



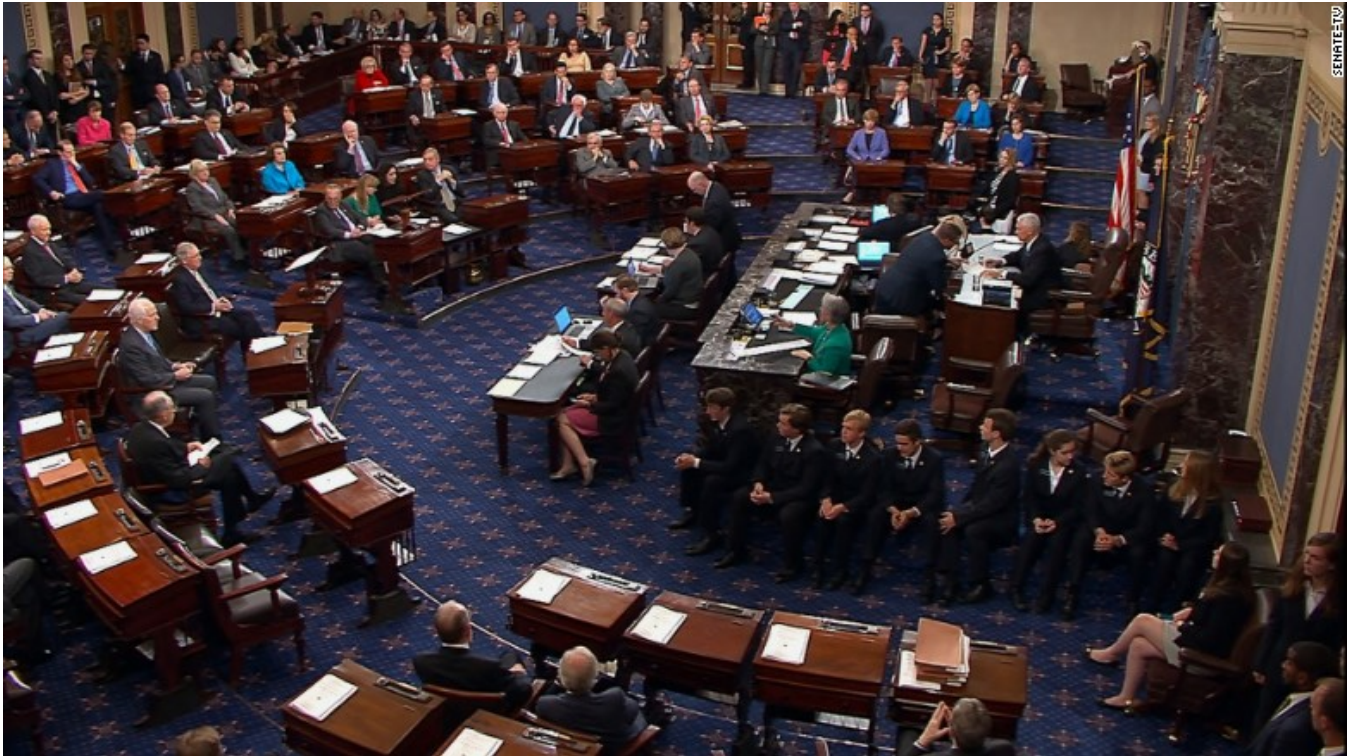
The Top-Down

Tax reform took center stage again this week, and the markets are embracing what the Republican package has promised to deliver. The rally continued on Tuesday, as the Senate version made its way out of the Budget Committee and again on Thursday when Senator John McCain voiced his support. Late in the trading day The Joint Committee on Taxation released their non-partisan assessment of the plan.

Instead of the robust 3%-5% growth boost touted by the White House, their analysis resulted in a far smaller contribution of 0.8% over ten years. Democrats cheered the report, while Republicans immediately said it was based on bad math that underestimated capital spending and wage growth. John Harwood frames the 'faith v. evidence' debate.

Stillwater View: While directionally positive for the economy and growth, the process by which this bill is coming together feels a lot like the Affordable Care Act. Not a single vote from the other side of the aisle and a party that wants it done to show they knew how to make something big happen. House Speaker Pelosi said at the time she wanted Obama Care passed 'so we could find out what's inside'. Let the grand experiment begin again.

'The World's Most Exclusive Club'

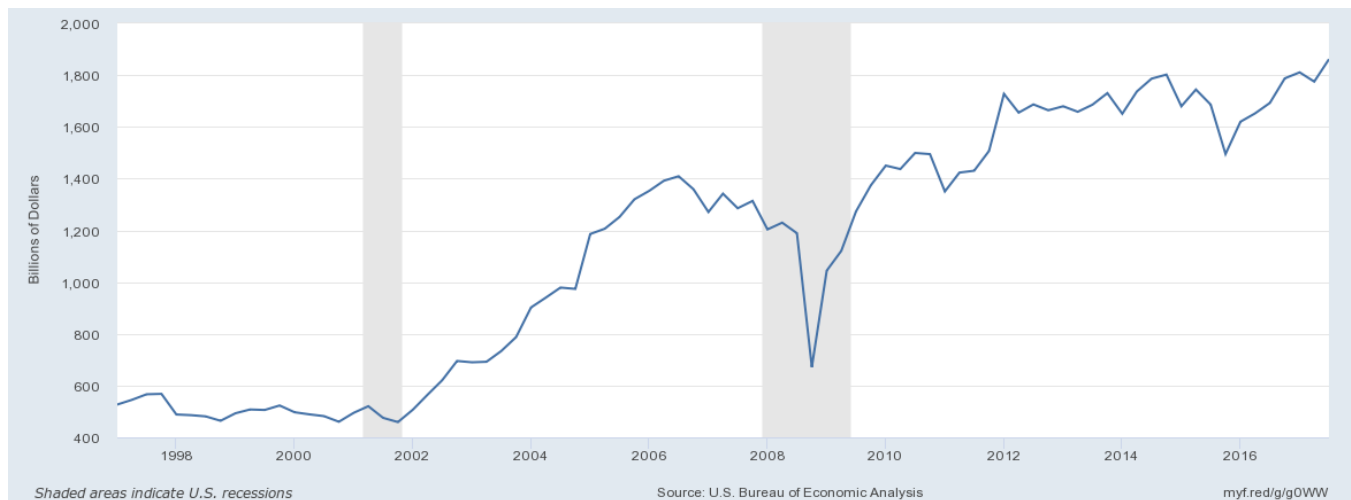


Source: CNN

The Senate is scheduled to vote on the measure at 11:00 am Eastern today. Once passed, the debate over who will win out, shareholders or jobholders, can begin in earnest.

Stillwater View: Drop the puck already and let the market get on with it's much anticipated 5, 10 or 15 percent rally. Nobody wants to put a parachute on the profitability dragster that is currently ripping down the equity market speedway.

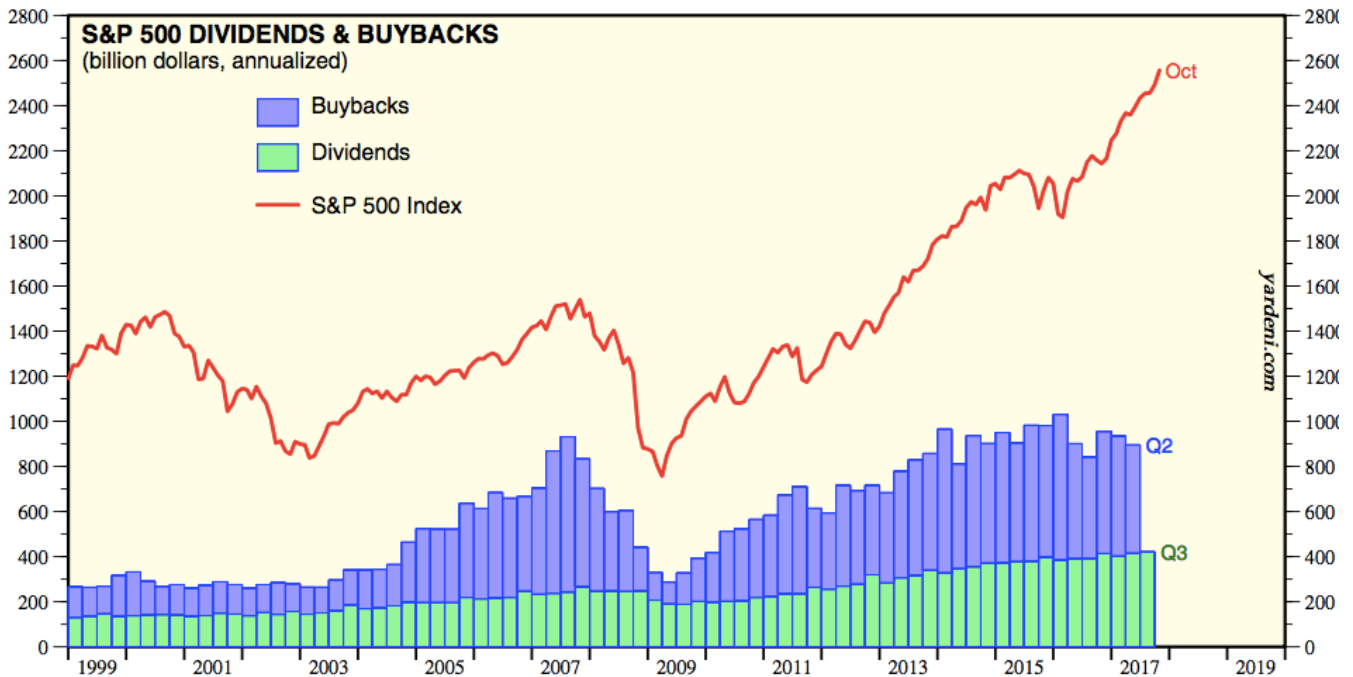
After Tax Corporate Profits



Source: St. Louis Federal Reserve

Natixis chief economist Joe LaVorgna doesn't like the bill, calling it "terrible" and that it "won't do much of anything for growth". He summed up his argument by saying "companies have the money to spend, they're just not spending it. They're buying back stock. They'll do more of that." And increase dividend payouts as well.

Dividends & Buybacks

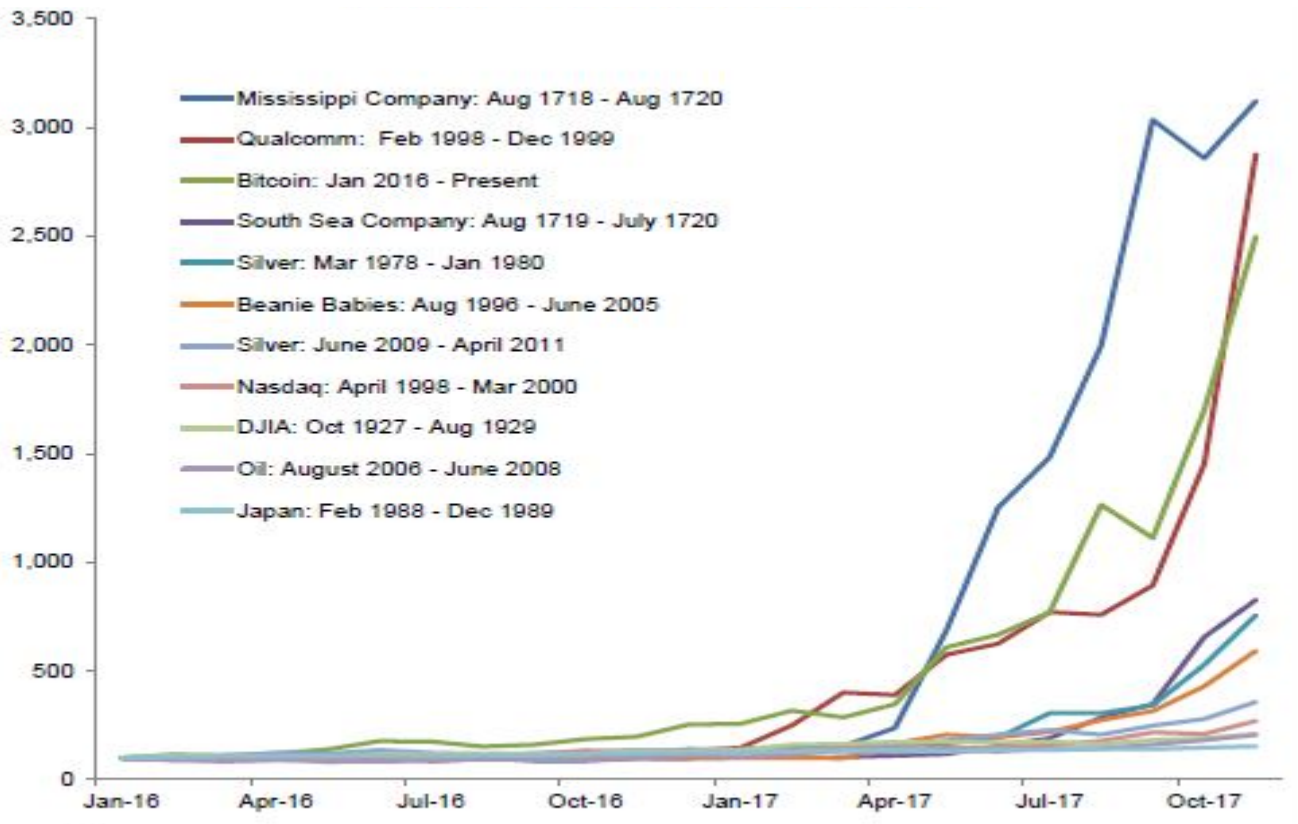


Source: Yardeni Research

Stillwater View: This plan includes a corporate side that is probably too aggressive and an individual side not aggressive enough. Or aggressive the other way if you live within 100 miles of the Atlantic or Pacific Oceans. The risk here is that the economy gets juiced late in the cycle and that draws inflation forward. An accompanying spike in interest rates would be a challenge for a stock market currently devoid of fear.

Activist shareholder and Trump confidant, Carl Icahn made an appearance on CNBC Thursday and provided his opinion that while earnings are going to be very good, the market 'has gotten into a euphoric state' and that 'there might be a big correction but I can't say it's insane'. If it makes you feel better, Carl the billionaire investor can't comprehend Bitcoin either.

Bitcoin Compared to Previous Bubbles

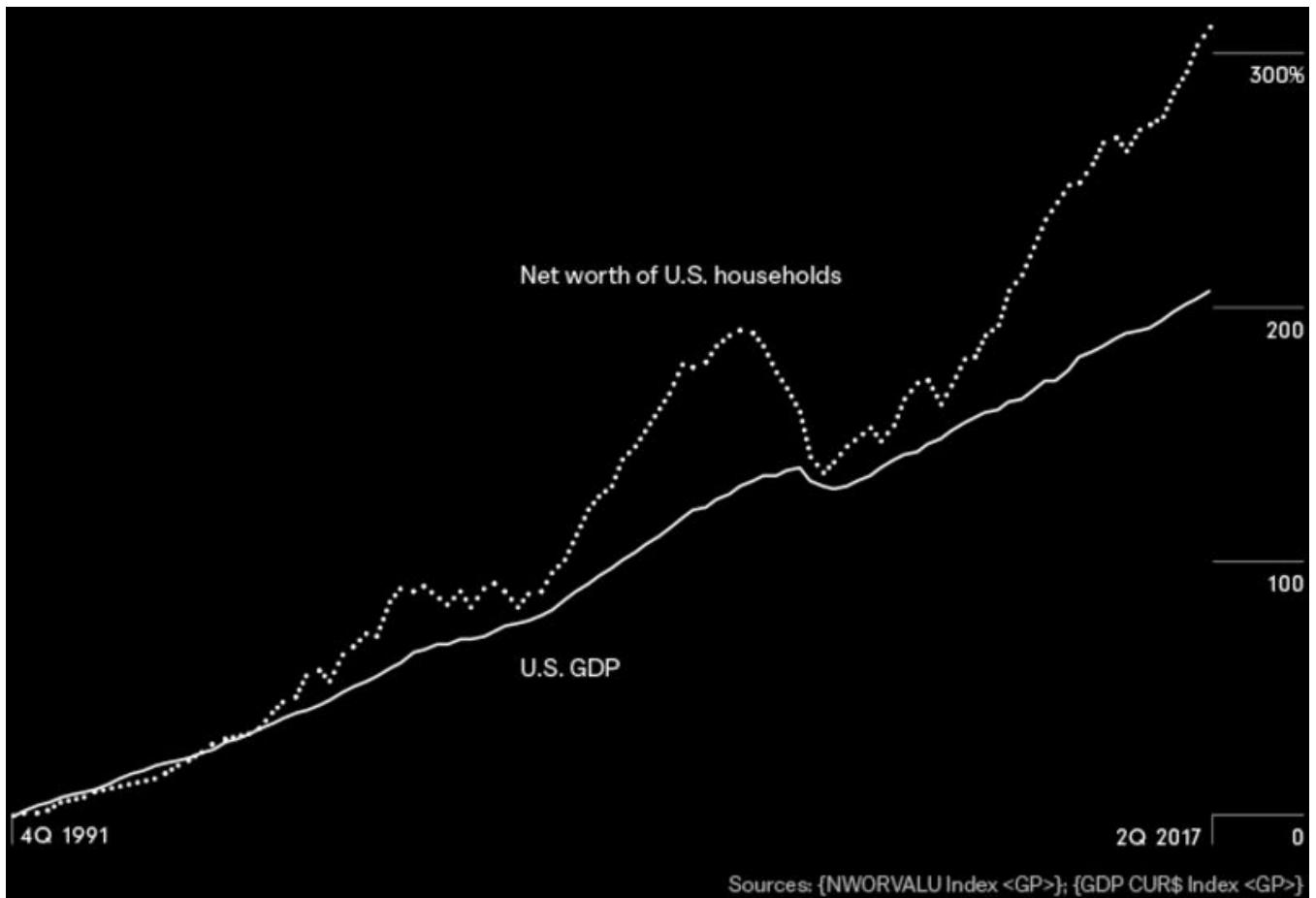


Source: Birinyi Associates

Bloomberg ran an article this week entitled “What to Worry About in This Surreal Bull Market” which included observations from some of Wall Streets’ highest profile managers, including AQR’s Cliff Asness, Vanguards Bill McNabb, Hayman Capital’s Kyle Bass and Dan Fuss, the self-proclaimed optimist at Loomis Sayles.

One of the best comments came from TCW’s Stephen Kane, manager of the \$80 billion TCW/MetWest Total Return Bond Fund. Mr. Kane observed that adverse events, like the subprime meltdown, can occur months or years before a financial cataclysm, and that “the catalysts are invisible until they’re visible.” His partner Tad Rivelle uses the chart of net worth to GDP to show the “unstable deviation” of asset values to growth.

Net Worth to GDP



Source: Bloomberg

Fund giant Vanguard is convinced there is now a 70% chance of a market correction of 5% to 10% and that investors should lower their expected return assumptions going forward. The index giant says investors should expect a return of ‘no better than 4% to 6%’ annually over the next five years.

Stillwater View: To put that “4% to 6% annually” in perspective, the Dow Jones and S&P just handed you 3%...in four days! And keep in mind, those low return expectations come from a firm that is in the business of taking your dollars and investing them on the long side of the market. At the lowest fee possible, of course.

Goldman Sachs was out earlier in 2017 highlighting just how expensive the aggregate market has become.

Goldman Sachs Looks at Aggregate Valuation

Metric (Aggregate index)	Aggregate Index		Median Stock	
	Current	Historical %ile	Current	Historical %ile
EV / Sales	2.3 x	96 %	2.9 x	100 %
Forward P/E	18.1 x	89	18.3 x	97
Cyclically adjusted P/E (CAPE)	26.5 x	88	NA	NA
Cash flow yield (CFO)	7.1 %	88	7.0 %	98
EV / EBITDA	11.7 x	88	11.9 x	98
Price / Book	3.3 x	87	3.4 x	99
P/E to growth (PEG)	1.3 x	81	1.8 x	100
Free cash flow yield (FCF)	4.1 %	55	4.2 %	55
Median		88 %		98 %

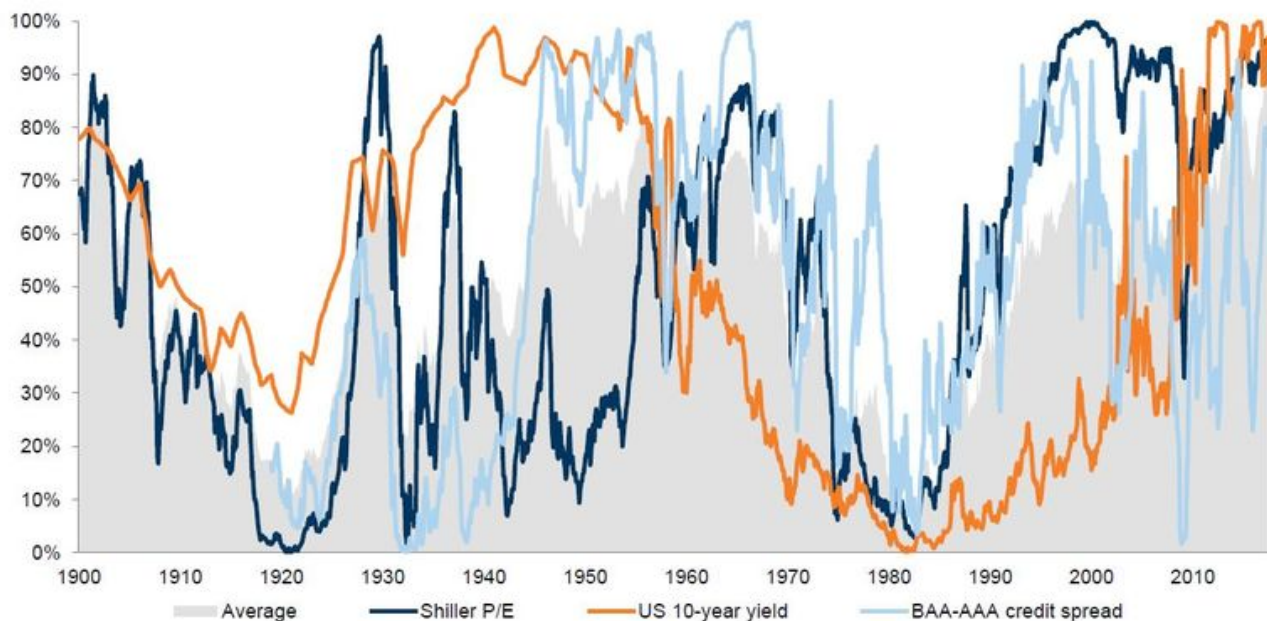
Note: Data since 1990 for CFO and FCF, 1981 for PEG, and 1976 for all others.
Cash flow from operations yield and free cash flow yield exclude Financials and Real Estate.

Source: Goldman Sachs

This week they doubled down when the firm released a report highlighting that stocks and bonds have not been this expensive since 1900. “Elevated valuations increase the risk of draw-downs for the simple reason that there is less buffer to absorb shocks,” Goldman’s Christian Mueller-Glissman wrote. “The average valuation percentile across equity, bonds and credit in the U.S. is 90 percent, an all-time high.”

In a separate report, the firm said that if you liked 2017, you are going to love 2018 as the late cycle party is likely to keep going. *Bloomberg* has the firm’s top eight trades for the new year.

Valuation Percentile Since 1900 - S&P 500, U.S 10-Year and Credit Spreads



Source: Schiller & Goldman Sachs International Research

The Bottom-Up

Bloomberg noted this week that broad index strength has been masking rotation under the surface. This was highlighted on Wednesday when the market leading technology sector stumbled badly while the retail and financial services side rallied. The former being attributed to short covering, and the latter to a move forward on deregulation and tax reform.

J.P Morgan equity derivatives strategist Shawn Quigg, thinks the rotation, out of the well owned growth category could continue. This would not bode well for the “hedge fund hotel”, otherwise known as the FANGs. Growth has outperformed value by 17% this year.

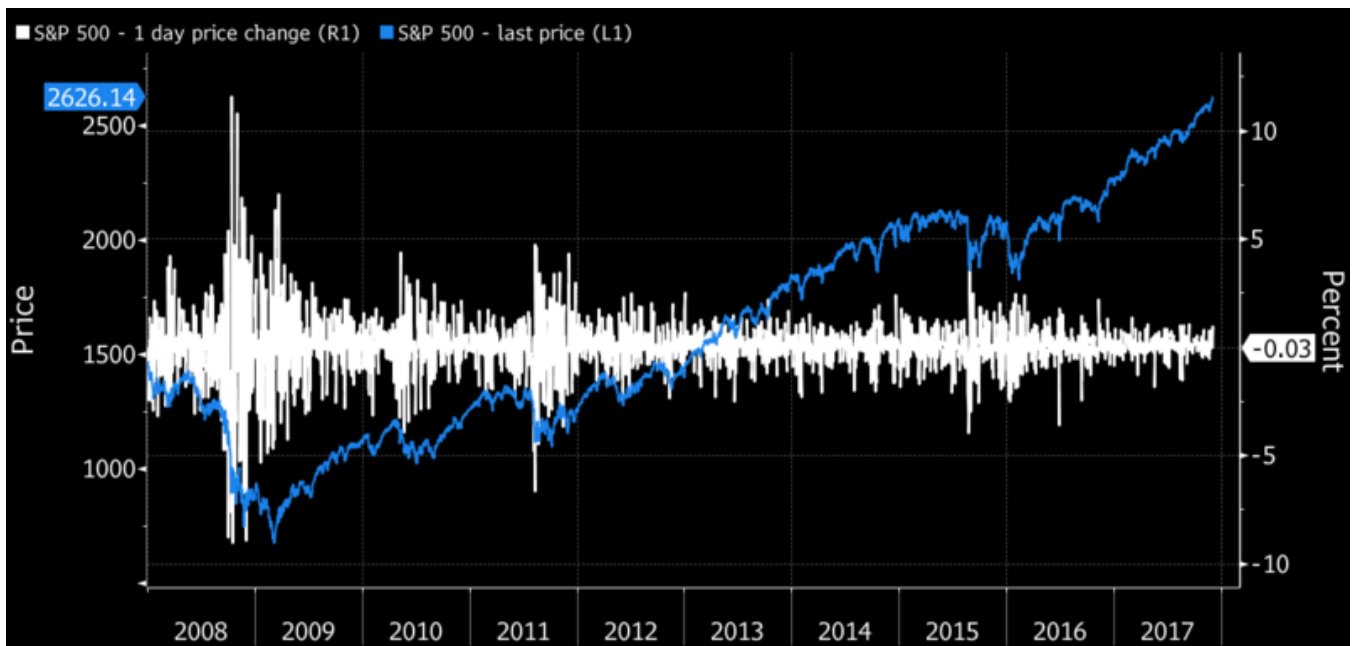
Growth v. Value



Source: Bloomberg

Meanwhile the historic rally continues with ever lower volatility.

S&P 500 Index with the One Day Price Change as Backdrop



Source: Bloomberg

Talk about a down round, SoftBank Group has ponied up \$6 billion to Uber investors who want to sell their stake at a 30% discount to the most recent round. The tender started on Tuesday and can last up to 20 days. If an insufficient number of sellers show up SoftBank can raise their offer or walk away.



In other down round news, Jessica Alba's Honest Company took a 57% valuation haircut in October when it raised \$75 million at a value of \$19.60 per share. The previous Series D was priced at \$45.75 in 2015. The company has taken a reputational hit over the last two-years, as lawsuits targeting the companies claims on the purity of ingredients have tarnished the brand and forced it to start writing checks to make the plaintiffs go away.

Actress Jessica Alba with Honest Company Products



Source: Latina Magazine

Amazon hosted their annual re:Invent conference in Las Vegas this week. The gathering brings together developers and users of the company's Amazon Web Services. Goldman Sachs took the opportunity to raise their target price by \$150 to \$1,450, giving the stock 21% upside from here. As John Malone and Rodger McNamee said recently, the world is running scared by the company's reach, as business after business are increasingly in range of the 'Death Star'.

The Death Star Going About Its Planet Destroying Business



Source: Nerds.com

Up and Down Wall Street

Citadel founder and billionaire Ken Griffin, joined CNBC this week, and as Dealbreaker reported, he ‘\$h!t on just about everything’. The markets are late innings, Bitcoins are tulip bulbs. And tax reform is ‘useless’ in terms of timing.

Ken Griffin has \$8 Billion Reasons to Smile...and Opine on Just About Everything



Source: Chicago Tribune

Wells Fargo is releasing their 2018 broker compensation plan this morning. And in a move to retain top producers, they are increasing payouts to 50% on every dollar of revenue for certain brokers.

Wells Fargo was also in the news this week for behavior that doesn't reflect well on the institution as reports emerged that foreign exchange trades performed by the bank for clients were rarely settled at the price offered.

The Wall Street Journal reported that of the 300 fee arrangements Wells had with clients, roughly 35 were charged the actual price that was agreed upon. *The Journal* also highlighted that transaction costs ranged from 1% to 4% of the trade, while the industry average is 0.15% to 0.5%. Wells Fargo disputes the claim. Charles Pierce, who presides at that venerable business publication known as *Esquire*, wrote that the financial institution is “three fedoras short of being the Gambino family”.

Stillwater View: While only a small piece of the overall profit pie at Wells Fargo the not so pleasant headlines just keep coming. The tarnish of which will last for some time.

Wells Fargo Retail Branch



Source: Wells Fargo

Barriers to exit are going up on Wall Street as both Morgan Stanley and now UBS have left what is called the “broker protocol”. Created in 2004 as way to cut back on litigation and arbitration, the agreement allows financial advisors to leave a member firm and take with them their client name, address, phone number, email address, and account title of the clients they serviced while at the firm.

It also allowed for the solicitation of former clients once the broker landed at a new home. The exit from the protocol by UBS is another sign that traditional wire-house brokerage firms have seen enough of the flood of advisors choosing to break away. Speculation is high that Merrill Lynch will opt out by year-end.

The Protocol is Losing Members...Fast

Protocol for Broker Recruiting Signatories That Withdrew in 2017

Company	Joining Date	Exit Date
Cornerstone Financial Partners	4/18/16	12/1/17
UBS Financial Services	8/19/04	12/1/17
Bronfman E.L. Rothschild	1/17/17	11/19/17
Legacy Financial Strategies	2/6/17	11/17/17
Biondo Asset Management	3/10/09	11/13/17
Morgan Stanley	6/1/09	11/3/17
Wellington Shields	11/2/16	10/9/17
NB Wealth Management	6/27/16	7/27/17
Freestone Capital Management	5/22/15	7/17/17
HoyleCohen	6/22/12	5/11/17
Orion Investment Advisors	11/23/15	4/13/17
Oxford Financial Group	3/27/15	4/1/17
SNS Financial Group	8/25/14	3/26/17
MetLife Securities	1/7/15	3/25/17
Iso-Ahola & Brown	3/3/17	3/23/17
Davis Management	3/3/09	3/17/17
Fairhaven Financial Advisors	8/8/12	3/16/17
Altman Advisors	7/11/16	3/12/17

Source: Carlile, Patchen & Murphy

The New York Times DealBook profiles the two men most likely to be headed for the top spot at Goldman Sachs. Current CEO Lloyd Blankfein appears to be having a good time with the speculation, as he said earlier this week, “I don’t want to give anyone out there false hope, but I’m not planning to die at my desk soon”.

Harvey ‘Big Harv’ Schwartz and David ‘D.J. D-Sol’ Solomon



Source: The New York Times

Diversions

The first, and last, Supermoon of 2017 will rise on Sunday night. Also known as the ‘Full Cold Moon’, the occurrence will have the planet nearest earth appearing 15% brighter and 30% larger than usual. Supermoons are not to be confused with the ‘Bad Moon’, rising of course. Or the Cape Cod Moonfish known to swim the waters off Hyannis in late August...at night.

The Supermoon Rises on Sunday

SUPERMOON!

Because its orbit is not perfectly circular, the moon is sometimes closer to the Earth. Perigee is the term for when the moon is closest to the Earth. When a full moon coincides with perigee, it's time for ... supermoon!

NEAREST FULL MOON
Appears 14 percent
larger and 30 percent
brighter

FARTHEST FULL MOON
Apparent diameter to scale



EARTH AND MOON: SIZE AND DISTANCE TO SCALE

NEAREST (PERIGEE)

225,622 miles (363,104 kilometers)


Earth

FARTHEST (APOGEE)

252,088 miles (405,696 km)

Source: Space.com

It's hard to believe, but we have reached Championship Weekend in college football. Auburn punched their ticket to Atlanta with a win over Alabama last Saturday. They will face the resurgent Georgia Bulldogs for a shot at the national title. Miami faces down top ranked Clemson. The Wisconsin Badgers put their undefeated season on the line against Ohio State. And tonight, out west, it's a battle of two annoyingly consistent football teams as USC plays Stanford at Levi Stadium in Santa Clara for another January 1st trip to Pasadena.

Stillwater View: The Bulldogs, Miami, Wisconsin and USC win this weekend. Full disclosure, a 3x levered inverted ETF of Stillwater sporting pics would have outperformed Bitcoin this year. Buyer beware!

The B-2 Flyover Before the 2016 Rose Bowl

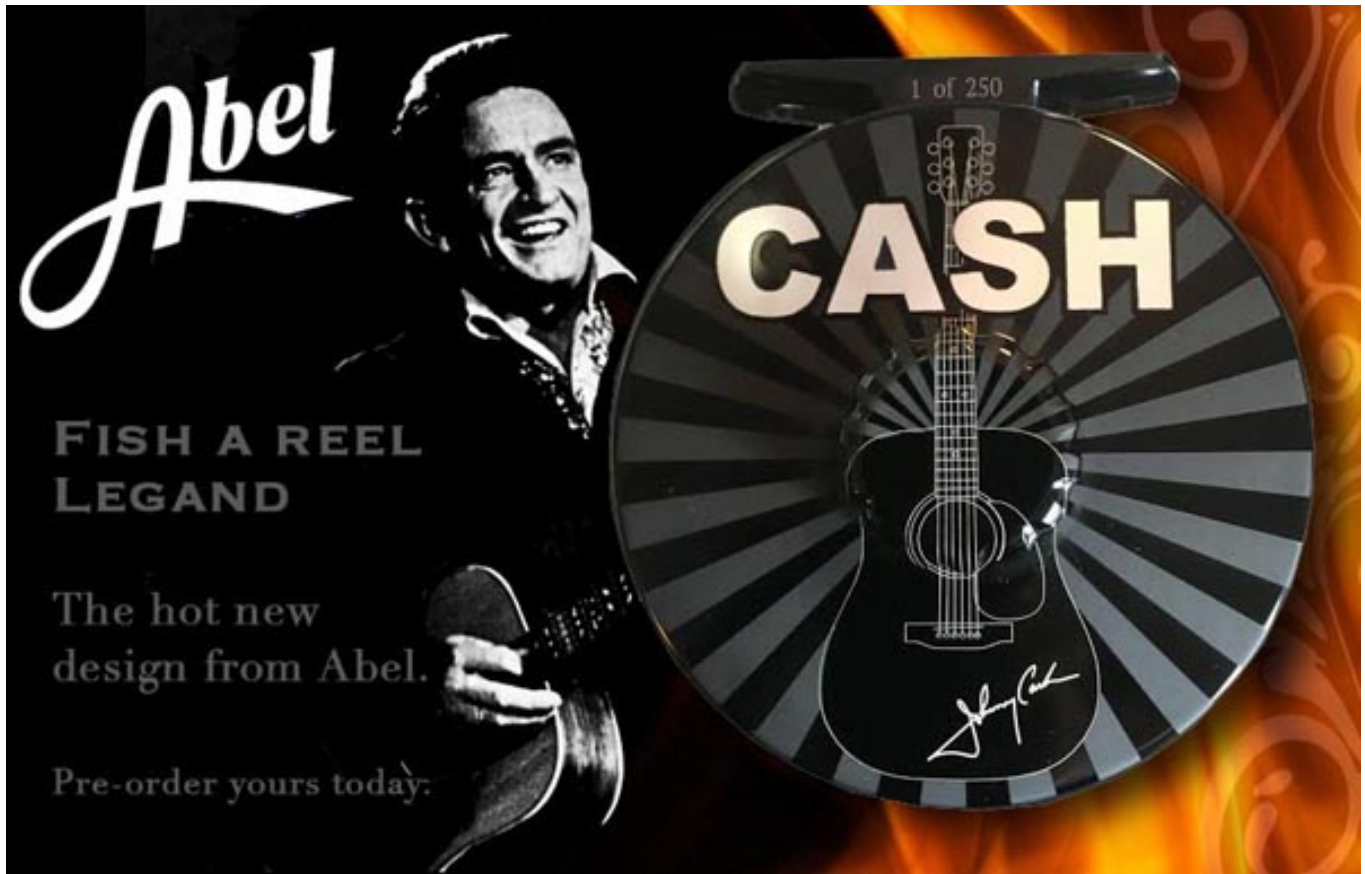


Source: Mark Holtzman Photography

From here until December 25th Stillwater will provide holiday gift ideas somewhere north of the 99 Cent Only Store and south of Neiman Marcus. *Bloomberg* lends an early assist with the list of best luxury cars coming out of this week's Los Angeles Auto Show.

For the fly fisher in your life there is the limited-edition Johnny Cash Fly Reel from Abel. The company produced only 250 of these trout slaying pieces of art. Each will set you back a cool \$1,355.00. Chances are yours will never touch the water.

The Abel Reels Johnny Cash Special



Source: Abel Reels

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