ALL STAR FINANCIAL

Build Wealth. Retain Wealth.

QUARTERLY

REVIEW & PREVIEW

FIRST QUARTER 2018
VOLUME 25 ISSUE 1

It's Back! Volatility Returns to the Markets

If 2017 was notable for a stock market that exceeded all-time highs with minimal volatility, the 1st quarter of 2018 was something entirely different. Most of the twists and turns occurred after a strong start in the first part of January that saw global equity markets race ahead by 7.5%. By early February, the stock market experienced its first correction in close to two years by losing more than 10% of its value. It was a stark reminder to investors of the market's short-term unpredictability.

Interest rates continued to trend higher, subjecting bond investors to some of the same challenges facing those in the stock market. Core U.S. bond indices lost 3% in value by mid-February before stabilizing in March.

A variety of factors contributed to the market's turbulence. First was the continued momentum of the economy, which heightened concerns about a potential uptick in the inflation rate that would force the Federal Reserve to increase the pace of its interest rate hikes. The Trump administration's sudden imposition of tariffs on steel and aluminum imports in early March led to fears that similar actions by other countries could derail what's been a period of solid growth in the global economy. In addition, investors in technology stocks became concerned amid a flurry of bad news related to data privacy (Facebook), subscriber concerns (Netflix) and self-driving car technology (Nvidia & Tesla).

However, the fundamentals remain positive as the strength of the U.S. economy persists and corporate earnings continue to grow with the tailwind created by the tax reform passed by congress (see Bob's corner). Over the next 12 months, earnings among S&P 500 companies are expected to jump 17%[1], with global economic growth (as measured by Gross Domestic Product or GDP) projected to exceed 3%. These projections suggest this economic cycle has room to run.

However, volatility is likely to remain part of the fabric of this year's investment environment. Investors will continue to question the stability of the economy and attempt to anticipate future central bank rate hikes that could tighten financial markets. **Uncertainty = Volatility**

BOB'S CORNER

The Benefits of Tax Reform

A short 6 months ago we were uncertain of whether the much-anticipated proposed tax reform act was even going to pass. The benefits are clear. This may be the icing, on top of icing, on top of the cake. These are the benefits of the new Tax Cuts and Jobs Act passed in 2017[2]:

- Individuals – 95% will pay less tax in 2018
- Corporations – top rate reduced from 35% to 21%
- Corporations – Potential repatriation of $2+ Trillion in cash at 10% Tax rate – 8 years to pay
- Corporations – Equipment purchase write-off over a shorter period of time

All of these benefits deliver more spendable income for individuals and better bottom line revenue for corporations. This may be the good news that creates the bad news. As we discussed last quarter, the Fed's decisions to continue to raise interest rates could prove to be the biggest hindrance of the continued economic expansion. If the economy becomes too good and rates rise too fast, creating an inverted yield curve, the likelihood of a recession will be high. The Fed Chairman is walking a fine line.

As always, we want to **THANK YOU** for trusting your financial future to the All Star Financial Team. Our team puts your interests first and we are committed to going the **EXTRA MILE** to help you and your family reach your financial goals!

BUILD WEALTH. RETAIN WEALTH.

All Star is passionate about providing strategies for a safer way to a successful retirement for people who are serious about their money but uncertain about how to nurture it.

The Economy

105 Months of Expansion

March marked the 105th consecutive month of economic expansion in the U.S., following the end of the financial crisis and the Great Recession in March of 2009. By May, we'll have experienced the second longest U.S. recovery on record. In the last three quarters of 2017, GDP expanded at a solid 2.9% annualized rate, modestly exceeding expectations. Growth may top 3% in 2018.

Driving the optimism are expected increases in personal income (from reduced taxes) and personal spending. Consumer spending rose 4% in the 4th quarter of 2017, exceeding analysts' predictions. The nation's unemployment rate has dropped to 4.1%. Consumer confidence is high with many consumers in a position to boost discretionary spending.

Economists will keep a close watch on the inflation rate. At the end of February, core inflation had increased 1.9% over the past 12 months. Investors are keeping a close eye on economic indicators that suggest an accelerating inflation reading, which could signal accelerated rate hikes by the Fed.

Looking Ahead

Key data points measured by economists suggest that the U.S. is moving well past the midway point of the economic cycle. Low unemployment, increased earnings growth, higher inflation and strong consumer sentiment are important signals that we have witnessed in the recent months. Now the focus turns to the Federal Reserve, which keys in on trying to keep the economy from overheating. Its main instrument to accomplish this is interest rate hikes. The Fed's job may be more difficult following the move by policymakers in Washington to cut taxes in late 2017, particularly at the corporate level. That could boost corporate spending more than we typically see at this stage in the economic cycle, which could fan the flames of economic growth and inflation. That creates good and bad results which would likely force the Fed to more quickly move away from its easy money policies of the past decade.

Bond Markets

Yields Take a Wild Ride

Bond investors were not immune to the market's volatility as most bond indices experienced negative total returns for the quarter. The yield on the benchmark 10-year Treasury note rose 0.54% from January 1 to February 21, close to the 3% barrier last topped in 2011. By the end of the quarter, the yield leveled off at 2.74%, but rates rose enough to result in a 3.61% decline in total return for 10-year Treasuries.

The Barclays U.S. Aggregate Bond Index declined 1.46% during the quarter and has managed a paltry 1.2% total return over the past 12 months. Only 3-month Treasury bills managed positive returns for the quarter, at just 0.26%. Among other domestic categories, High Yield bonds (-0.86%) held up the best. Global bond markets outperformed the U.S. market, with the Barclays Global Bond Index gaining 1.36% during the quarter.

All-Star's bond portfolio performed better than comparative bond indices during the quarter. Year-to-date, our bond positions limited losses to just -0.60%, compared to a return of -1.46% for U.S. aggregate bond indices. Our allocation to floating rate and global bonds helped mitigate losses in a rising interest rate environment.

Looking Ahead

The performance of bonds in the 1st quarter is a reminder of the close relationship between interest rates and bond returns. Bonds are particularly susceptible to the actions of the Fed. While interest rates have experienced a secular decline over the past three-plus decades, we've begun to see a reversal of that trend. As interest rates rise, declining bond values will be a drag on the total return for most bond investors. In light of this challenge, All Star has diversified into non-traditional bond investments such as floating rate and global bonds.

Quote of the Quarter:

"Great things in business are never done by one person; they're done by a team of people."

– Steve Jobs

Domestic Stock

A Winning Streak Ends

After enjoying a run of 10 consecutive quarters of gains, both the S&P 500 (-0.8%) and the Dow Jones Industrial Average (-1.9%) posted losses during the 1st quarter of 2018. The S&P 500 experienced 11 different days with declines of 1% or more in the opening three months of the year. By comparison, the market suffered only four days of 1% or more declines in all of 2017. The volatility has been more significant on the up side as well in 2018. During the first quarter there were over ten days of 1% increases compared to only four 1% gains in all of 2017. The spike in volatility happened as we marked the 9th anniversary of the current bull market. **Uncertainty = Volatility**

Growth stocks, which enjoyed a performance advantage of 17%[1] over value stocks in 2017, continued that trend in the 1st quarter. The Russell 3000 Growth Index ended the quarter relatively flat, gaining 1.48%, while the Russell 3000 Value Index declined by 2.82%. Small cap stocks held up better than large cap stocks. The Russell 2000 Small-Cap Index declined 0.1% while the Russell 1000 Large Cap lost 0.7%.

Distinctions in sector performance were notable in the opening months of the year as well. Technology stocks drew a fair amount of negative attention, but over the course of the quarter, generated the strongest return among all sectors with a 3.7% gain. Consumer Cyclical stocks, those sensitive to economic trends, were close behind with a 3.4% return. The two worst performing sectors to start the year were Telecommunications (-6.6%) and Energy (-5.7%). Both sectors extended struggles that plagued them through most of 2017.

Looking Ahead

The price-to-earnings (P/E) ratio on the S&P 500 Index, a measure of the market's valuation, dropped to 24.51 at the end of March (based on trailing 12-month earnings)[3]. It stood at 25.52 at the end of December. It is the first decline we've experienced in several quarters. A combination of the slight decline in index value and improved corporate earnings helped temper what some view as excessive valuation levels. The outlook for corporate earnings growth remains very positive for 2018, leaving room for stocks to gain ground. The S&P 500 companies are ***projecting*** 17%[1] earnings growth this year. Nevertheless, investors should remain prepared for volatility to continue even if markets move in a generally positive direction.

International Markets

Setback for Global Stocks

International equity markets underperformed during the quarter, due in large part to fears centered on trade restrictions and tariffs. Despite strong economic indicators throughout Europe and Asia, equity markets across the globe lost ground in the 1st quarter. The MSCI All Cap World Index lost 1% during this period as European stocks declined 2% and Japan rose slightly with a 0.8% gain.

Emerging markets generated better performance. The MSCI Emerging Markets Index gained 1.42%. Latin America was the best performing region, with the MSCI EM Latin America Index gaining 8%.

All Star's international equity investments outperformed key benchmarks with a gain of 0.8% for the quarter. Our portfolios benefited from our increased focus on emerging markets, which contributed a +1.9% return for the period. We remain committed to our tactical allocation with an overweight position in non-U.S. equities, based on relative valuations and cyclical observations. We believe our focus on emerging markets, identifying active managers, and utilizing low cost ETF options for strategic allocations in the international equity asset class offers the best opportunity to add value to our portfolios.

Looking Ahead

Investors entered 2018 optimistic about the outlook for global stocks given the worldwide economic growth that was underway. Instead, the focus turned to central bank interest rate hikes, new restrictions on trade and general geopolitical unrest in many parts of the globe. Asian equities did benefit from a sudden thaw in relations between North Korea, South Korea and the U.S. It perfectly exemplified the current tug-of-war between the hope for global cooperation in contrast to the recent tariffs put in place by the Trump Administration and recent diplomatic strife with Russia. Non-U.S. markets continue to offer more attractive valuations than U.S. stocks, with forward P/E ratios of 13.7 times earnings, below historical averages for global markets and significantly lower than P/Es for U.S. stocks.

Sources: All economic data is from JP Morgan's Guide to the Markets, March 2018 (https://am.jpmorgan. com/us/en/asset-management/gim/per/insights/guide-to-the-markets/viewer#/share-by-email) and all rate of return data is from Morningstar.com, unless otherwise noted by citation: 1 –seekingalpha.com 2 – www.taxpolicycenter.org 3 – Wall Street Journal

PERFORMANCE UPDATE

First Quarter

Market Index	1st Qtr	1 Year	3 Year	5 Year
DJ Industrial Average	-1.96	19.41	13.48	13.32
S&P 500	-0.76	14.00	10.78	13.31
Russell 2000	-0.08	11.80	8.39	11.47
S&P Mid Cap 400	-0.77	10.98	8.96	11.97
Russell 3000	-0.64	13.82	10.22	13.03
S&P Global BMI	**-0.74**	**15.74**	**8.87**	**9.92**
MSCI EAFE	-1.53	14.81	5.55	6.50
MSCI Emerging Mkts	1.42	24.95	8.81	4.99
NASDAQ Composite	2.59	20.78	14.27	18.07
Barclays US High Yield Bond	-0.86	3.78	5.17	5.00
Barclays US Aggregate Bond	-1.46	1.20	1.20	1.83
Barclays Global Aggregate Bond	1.36	6.98	3.14	1.49
JPM Emerging Bond Diversified	-1.74	4.30	5.78	4.69
Barclays US Government Bond	-1.15	0.44	0.48	1.07
Barclays US Credit Bond	-2.13	2.59	2.16	2.83

*The above after-fee annualized total returns, betas, and alphas represent All Star Financial composite model performance. Your portfolio's actual returns, betas, and alphas may differ depending on your specific holdings and timing of cash flows.

Diversification, asset allocation, and value investing do not assure or guarantee better performance and cannot eliminate the risk of investment loss.

All Star Financial works on a "best efforts" basis and does not promise or guarantee any results. Past performance does not represent future results.

SUMMARY & OVERVIEW

It was almost exactly 10 years ago that the financial giant Bear Stearns collapsed, one of the first dominoes to fall in a downturn that would engulf Wall Street and world markets. The U.S. stock market reached its low point in March 2009 and the recovery from that low continues today. Since then, U.S. equities have risen nearly 300% and unemployment has dropped from more than 10% to roughly 4% today. Much of the turnaround can be credited to low interest rates combined with low inflation, and the $4.5 Trillion infused into the financial markets through Quantitative Easing.

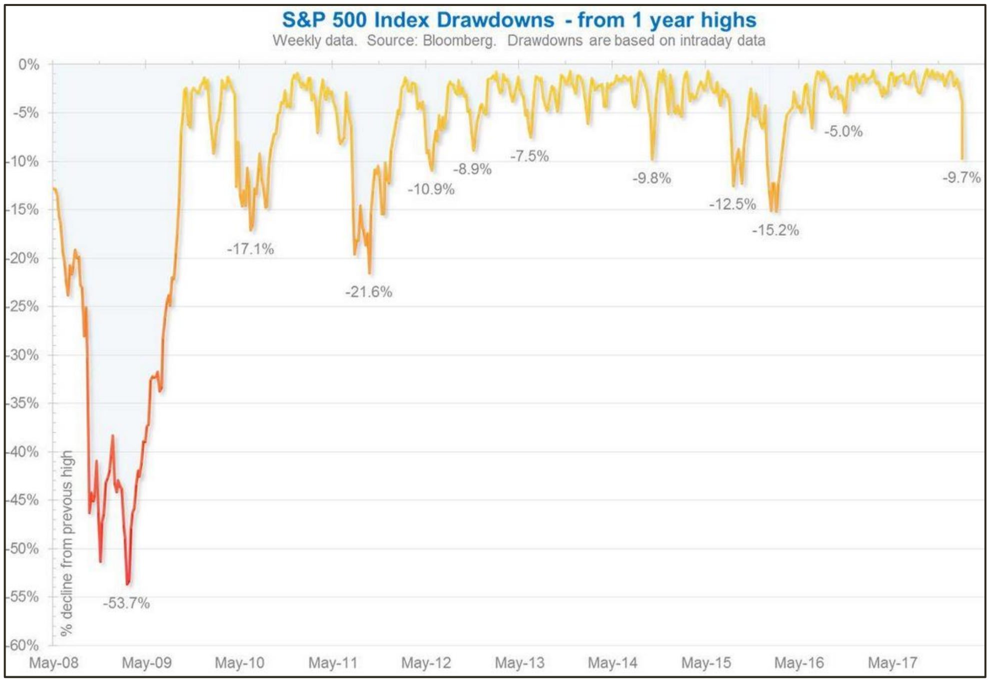
As those measures begin to reverse themselves, the issue is how long the economy can continue to grow before a recession strikes. With the tailwind of new tax cuts, strong consumer sentiment and favorable profit trends for corporations, it appears that the economy should continue on its present course for the foreseeable future. At the same time, we are closely watching the impact of trade restrictions, potential regulations on technology companies and growing geopolitical tensions in parts of the world. The driver for both upside and downside volatility is UNCERTAINTY!

With that as context, investors must again focus on diversification. Bond total returns suffered in the first quarter and may not be a risk-free safe haven against headwinds for equities. A mix of the right risk mitigating investments along with a solid and focused equity portfolio is critical in this late phase of the economic cycle.

"It's not how much you make, it's how much you keep!"

-Bobby K

Volatility *Returns*!

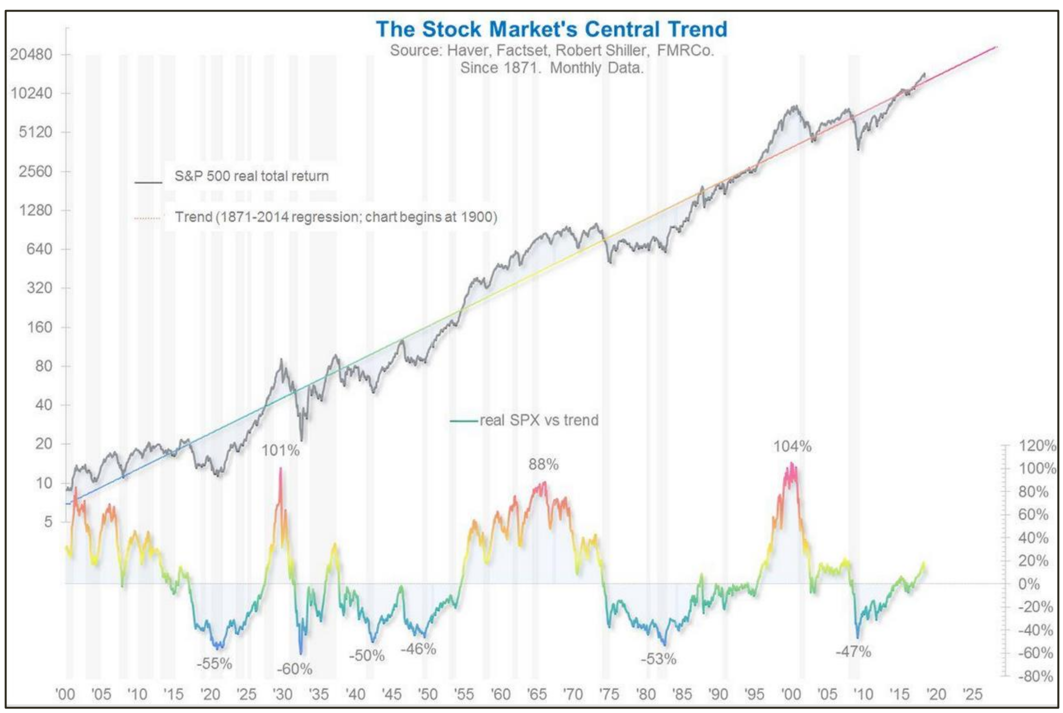


400 Days Between "Corrections"

March of 2009 marked the bottom for equities during the financial crisis after a 53.7% decline. Since then, domestic stocks have risen at a dramatic pace. Between January 26th and February 8th of this past quarter, we witnessed a 9.7% drawdown (decline in value from the recent market peak). In the context of this 9 year bull-market, that was the 7th most significant drawdown through this period. Do you remember the 12.5% and 15.2% drawdowns in 2015 and 2016? Two years later, many investors have forgotten those significant pull backs and replaced those memories with the success of the past 20 months. Markets are volatile and the ability to focus on long term trends and take advantage of opportunities rather than react to short term volatility will help investors achieve their investment goals!

100 Years of Market Perspective

Daily market movements so far in 2018 have seemed out of the ordinary. However, when you evaluate them relative to the movement of the S&P 500 dating back to 1871, we gain a better long term perspective. The graphic at the right shows the trend line (average return) of the S&P 500 since 1900 compared to the ACTUAL market movement. You can see that during periods of disruptive growth, the actual return grows above the trend line. For example, the last significant rise above trend was during the tech-bubble from the late 1990s to the early 2000s when the index rose 104% above the trend line. Today, the S&P 500 is also above the historical trend by almost 20%. The index will most likely revert to the trend line during the next recession. The question is how long the US economy can continue to grow as financial conditions tighten.



OUR MISSION IS TO HELP YOU ACHIEVE YOUR DESIRED STANDARD OF LIVING AND FINANCIAL PEACE OF MIND.

The experienced All Star team of professionals is dedicated to understanding your individual needs and objectives, offering a comprehensive wealth management platform that is designed with one purpose in mind — to serve you, our valued client.

Restaurant Recommendation: *The Anchor Fish & Chips*

Dreaming of authentic Fish & Chips from across the pond? Look no further than Northeast, Minneapolis! The Anchor Fish and Chips uses only the freshest ingredients to make their classic Alaskan Cod & Hand Cut Chips as well as their other popular items which include Shepard's Pie, Grass Fed Burger and Meat & Veggie Pasties. For early birds, they offer a full Irish breakfast on Saturday and Sundays. The Anchor Fish & Chips provides a true Irish pub experience by serving Guinness, Kilkenny, Harp & Magners Cider, amongst many others!

Out and about? The Anchor Fish & Chips food truck might be near you! View their most up-to-date Food Truck Calendar by visiting their website!

Recipe of Quarter: Steak Kabobs

Marinade Ingredients:

1/4 c olive oil
1/4 c soy sauce
1 1/2 tbsp fresh lemon juice
1 1/2 tbsp red wine vinegar
1 tsp freshly ground black pepper
2 1/2 tbsp Worcestershire sauce
1 tbsp honey
2 tsp Dijon
1 tbsp garlic

Kebabs Ingredients:

1 3/4 lbs sirloin steak (look for thicker steaks), cut into 1 1/4 inch pieces
8 oz button or cremini mushrooms , halved
2 - 3 bell peppers cut into 1 1/4-inch pieces
1 large red onion diced into chunks (about 1 1/4-inch)
1 Tbsp olive oil , plus more for brushing grill grates
Salt and freshly ground black pepper
1/2 tsp garlic powder
10 wooden skewer sticks soaked in water for at least 30 minutes

Instructions:

For the marinade:
In a mixing bowl whisk together all marinade ingredients.

For the kebabs:
Place steak into a gallon size resealable bag. Pour marinade over steak then seal bag while pressing out excess air and message marinade over steak. Transfer to refrigerator and allow to marinate 3 - 6 hours.
Preheat a grill over medium-high heat to about 425 degrees. With veggies on cutting board, drizzle with oil and lightly toss to coat. Sprinkle veggies evenly with garlic powder and season with salt and pepper. To assemble kebabs layer steak and veggies onto kebabs in desired order, work to fit 4 steak pieces onto each kebab. Brush grill grates lightly with oil. Place kebabs on grill and grill until center of steak registers about 140 - 145 degrees for medium doneness, turning kebabs occasionally, about 8 - 9 minutes. Let rest for a few minutes then serve warm.

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