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One cannot step twice in the same river – *Heraclitus*

Perhaps you are familiar with the book Tuesdays With Morrie by Mitch Albom, a story of life's lessons as told by one generation to another. The three of us have our own Morrie, who for over 25 years has guided us as a professor of finance, mentor and friend. Our Morrie (not his real name) served clients as a portfolio manager and chief investment strategist with inspiring dedication and acclaim for nearly five decades. He also formally taught hundreds of young Chartered Financial Analyst candidates how to analyze investments and properly allocate portfolios. Those of us fortunate enough to fall under his tutelage were shepherded through some of the toughest markets this side of 1929.

We have met with our mentor for an annual end-of-year holiday lunch since 2000. Together, we summarize the financial markets for the year past and share our best individual forecasts for the year ahead. At our last lunch, we learned our mentor has an illness that will, according to his doctors, take him soon. And, that he still has more to teach and share.

While his focus has shifted from his usual concentration on the markets to more pressing affairs, he shared that he has never invested in such a complicated market. He outlined short and long-term political and financial risks and the dangers of the unwinding of today's excesses. He reminded us that markets can persist in an upward trend inducing a false sense of confidence that causes investors to believe that any correction should be interpreted as a buying opportunity. For now, momentum is a tailwind we should enjoy but, he cautioned, rebalance carefully and often so as not to become lopsided towards stocks.

Our stance for 2018 is consistent with this advice. We remain unchanged from our posture last year which is to say, in the middle each client's allowable stock allocations and we are rebalancing often with tighter rebalancing bands. We view the beginning of quantitative tightening (QT) as the largest risk to the market's continued march higher. QT is the removal of the quantitative easing (QE) programs which have stoked asset prices and supported markets since the great recession. QT changes the landscape of investing. Due to the normal lag effect, economic numbers will not register QT related changes until mid-2018 with the true impact not likely felt until the end of the year. In a vacuum, QT will strip away the US stock market's buoyancy. But we do not have the disadvantage, or advantage, of operating in a vacuum.

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It is possible that banking deregulation favored by President Trump's administration and newly appointed Fed Chair Jerome Powell will offset the negative of QT. By deregulating banks, money could start flowing again from the banking system which has been hampered by post-great recession regulation. It is also possible that economically supportive fiscal policy (in the form of tax reform and/or infrastructure spending) will take the reins, boost growth and flawlessly maintain the current trajectory of things. This will take time to play out … and you can mark us … skeptical.

We believe in the law of unintended consequences. To the degree tax reform spurs the hiring and wage increases that GOP law-makers anticipate, inflationary pressures should follow. Today, inflation remains well below Fed targets, so we are not losing sleep. But, we are watching very carefully.

Additionally, passage of the tax reform bill essentially guarantees that the US will need to issue a large amount of US Treasuries to "fill the gap" caused by the $1.5 trillion reduction in tax derived revenue over the next 10 years. We are mindful that this increased funding will occur simultaneous to QT (whereby other investors must fulfill the role of Buyer as the Federal Reserve becomes a Seller). This is perilous territory for bonds and our expectation is that yields will rise. Our concern is that the rise may be disorderly.

Our mentor reminded us that forecasting is important but is not an advisors' primary focus. Our primary focus is to manage risk using asset allocation and to invest based on sound fundamental analysis within ranges that suit each client's unique objectives.

Our real value, he said, is "your clients have entrusted Blue Oak with all their money to tend. They trust you to do the right thing. Because of this, they can rest easier knowing they have you to care for their family wealth. They are friends and in many cases, are like family."

He suggested that our work gives our clients time: time to do things that might otherwise be taken up by dealing with or worrying about financial matters. He reminded us that we all know people with "more money than they can spend in 10 lifetimes" and the one thing they cannot buy is time. "Peace of mind and time are priceless."

We are grateful for your trust in us and we don't take it for granted. We appreciate our partnership with each of you and appreciate our time with you.

Our best wishes for a wonderful 2018.