going to have to talk about politics for a moment. We will have an election in a few weeks and there could be a major impact on markets. *Could* because, in general, the impact of elections is short term. Politicians rarely are able to enact the agenda on which they ran so analysis of their proposals is basically a waste of time for an investor. There are rare times when big changes do have big market impacts and long lasting economic effects. We don't think this is one of those times.

The election will though likely be a primary driver of volatility in the very short term. There are any number of surprises that could roil the market, a Trump win being only one. The consensus at this point seems to be a Clinton win and split Congress with Democrats taking the Senate and Republicans the House. Any outcome other than that one will probably produce some angst and volatility.

There is a fairly widespread expectation that the new President – whoever it is – will propose and Congress will pass a large fiscal package centered on infrastructure (however that might be defined). But is that realistic? We don't think so. If President Obama couldn't get a large fiscal package through a Republican Congress what makes anyone think Hillary Clinton will? As for Trump, his scorched earth march through the Republican party has certainly not won him any friends or influence. As for the economic impact of any fiscal package that might depend on the form it takes but unless it is radical probably not. You may not have noticed – the economy certainly hasn't – but a $305 billion infrastructure spending package was signed by President Obama in December of last year. No word as to whether any shovels have hit the ground yet. I would also point out that the budget deficit is rising again along with interest rates and a blow-out fiscal package might not be looked upon favorably by bond markets. One last item of note: there is no discernible correlation between government spending or deficits and stock market returns. None. Zero. Nada.

So don't spend a lot of time thinking about the election in relation to your investments. As a citizen, sure, take it seriously and if the Presidential selections are as disappointing to you as they are to us, spend your time analyzing the down ballot items. Those are probably more important and will have a bigger impact on your life than what happens at the top of the ticket.

Economic Situation

Economic Scorecard

Economic Growth & Investment	Prior	Consensus	Actual	YOY % Change
Industrial Production	-0.5%	0.2%	0.1%	-1.03%
Manufacturing	-0.5%	0.1%	0.2%	
Capacity Utilization	75.3%	75.6%	75.4%	-1.3%
Chicago Fed Nat'l Activity Index	0.24	0.15	-0.55	
Existing Home Sales	5.38M	5.44M	5.33M	0.80%
Personal Income	0.4%	0.2%	0.2%	3.12%
GDP	1.1%	1.3%	1.4%	1.28%
Leading Economic Indicators	0.5%	0.1%	-0.2%	

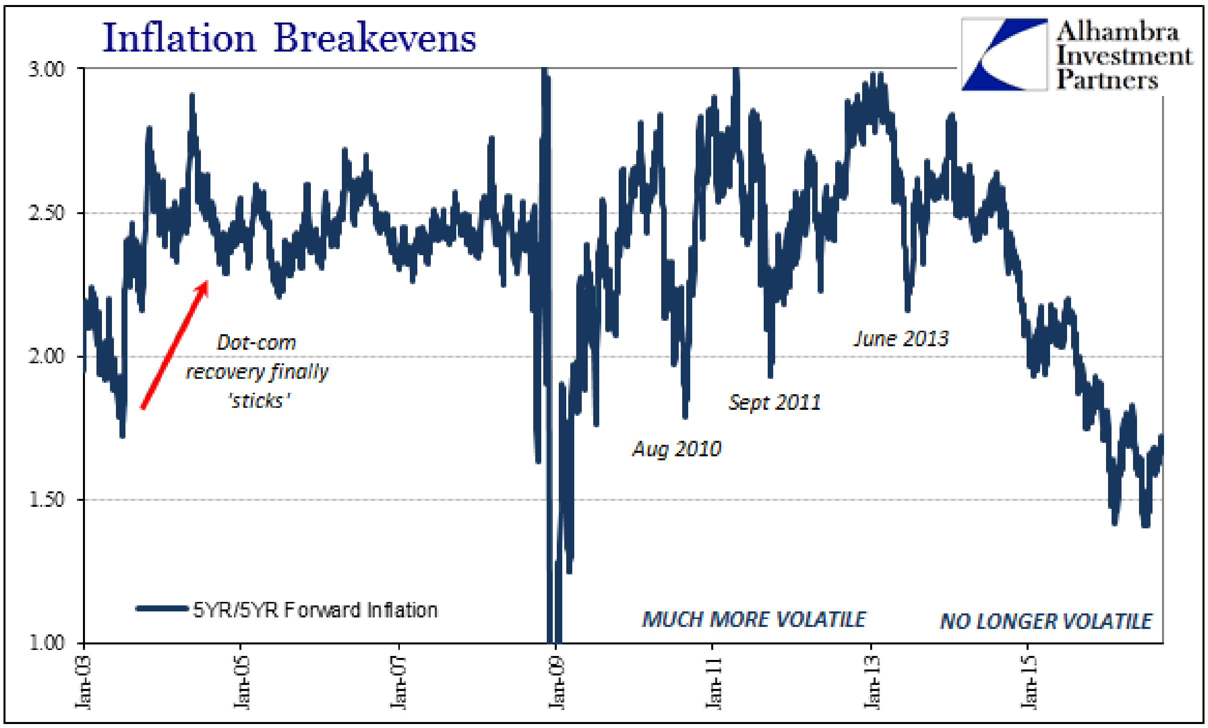
Corporate Profits	-2.2%		-1.7%	-1.66%
Non-Farm Productivity	-0.5%	-0.6%	-0.6%	-0.42%
Personal Saving Rate	5.6%		5.7%	-3.39%
Disposable Personal Income	0.4%		0.2%	3.36%
Quarterly Services Survey	1.4%		-0.1%	3.80%
Production				
Empire State Mfg Survey	-1.99	1.00	-6.80	
Philly Fed Survey	2.0	2.0	12.8	
ISM Non-Mfg Survey	51.4	52.9	57.1	
ISM Manufacturing Index	49.4	50.2	51.5	
Chicago PMI	51.5	52	54.2	
Dallas Fed Mfg Index	-6.2		-3.7	
Richmond Fed Mfg Index	-11		-8	
Kansas City Fed Mfg Index	-4		6	
Consumption & Distribution				
Retail Sales	-0.2%	0.6%	0.6%	2.67%
Less Autos	-0.2%	0.5%	0.5%	2.72%
Less Autos & Gas	0.0%	0.3%	0.3%	
E-Commerce Retail Sales	4.0%		4.5%	15.18%
Wholesale Sales			0.5%	-2.50%
Motor Vehicle Sales	16.693M		16.91	-3.78%
Domestic Vehicle Sales	14.2M		14.1M	
Consumer Spending	0.4%	0.2%	0.0%	3.62%
Inventories				
Business Inventories	0.0%	0.1%	0.2%	0.70%
Inventory/Sales			1.39	0.72%
Wholesale Inventories	-0.1%		-0.2%	0.50%
Inventory/Sales			1.33	1.52%
Orders				
Factory Orders	1.4%	-0.2%	0.2%	-1.6%
Durable Goods	3.6%	-1.9%	0.0%	-1.3%
Ex-Transportation	1.1%	-0.5%	-0.4%	-1.1%
Core Capital Goods	0.8%		0.6%	-3.1%
Trade				
Trade Balance	$-39.5B	$-39.0B	$-40.7B	-8.77%
Exports			0.8%	0.7%

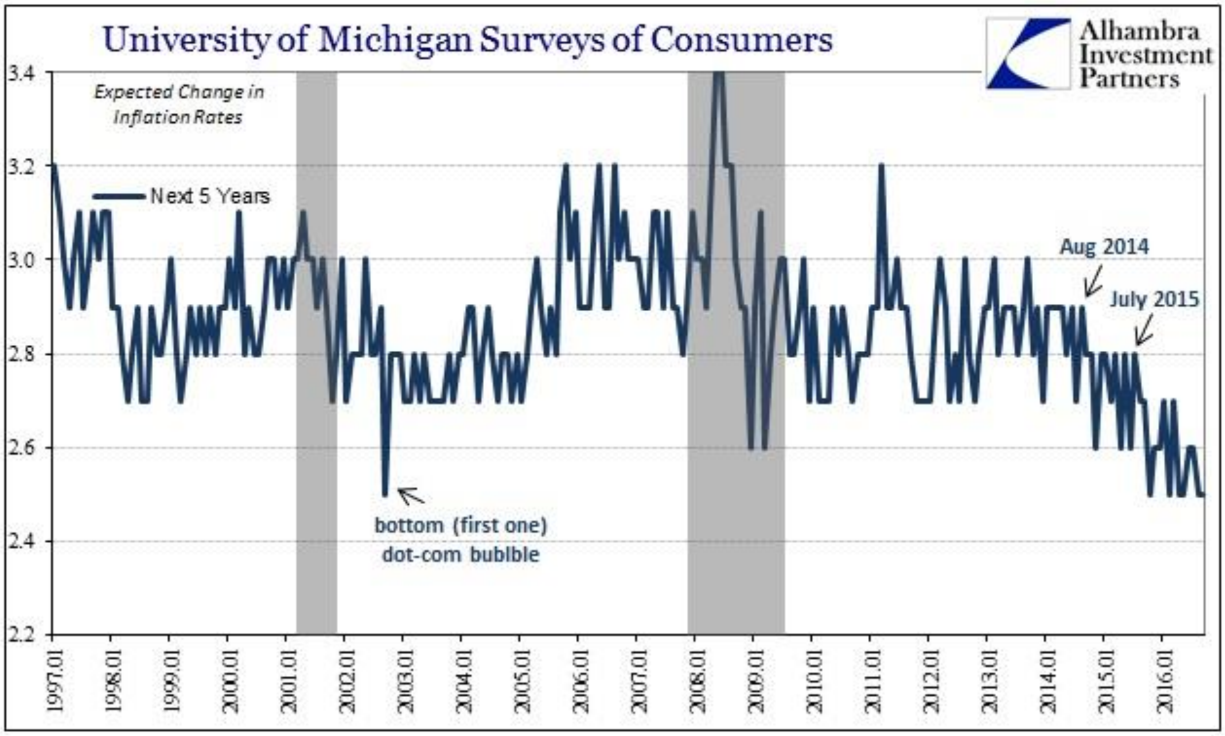
Imports			1.2%	-1.2%
Trade in Goods	$-58.8B	$-62.3B	$-58.4B	
Exports	3.00%		0.70%	
Imports	-1.00%		0.30%	
Inflation				
CPI	0.2%	0.3%	0.3%	1.5%
less food & energy	0.3%	0.2%	0.1%	2.2%
PPI	0.0%	0.2%	0.3%	0.7%
less food & energy	0.1%	0.1%	0.2%	1.2%
GDP Price Index	2.3%	2.3%	2.3%	1.2%
Import Prices	-0.2%	0.1%	0.1%	-1.1%
Export Prices	-0.8%	0.1%	0.3%	-1.5%
Employment Cost Index	0.6%	0.6%	0.6%	2.3%
Unit Labor Costs	2.0%	2.1%	4.3%	2.6%
PCE Price Index	0.0%	0.2%	0.1%	1.0%
PCE Core	0.1%	0.2%	0.2%	1.7%
FHFA House Price Index	0.3%	0.4%	0.5%	5.8%
Case Shiller HPI	-0.1%	0.1%	0.0%	5.0%
Farm Prices	-0.7%		3.9%	-6.4%
Employment				
New Jobless Claims	246K	254K	246K	-6.11%
Job Openings	5.831M		5.443M	2.54%
Labor Market Conditions Index	-1.3		-2.20	
Non Farm Payrolls	167K	168K	156K	1.72%
Private Payrolls	144K	170K	167K	1.91%
Unemployment Rate	4.9%	4.9%	5.0%	
Participation Rate	62.8%		62.9%	
Avg Hourly Earnings	0.1%	0.3%	0.2%	2.6%
Avg Workweek	34.3	34.4	34.4	-0.3%
Challenger Job Cuts Report	32188		44324	-24.72%
ADP Employment	175K	170K	154K	1.90%
Construction				
Housing Market Index	65	63	63	3.2%
Housing Starts	1.212M	1.190M	1.142M	0.88%
Housing Permits	1.144M	1.167M	1.139M	-2.32%
Construction Spending	-0.3%	0.3%	-0.7%	-0.30%
New Home Sales	659K	598K	609K	20.59%
Other				
Consumer Sentiment U of Mich.	91.2	92	87.9	

NFIB Small Business Optimism	94.4	95	94.1
Consumer Confidence Conference Bd.	101.8	98.8	104.1

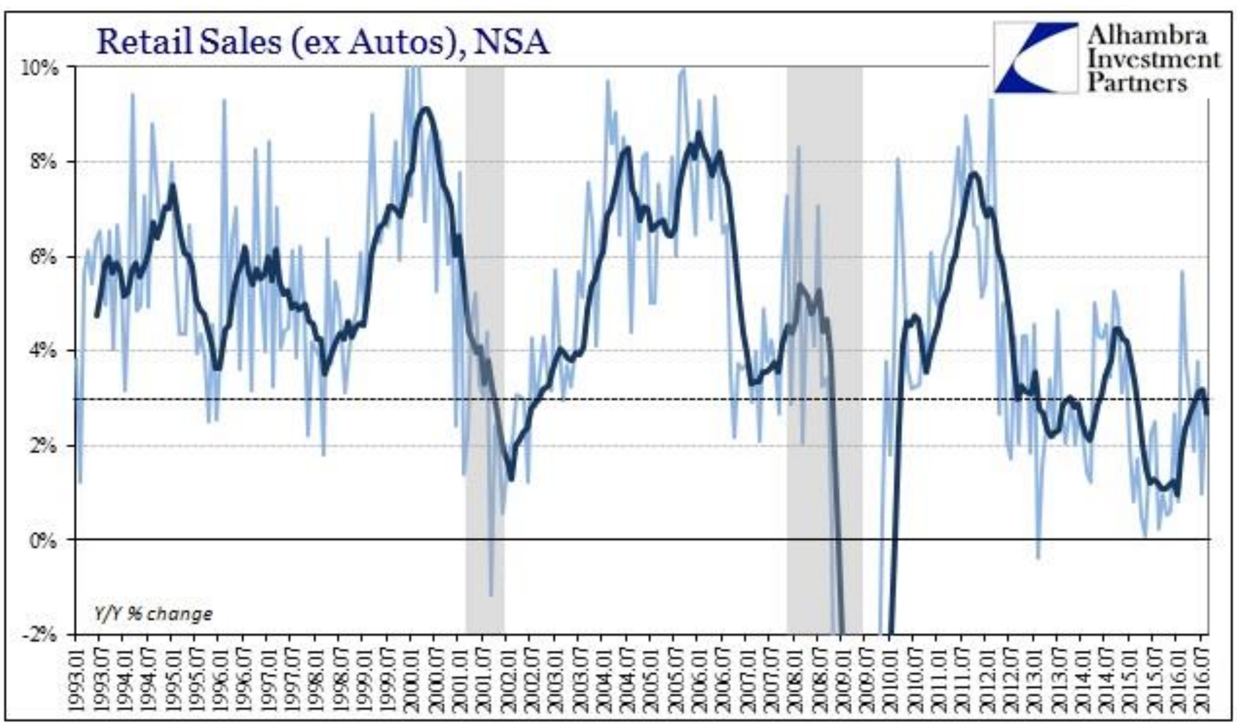
Selected Economic Charts

Inflation expectations are falling long term but have recently perked up.





Consumption is still growing but at rates well below previous expansions.



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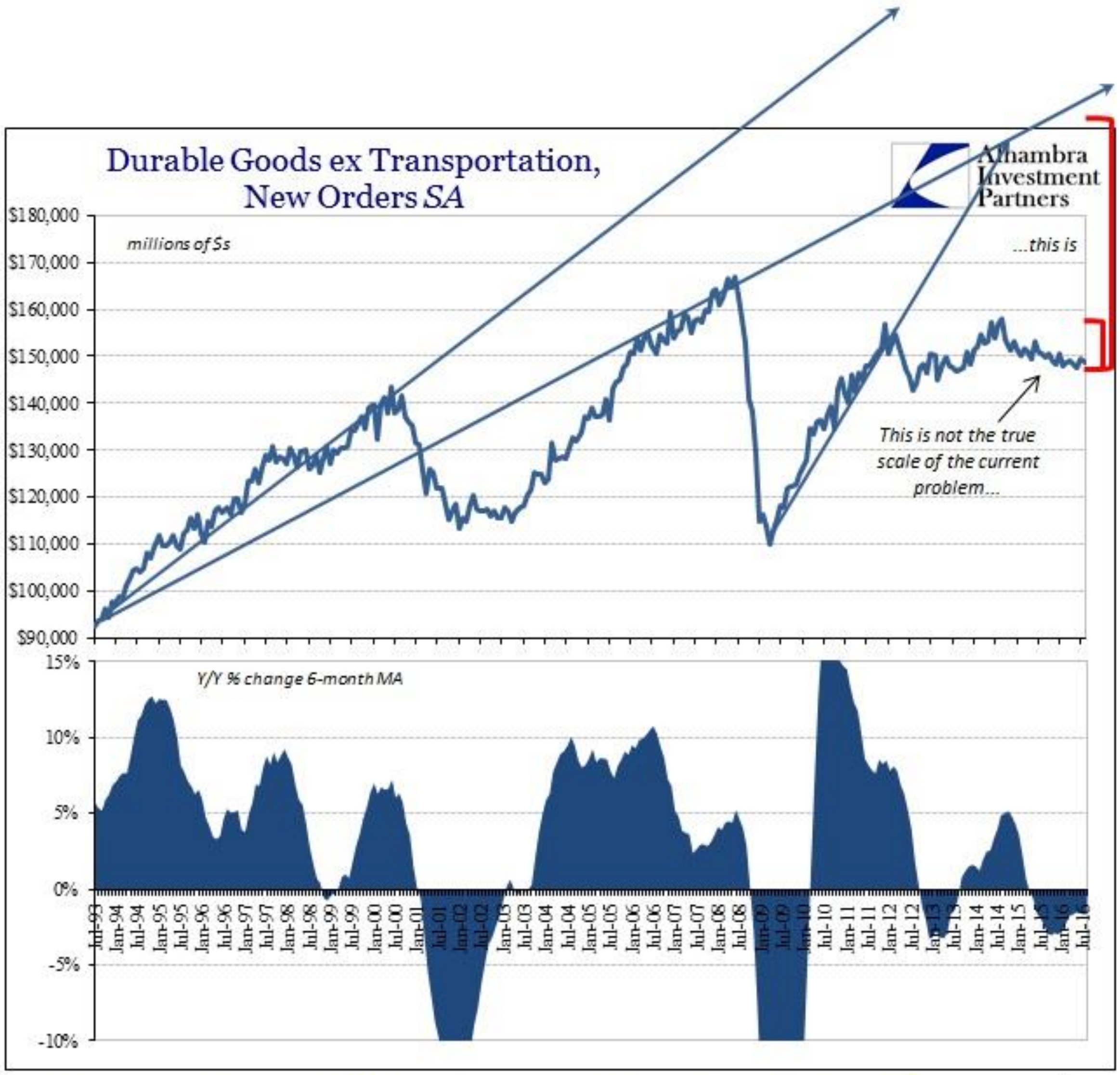
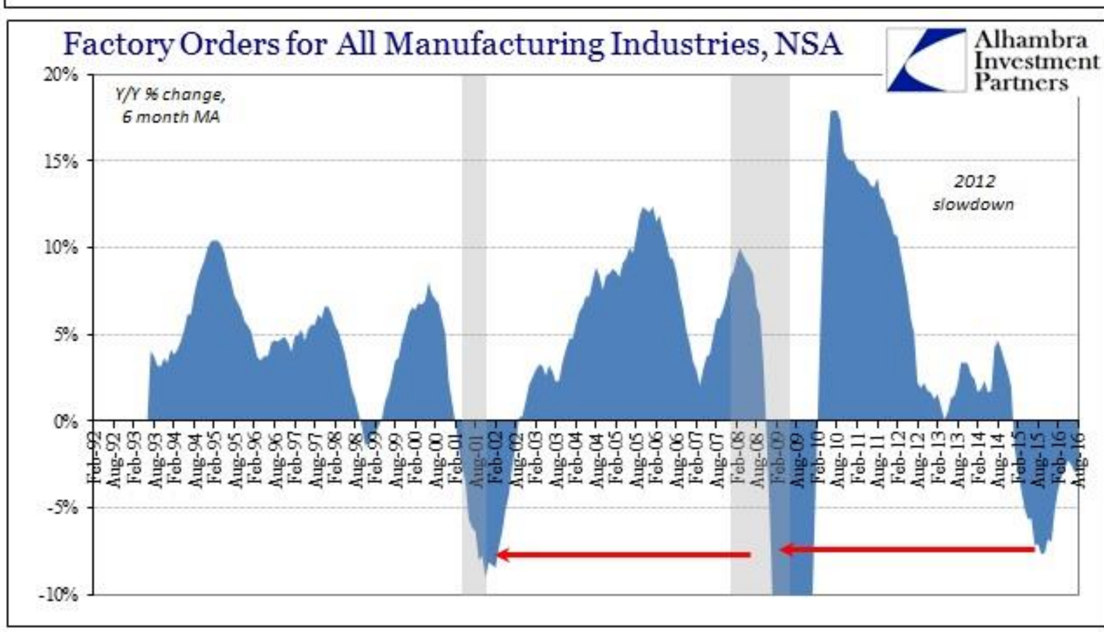
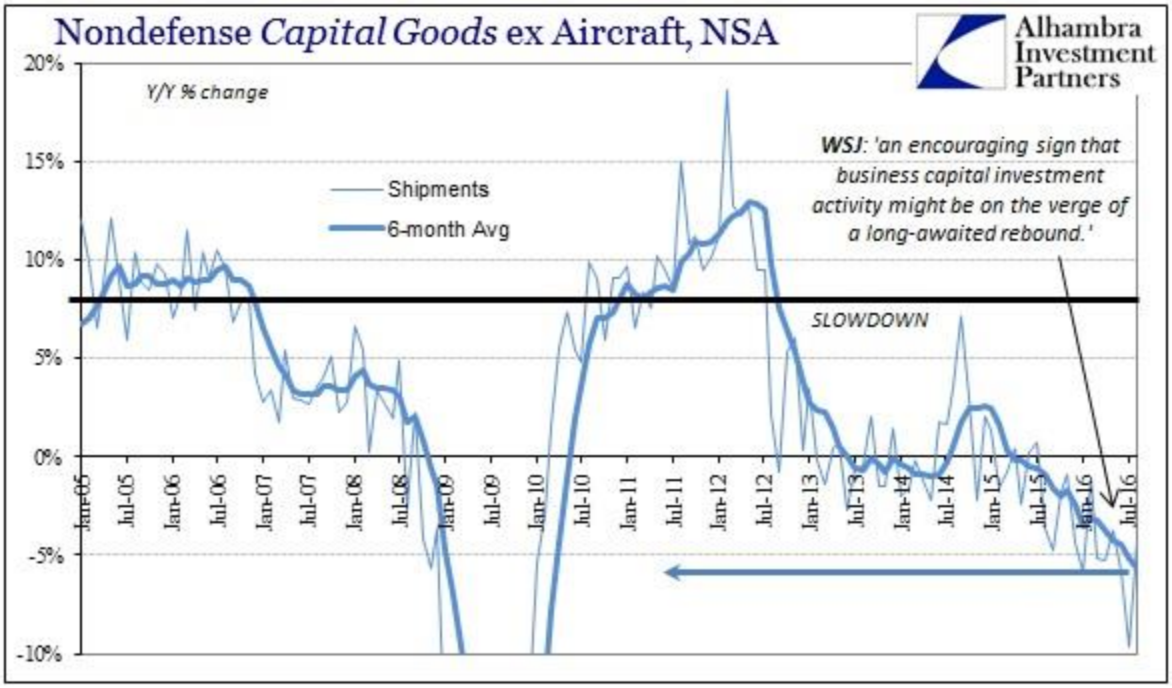
The stagnation of the goods sector of the economy is odd and unprecedented outside of recession.

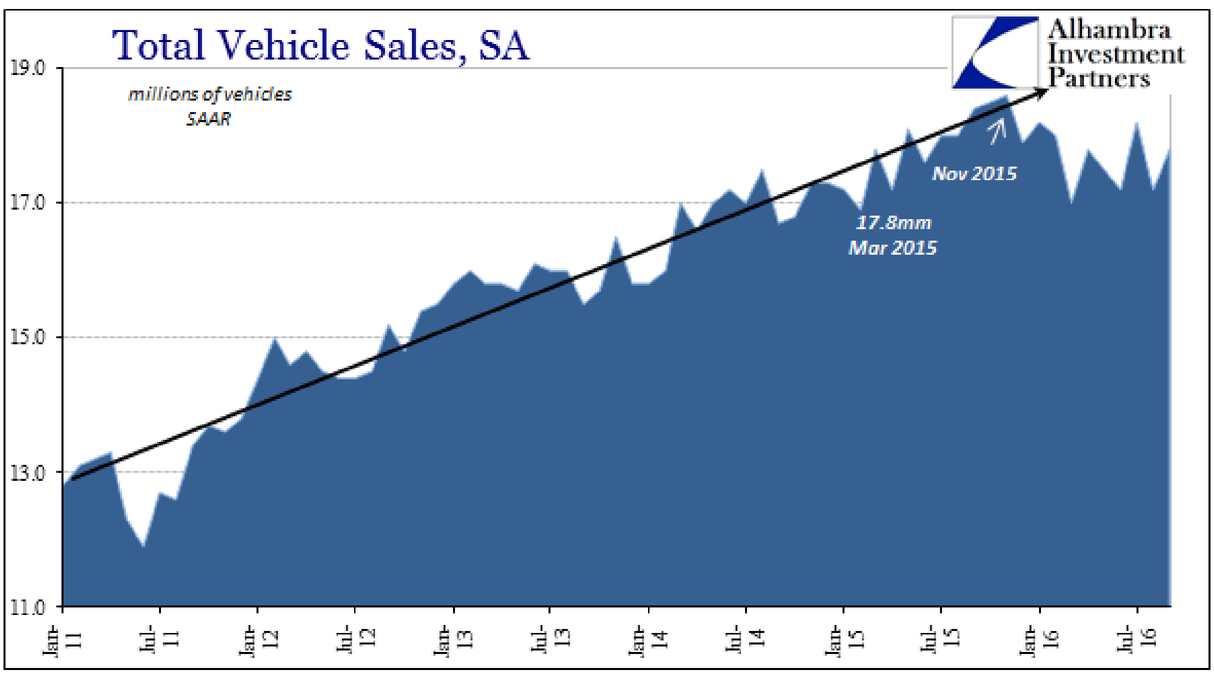




Investment is not rebouding.



Auto sales appear to have peaked.



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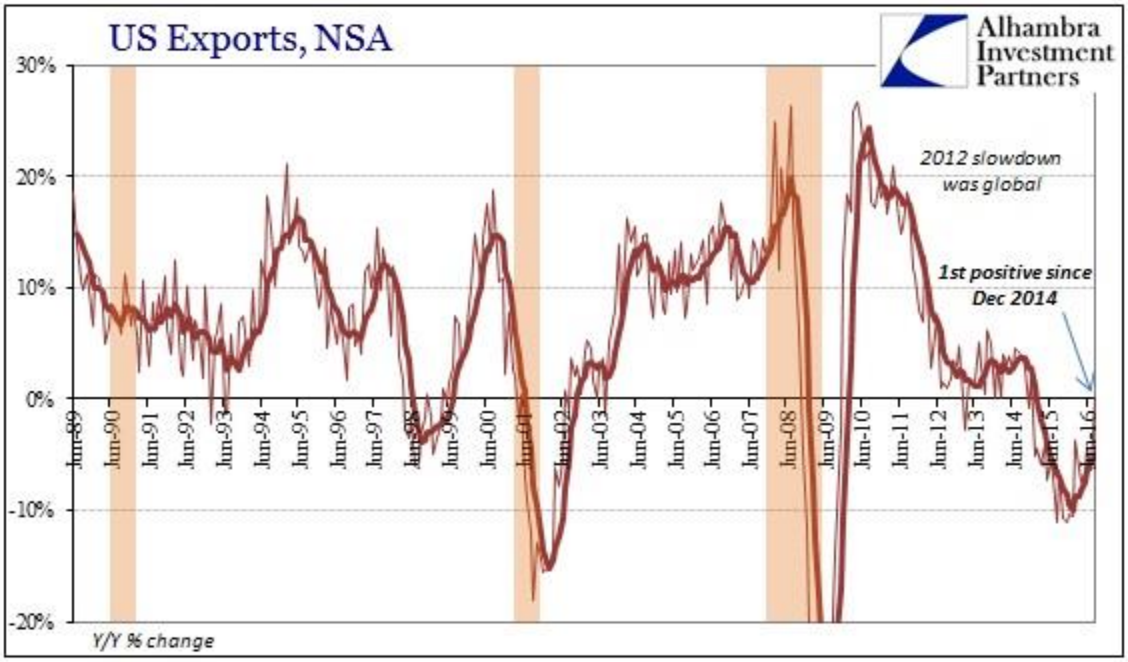
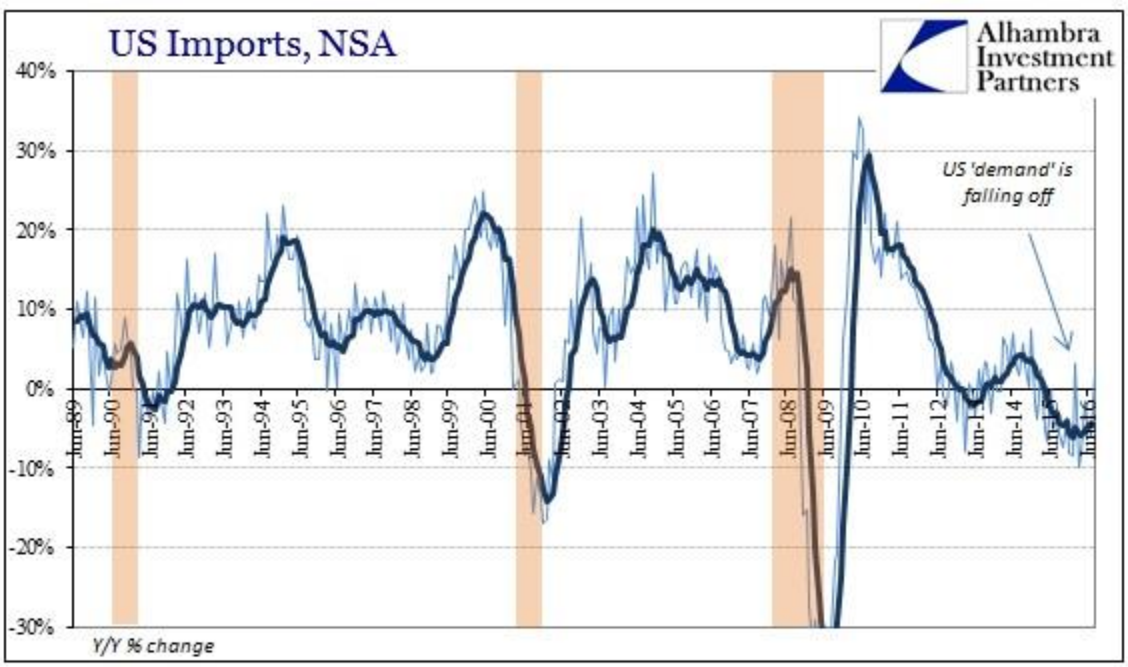
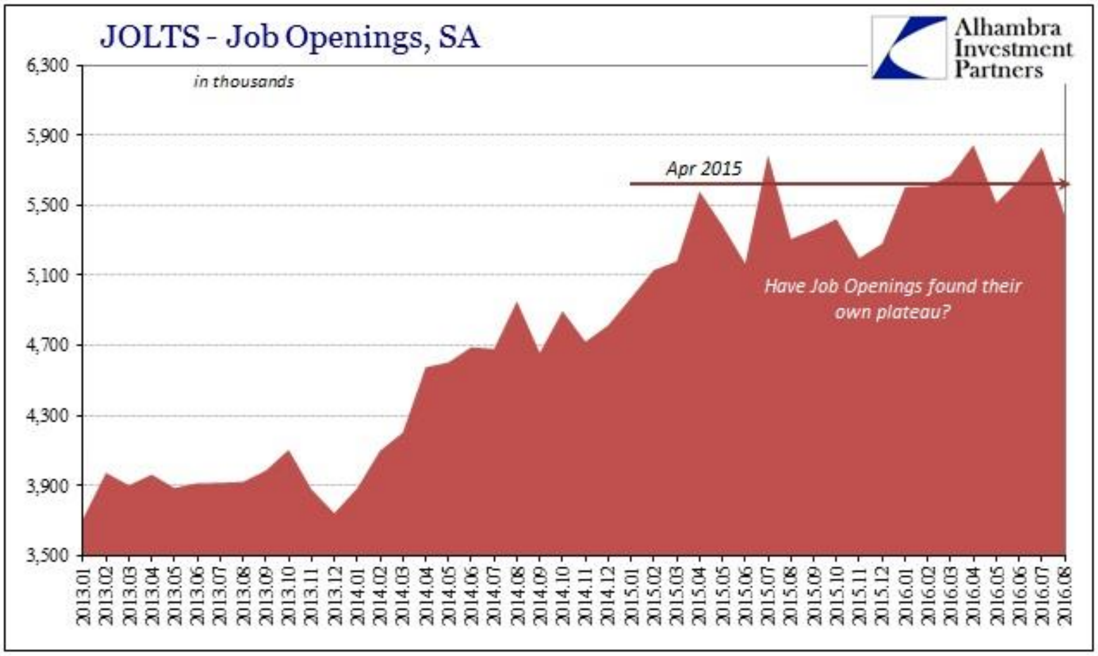
Exports and imports have recently ticked higher but the improvement is minimal so far.

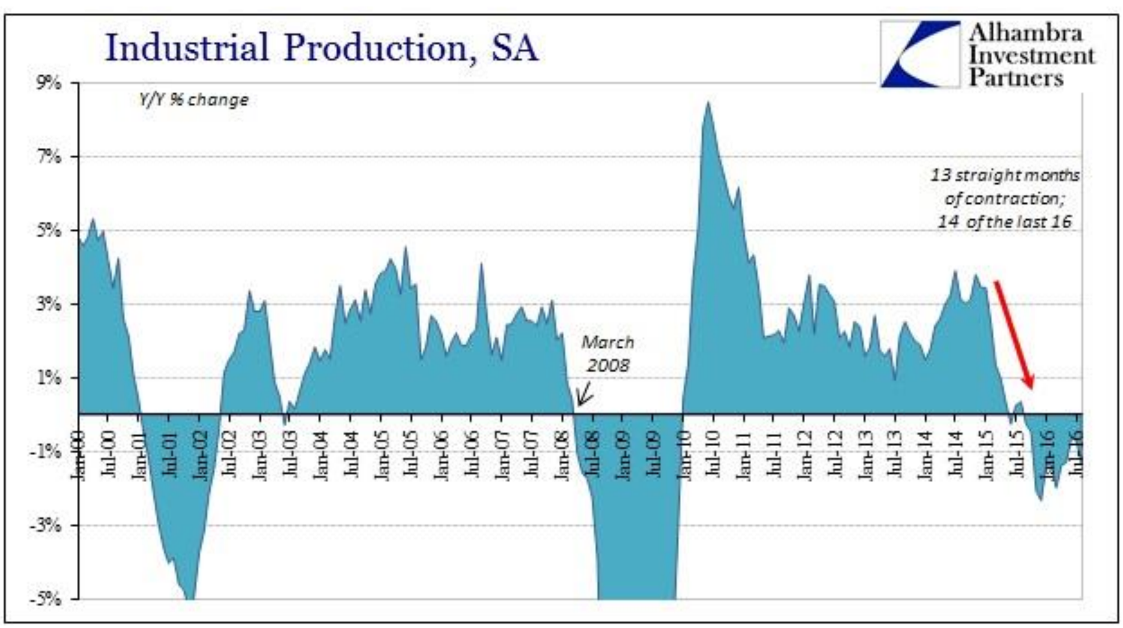




Job openings, which have been a positive, may have peaked.

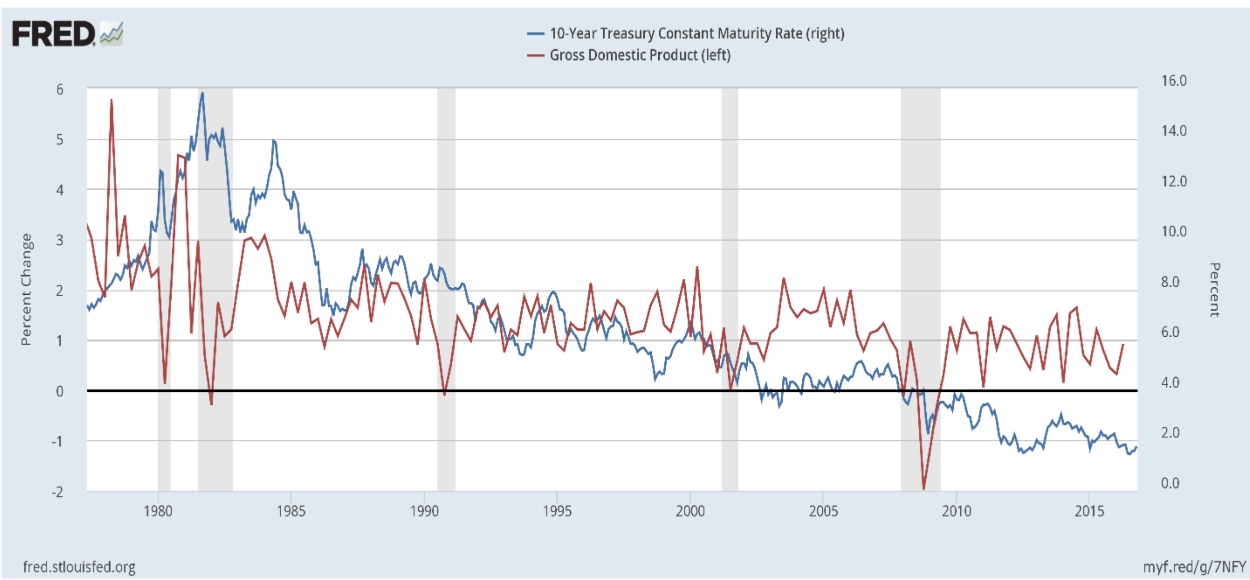


Once the election is over and everyone realizes that the new President probably can't accomplish all that much – thank God for small favors – the market will be stuck with the economy we have rather than the one of campaign promises. And that economy isn't looking all that great right now. The Fed may want to hike rates in December and maybe they'll go ahead but the evidence of economic slowing is piling up. Just to pick one metric, Industrial Production has been down for the last 13 months in a row and 14 of the last 16. That has never been seen outside recession. And there are plenty of other metrics that have a similar cut to their jib. There are some bright spots – housing seems to be improving steadily - but signs of accelerating growth are hard to find.



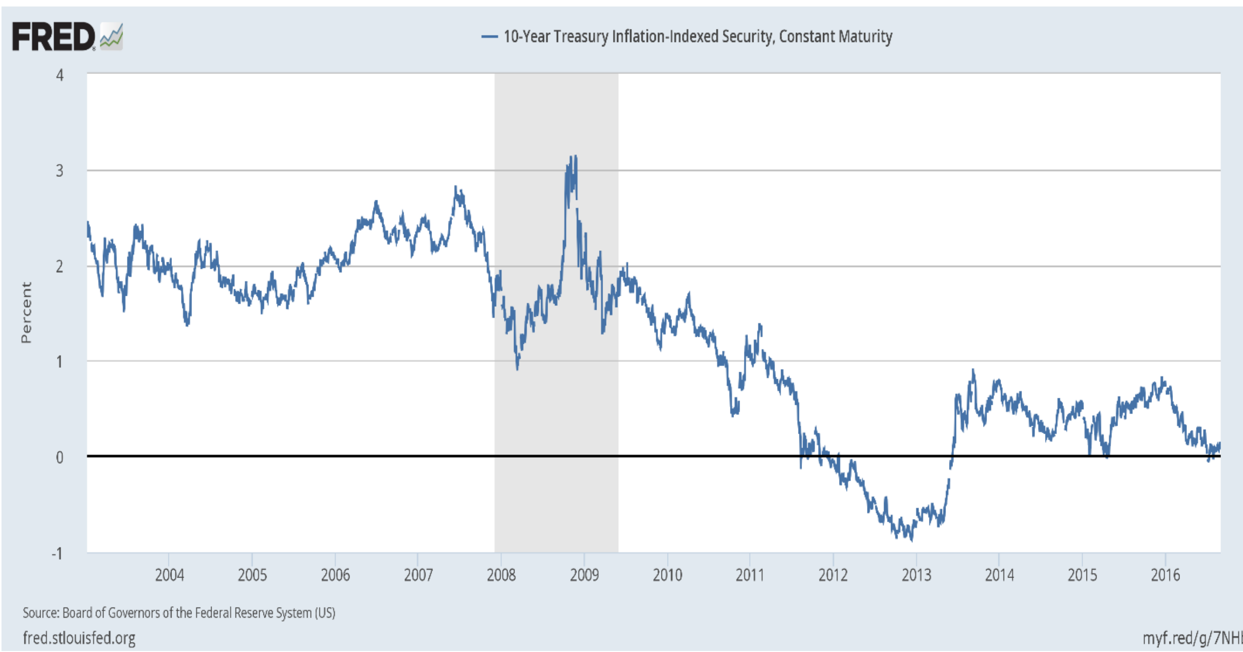
We don't spend a lot of time worrying about each and every economic release. We prefer our economic tea leaves be market generated. You don't need to go through every economic statistic to figure out where we stand overall although good micro level information can be gleaned from them. The 10 year Treasury note yielding 1.75% tells you almost everything you need to know. Here's a hint: if the next President is about to unleash an economic program that will make us great again or make us stronger together or whatever it is they are promising today, 10 year interest rates would not be stuck below 2%. If the US economy is about to accelerate as the Fed keeps promising, interest rates would not be stuck below 2%.

The 10 year Treasury yield is a good proxy for nominal growth expectations:



Remember Alan Greenspan's "conundrum"? When the Fed started to hike rates in the last cycle Greenspan – and others – were flummoxed by the seeming indifference of long term bonds. As you can see above during the period prior to the 2008 recession the 10 year Treasury yield barely budged higher even as the Fed hiked short rates by 400 basis points. Turns out it wasn't a conundrum. It was the bond market being right about future growth. You'll notice a similar disconnect now. Who you gonna believe? The Fed who says growth is just fine and about to get better? Or a bond market that says not frigging likely? Not a hard choice in my opinion.

Another clue about future growth can be found in the real interest rate, the rate offered by TIPS. Real rates are set by the intersection of savings and investment demand. Low and falling real rates indicate either an enhanced desire to save or a decreased desire to invest. Or more likely, some of both. For reference you might consider that real rates were relatively high in the 1950s and 60s, fell to negative in the 70s, started to rise around 1980, peaked in the mid to late 80s and stayed fairly high until after the 2008 crisis. They are now negative – just like the good old days of disco - all the way out to the 10 year maturity which currently yields a paltry 0.11%. Again, if long term growth prospects were improving, if investment demand was expected to rise, real rates would be going up, not down.



So, whatever outcome the market is pricing in for the election, the bond market doesn't think it is positive for growth. If today's rates are a reflection of an expected Clinton win, it might give one pause to consider that real rates have basically been falling all year; whatever ails the economy, the market doesn't think Clinton and a hostile Congress will find a cure. Would a Trump upset raise growth expectations and interest rates? Maybe, but the consensus is that a Trump win is very negative – due to his views on trade primarily - so the knee jerk reaction would probably be negative. The initial market reaction though is emotional and often reversed – see Brexit. But no matter who wins, let the bond market be your guide on growth.

The Fed

The other potential market mover in the fourth quarter is, of course, the Fed which is now widely expected to hike rates one more time before the end of the year.

While there are two meetings the overwhelming odds are that the hike – if it comes – will be after the December meeting. So, will they or won't they? And does it matter?

The market is pricing in about a 2/3 probability of a ¼ point rate hike at the December meeting and there has been sufficient hawkish talk from Fed members to make that plausible. But there has also been quite a bit of talk, especially from Janet Yellen recently, that the Fed should let the economy run a little hot for a while even if their stated targets are met. The thinking is that the Fed should let inflation overshoot to get prices back on the previous trend. That would also mean – probably – higher end rates and more "ammunition" for the next recession. Of course, that all might just be more of this Fed's wishful thinking on growth; so far they haven't been able to get to lukewarm much less "overheated".

Just as with the election, there is no way to know the outcome of Fed deliberations in advance but the market does provide guidance through the yield curve. Until about June the curve was flattening pretty steadily but has essentially stopped since then. There has been a very slight steepening recently. Since August 30th the 10 year note yield has risen 20 basis points while the 2 year note has moved up 1 basis point for a 19 basis point change in the yield curve spread. So there has been a slight – very slight – uptick in nominal growth expectations but monetary policy expectations are steady. They may hike in December but so far the market seems to be saying one and done.

We'll be a bit surprised if the Fed does move this year. The fact is that neither the economic statistics nor the bond market show sufficient growth or inflation expectations to support a rate hike. If the Fed goes ahead we think you can expect to hear more about the "conundrum" of long term rates. Rather than take the bond market at its word – growth is not getting better no matter how much the Fed wants it to - the economists will all wonder what's wrong with it, why it doesn't respond as the textbook says it should or the way their model says it should.

We may see some volatility around the Fed meetings but right now we don't think it matters much whether they hike or not. Economic growth this year will likely be less than last year and less than the already punk 2% to which we've become accustomed. Year over year growth peaked at 3.3% in Q1 2015 and was all the way down to 1.28% in Q2 2016. And so far we see no evidence of an acceleration into the end of the year. And neither does the bond market.

CEO Comment

I know politics is a sore subject for most Americans right now and I'm sorry we had to bring it up. I generally try to follow my mother's advice and avoid politics and religion in polite company but sometimes we have to broach these delicate topics. Like a lot of Americans, I'm not thrilled with my choices at the top of the ticket, but I think we'll survive whoever gets the job.

Of more importance than my personal views on the candidates is how this election might affect the economy and markets. Based on history I don't think you have much to worry about. There might be some volatility around the election but remember, we aren't electing a dictator. Whoever gets the nod, they won't have free rein and the worst of their proposals will likely end up as so much campaign trash.

The US economy is already slowing and there is, in my opinion, little reason to expect the trajectory to change. We are slouching toward a recession ever so slowly and I suspect the next President's first year may be spent trying to figure out what to do about it. That is not unprecedented. Obama faced a recession in year one. Bush did too. Clinton got lucky to some degree as his was ending right as he took office. Reagan got a double dip recession in his first term. I could go on but I think the point is made. First year or first term recessions are not unusual at all. No matter which party wins the dubious prize of the Presidency.

And that's where our focus will be – on identifying the inflection points in the business cycle. That's when the biggest risks arise and where alpha is made. For now, we don't see a recession as imminent but it is inevitable. Until we get evidence of impending recession – from the yield curve, from credit spreads – we will continue working hard to find profit opportunities where we can.

And don't let the politics get you down. As the old adage goes, this too shall pass.

Joe Calhoun

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The hypothetical portfolio results are based on the following assumptions:

1. **The hypothetical portfolio record does not include deductions for brokerage commissions, exchange fees, or slippage.**
2. **The simulation assumes that prices are not influenced by the trades of Alhambra, its owners, or its representatives, regardless of the size of the positions taken.**
3. **The simulation assumes purchase and sale prices believed to be attainable. In actual trading, the prices attained may or may not be the same as the assumed order prices.**
4. **The hypothetical portfolio results do not take into account any tax implications arising from the sale or purchase of securities, which in actual trading do have an impact on gains and losses.**

Alright, enough of the legal mumbo jumbo. The bottom line is this. We are posting this information here in good faith. If you are following our model portfolios, you are doing so at your own risk. It's your money and your responsibility.

If you want us to assume that responsibility, we are happy to do so but only on a formal basis. Please contact Bob Williams at:

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