nVEST nSIGHTS

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Delivering financial peace of mind.

10268 Sawmill Parkway
Powell, Ohio 43065
614.389.4646

WWW.NVESTWEALTH.COM
Email: info@nvestwealth.com

WILL THERE BE MORE?

Bill Henderly, CFA, Nvest Wealth Strategies, Inc.

It seems the most legitimate comments about the sustainability of the current bull market relate more about the absence of signs of euphoria than the presence of investor enthusiasm. While the bull may be old in historical context at 91 months, current market charts do not provide classic signs of a top. That's hard to believe with the S&P500 only 1% below its all-time high and the other indexes – Nasdaq and Dow recently reaching new heights. Common stock investing is not close to being part of THE national point of focus as it was in 1999 or 2008. Rather, for the past 7 years (since 2009), net money flows for domestic equity mutual funds and ETFs are negative, in a redemption or withdrawal direction. That certainly can't be described as euphoria. Yet, the bull climbs onward, albeit over the past 2 years in a go-nowhere trading pattern.

Stocks in most all domestic markets achieved a new high during the 3rd quarter, the first in 285 trading days (almost 1year). That's a long time to wait for a new high, when waiting 50 days or so is more the typical market norm. Only 3 times since the 1950s did it take as long or longer to make a new high; during which the markets did experience each time a near 10% drawdown in value. Once breaking the abnormal long wait to the upside, the next 12 months were attractively positive experiences. We cannot guarantee this will be the future experience, but all the historical examples are encouraging. US stocks wrapped up the best quarter of the year, with the S&P500 rising 3.3% (also please see Benchmarking and Selected Mutual Funds for more market returns). Will there be more – more economic growth and rising market values? Investors hope to see actual sales and earnings start growing at a faster pace to permit the current market advance to continue.

Improving growth is critical to support current asset valuations – stocks are not cheap (and not exuberant). Bonds are more expensive; and real estate is not cheap (a seller's market). At the start of the 4Q, unresolved political questions for the economy and the market are in the air. What is puzzling, at least for now, is the market's reaction to a new world of political populism. Following the Brexit vote, the British stock market generated the strongest performance in the world. Investors ponder what reaction the economy and financial markets will incur during the 4th quarter and beyond following the US presidential election. Regardless of who wins, most strategists expect a shift away from accommodative monetary policy toward fiscal policy adjustments in the next several years. The Fed opted to pass on tightening during the 3Q, but will likely take opportunities to normalize rates when possible. Maybe the nature of fiscal stimulus (here and globally) can break the chains of secular stagnation and slow growth. That would boost the growth outlook for stocks in particular, and provide remedy to current valuation concerns and investor apathy. Maybe that pickup occurs slowly, starting in 2017.

Research about economic growth after a financial crisis, as summarized from "This Time is Different" by Carmen Reinhart and Kenneth Rogoff; noting that GDP growth is on average roughly 1% below normal annually for a decade after a major financial crisis. The last financial crisis can be dated in 2007 or 2008 (probably both). So, "secular stagnation" might persist through 2017 into 2018. That is, growth might not return to "normal" until after that time. So, could fiscal stimulus help? Yes, if appropriate spending, tax relief, and regulation adjustments are provided, along with slightly higher interest rates restoring incentive for banks to make loans (banks are the financial transmission for the economy); then economic and earnings growth could continue. That provides support, even encouragement for the current bull market to continue. In the nearer term, we may need to abide with more sideways, to slow advances in values; soft nominal returns. The current pace and building blocks for economic growth appear sufficient to forestall a recession in the intermediate-term (9 to 12 months). The current trends are not bad; but are they good enough?

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ANGER (PART 2)

The US Presidential election, as you know, will occur within one month. For most of us, we look forward to the end of a year-plus of presidential election process. Many struggle with the two choices, wondering if either is the best candidate America can identify. Whether it is Clinton or Trump who wins, both are the most unfavorable choices offered to the electorate, with unfavorability ratings approaching 60%. The overarching theme from the public about the election, and seen from the world population in general, is "anger" – wanting change from the last 7 years of no or slow economic growth with minimal income improvement, and increased government regulations. An angry public is difficult to predict, as evidenced by the surprise Brexit vote in June. Our November elections for President, Senators and the entire House of Representatives could also offer surprises.

"Maybe the nature of fiscal stimulus can break the chains of secular stagnation and slow growth. That would boost the growth outlook for stocks in particular, and provide remedy to current valuation concerns and investor apathy."

We are asked in almost every client meeting, "what does this election mean for investment portfolios; or should adjustments be prepared for one outcome or the other?" These are challenging questions; wish we owned a crystal ball. It is a little challenging to say what the stock market will do if Clinton wins; it seems more challenging to offer what it will do if Trump wins. And, the election impact on Congress will alter some of the market reactions as well. The new president cannot operate alone, and Congress is at least as influential on the longer-term path of the economy and policy at large. A Clinton presidency would likely cause very little change in the stock market backdrop, as she is viewed as likely to maintain more of the current policy direction. A Trump victory would likely create an initial negative market reaction, as his policy actions are more uncertain and less understood. Trump's path is simple – he's positioned as a candidate of change, anti-establishment; he's anti-Washington, expecting that he would challenge government representatives which the public feels are out-of-touch with every day pedestrian people concerns.

"longer term, studies show that the outcome of elections is not statistically significant; it is market fundamentals."

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Aside from the general unfavorability of both candidates, history provides some thought on the topic. In open election years, wherein the incumbent president cannot run for reelection, the market generally marks time or drifts slightly lower after summer leading up to the election. Separately, looking at the past 22 presidential elections, back to 1928, the stock market correctly identified 19 of the winners during the 3 months leading up to election day. If the S&P500 rose for the 3 months before the election (August 8 to November 8), then the incumbent party won (viewed as economy is okay and current policy direction of the outgoing incumbent would be similar). But, if the stock market produced losses, the challenger party won (because the trending economy and market deteriorating; change is desired). Moreover, the uncertainty associated with a new president could weigh on financial markets in the short-run. Thereafter the overall market tone often improves with a rally – those industries and sectors that would most benefit from policies of the new president rise the most.

Again, we should be reminded, the President is not a one-person government. The makeup of Congress in both the House and Senate can greatly affect policy change thereafter. It is in this vein since the last election with executive order regulations, that many of the populist are voicing anger. Anger can result in many surprises in the short-term. Yet longer term, studies show that the outcome of elections is not statistically significant (see chart at bottom of page 3); longer-term it is market fundamentals: growth – domestic and foreign trade; monetary policy; fiscal policy – spending, taxes, regulations; and confidence of business and consumers. Since 1928, there are many changing voter tones affecting the election outcomes, influencing short-term financial market reactions thereto. Yet, a long-term investor remaining true to their goals was greatly rewarded for their discipline. That principle is most likely still true.

For interesting perspective on the coming election and investment implications, a presentation for CFA Institute by Greg Valliere, a 30yr Washington strategist, can be found here:
http://bcove.me/xnpmtguz.

ANNOUNCEMENTS:

- Early October - 4Q 2016 fees collected
- October 10 - Columbus Day; bond market and banks closed.
- November 11 - Veteran's Day; bond market and banks closed.
- November 24 - Thanksgiving Day - banks and financial markets closed.
- December 26 - Christmas observed - banks and financial markets closed.
- December 30 - End of 4th Quarter; reports sent early January
- Our ADV Part 2A & B as required by the SEC & Ohio (and other states) is available to you anytime upon request.

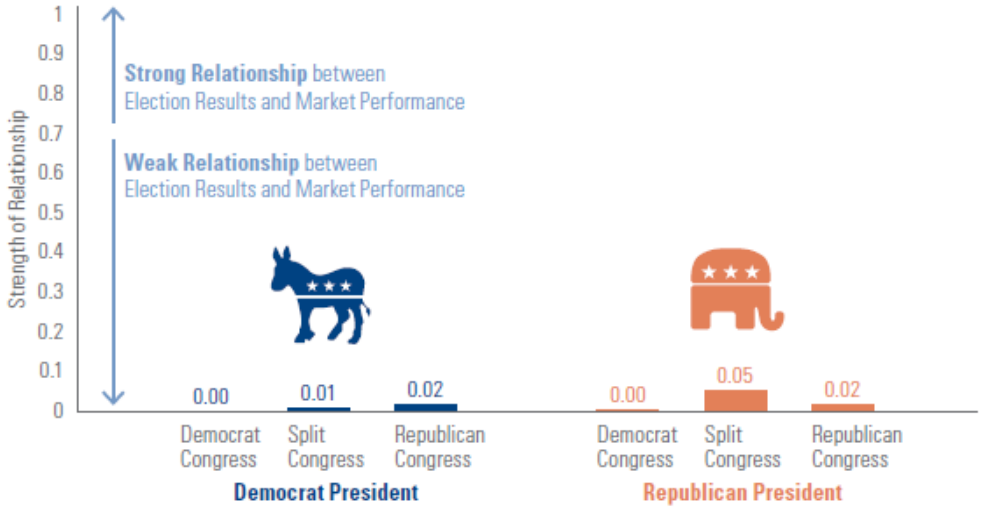
Benchmarking as of September 30, 2016

Summary of index portfolio returns compiled by Nvest Wealth Strategies, Inc.

Index Portfolio	Stock/Bond Allocation		Total Return Through 9/30/2016				
			3rd Qtr	YTD	12 Mths	3 Years	5 Years
Capital Preservation	0% / 100%	*Cumulative*	0.4%	2.3%	1.9%	3.8%	7.9%
		Annualized			1.9%	1.3%	1.5%
Income	20% / 80%	*Cumulative*	1.4%	3.0%	3.7%	6.8%	20.5%
		Annualized			3.7%	2.2%	3.8%
Balanced Conservative	35% / 65%	*Cumulative*	1.9%	3.4%	4.5%	8.4%	27.2%
		Annualized			4.5%	2.7%	4.9%
Balanced	50% / 50%	*Cumulative*	2.6%	3.8%	5.8%	10.8%	37.8%
		Annualized			5.8%	3.5%	6.6%
Balanced Growth	65% / 35%	*Cumulative*	3.4%	4.3%	7.0%	12.6%	48.1%
		Annualized			7.0%	4.0%	8.2%
Growth	80% / 20%	*Cumulative*	4.1%	4.8%	8.3%	15.2%	60.7%
		Annualized			8.3%	4.8%	10.0%
Aggressive Growth	95% / 5%	*Cumulative*	4.7%	5.2%	9.1%	16.4%	68.5%
		Annualized			9.1%	5.2%	11.0%

The index returns reflect returns of various mutual fund averages compiled by Morningstar and allocated as follows: Capital Preservation: 90% Bond Average, 10% Treasury Bill Index; Income: 80% Bond, 10% Large Cap, 3% Mid Cap, 2% Small Cap, 5% International; Balanced Conservative: 65% Bond, 15% Large Cap, 5% Mid Cap, 3% Small Cap, 7% International; Balanced: 50% Bond, 24% Large Cap, 7% Mid Cap, 4% Small Cap, 10% International; Balanced Growth: 35% Bond, 30% Large Cap, 9% Mid Cap, 6% Small Cap, 15% International; Growth: 20% Bond, 38% Large Cap, 12% Mid Cap, 8% Small Cap, 17% International; Aggressive Growth: 10% Bond, 40% Large Cap, 15% Mid Cap, 10% Small Cap, 20% International. You cannot invest in these indexes or averages and all above indexes/averages include a 5% allocation to the Treasury Bill Index, reflecting a nominal level of cash. The level of diversification represented by these benchmark averages may be materially different than actual client accounts; therefore, clients may experienced different levels of performance volatility. Past performance is no guarantee of future results.

Politics is not primary to portfolios. Data appearing to connect elections to market performance turn out to be weak.



Source: Bloomberg and GSAM.

The relationship between election outcomes and market performance is extraordinarily weak, statistically speaking.

The small sample size of US equity returns around US elections necessarily poses inherent limitations for those who would purport to assign advantage for one partisan outcome versus another. For these reasons, we believe investors should strive to separate their political views from their portfolios.

Selected Mutual Funds - Total Return Performance Summary

As of September 30, 2016

Bond Funds - Taxable	Style	3rd Qtr	YTD	12 Mths	3 Years	5 Years
Taxable Short-Term Bond Average		*0.5%*	*2.4%*	*2.0%*	*1.3%*	*1.7%*
Taxable Intermediate Bond Average		*0.8%*	*5.9%*	*5.2%*	*3.7%*	*3.2%*
Wells Fargo Ultra Short	AS	0.4%	1.4%	1.4%	0.7%	0.8%
AC Alternatives Market Neutral Value	AS	-0.5%	3.1%	3.0%	2.9%	N/A
Vanguard Short Federal	HS	0.1%	2.0%	1.6%	1.3%	1.1%
American Century Short Duration	HS	0.5%	2.3%	2.2%	1.5%	1.5%
Pioneer Short-Term Income	HS	0.6%	1.7%	1.6%	1.3%	2.0%
PIMCO Low Duration	HS	0.7%	1.9%	2.4%	1.3%	2.1%
Vanguard Short-Term Investment Grade	HS	0.6%	3.6%	3.3%	2.3%	2.5%
American Century GNMA Income	HI	0.3%	2.9%	2.7%	2.7%	1.9%
Diamond Hill Corporate Credit	LI	4.4%	11.0%	10.5%	5.4%	6.4%
Aberdeen Global High Income	LI	3.5%	7.4%	3.5%	0.6%	5.4%
Miller Convertible	LI	5.4%	8.3%	10.9%	5.9%	9.1%
Bond Funds - Tax Exempt						
Tax-Free Intermediate Bond Average		*-0.3%*	*3.1%*	*4.3%*	*3.8%*	*3.2%*
Vanguard Muni Limited Term	HS	-0.1%	1.4%	1.8%	1.7%	1.5%
T. Rowe Price Tax Free S/I	HS	-0.2%	1.3%	1.5%	1.6%	1.6%
Vanguard Muni Intermediate Term	HI	-0.3%	3.5%	4.9%	4.7%	4.0%
Vanguard Ohio Long-Term	HL	-0.6%	4.8%	6.8%	6.8%	5.2%
Stock Funds - Domestic						
S&P 500 Index		*3.9%*	*7.8%*	*15.4%*	*11.2%*	*16.4%*
Equity Fund Average		4.8%	*6.4%*	*10.7%*	*6.8%*	*13.5%*
Schwab Large Cap Growth	LG	6.0%	5.8%	12.1%	11.8%	17.1%
Wells Fargo Advantage Growth	LG	6.1%	3.5%	10.2%	6.0%	13.6%
Sit Dividend Growth	LV	3.1%	7.3%	14.3%	9.5%	14.4%
Hennessy Focus	MG	3.0%	4.4%	8.0%	8.9%	17.3%
Munder Mid-Cap Growth	MG	2.9%	4.4%	5.9%	5.9%	13.3%
John Hancock Disciplined Value Mid-Cap	MV	5.8%	9.1%	14.5%	11.8%	18.6%
SPDR S&P600 Small Cap Growth	SG	7.2%	11.4%	15.6%	9.3%	17.5%
Century Small-Cap Select	SG	5.9%	0.4%	2.9%	3.3%	11.8%
Neuberger & Berman Genesis	SB	4.2%	10.2%	13.3%	6.4%	13.4%
Diamond Hill Small-Cap	SV	3.4%	5.9%	4.9%	4.8%	13.1%
Wells Fargo Small-Cap Value	SV	8.0%	22.1%	30.0%	4.7%	10.6%
Stock Funds - International						
Morgan Stanley EAFE Index (Foreign)		*6.4%*	*1.7%*	*6.5%*	*0.5%*	*7.4%*
Harbor International	LV	6.0%	4.8%	7.8%	-0.6%	7.3%
Oakmark International	LV	13.3%	1.4%	6.7%	-1.2%	9.8%
Allianz NFJ International Value	LV	4.2%	-4.3%	-2.7%	-6.8%	2.2%
John Hancock International Growth	LG	5.2%	4.4%	9.2%	6.0%	11.7%
Thornburg Developing World	LG	5.6%	10.8%	13.2%	-1.4%	6.4%
Harding Loevner International Small Company	SG	4.6%	4.3%	11.1%	3.2%	10.1%
Stock Funds - Specialty						
Salient-Forward Select Income (REIT)	MV	4.5%	13.8%	15.7%	9.6%	11.3%
Neuberger Berman Real Estate Securities	MV	-1.9%	8.5%	17.1%	11.6%	13.4%

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Powell, Ohio 43065
Ph: 614.389.4646
Email: info@nvestwealth.com

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RE: Request Current Disclosure Form ADV Part II

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PERSONAL FINANCE: TAX PLANNING STRATEGIES FOR YEAR-END

Now is the time to implement smart tax strategies that can save you money and/or prepare you for a less-stressful tax-filing experience next spring. As we emphasize to clients, we experience two enemies to investing and building net worth – inflation and taxes. Both erode the long term accumulation and value of savings and investments. Thus, being smart with how one accumulates and invests their savings ("life effort compressed") is being a smart and wise steward. Year-end (before 12/31) is tax planning season; but all year is tax awareness season. The US tax code is complex, but offers many ways to reduce taxes. It is legal, correct, and prudent to pursue various tax saving strategies, as both individuals and businesses attempt to minimize their tax liability (not maximize it). Again, paying taxes is our responsibility, yet it is also one of our biggest enemies to growing our savings, investments, and net worth. Below are several tax reducing strategies to consider – we utilize several of them when working with clients and investments.

- Defer receipt of income – if offered the choice of receiving a bonus at year-end or in January, if you know your income and tax rate, and the level of income that would cause the tax rate to be higher, you may want to delay receipt of the bonus until next year. Why pay a higher tax rate on additional income?
- Bunch your deductibles – if earned income is high, consider pre-paying real estate taxes or making charitable gifts ahead of time, to aid reducing current year tax liability (this is the opposite strategy concept to above, deferring income). Itemizing your deductions may provide a greater tax liability reduction than taking the standard deduction; always take the greatest deduction to save paying taxes.
- Contribute to your 401k or IRA – putting money into retirement savings is a good tax reduction strategy; pretax contributions lower your taxable income. Regular contributions to retirement accounts boost your flexibility in retirement. Withdrawals of retirement account savings in retirement are often at lower tax rates than when working/earning higher income.
- Donate to charities – gifting money to a charity is tax deductible. Consider donating highly appreciated stocks from a personal investment account to charity instead of cash. As an example: Gift $1,000 of stock (paid $200 for it years ago), and put the $1000 cash back into your personal account to reinvest. Receive the $1,000 charitable gift deduction and avoid incurring capital gains taxes of $800.
- Consider Qualified Charitable Distributions – if you are over age 70.5, consider distributing monetary gifts to charities directly from your IRA. This type of distribution (QCD) to a charity from your IRA avoids the distribution being counted as income and is valuable if you are unable to itemize deductions (losing tax benefit of giving) or are worried about preserving eligibility for deductions/subsidies subject to income phase-outs.
- Harvest investment losses against investment gains – throughout the year, in the course of managing personal investment accounts, we capture losses to offset realized gains where possible. The purpose is to minimize capital gains and taxes due thereon. Sometimes, when the bear in the market is decreasing asset values, it is wise to harvest losses to store-up or carryforward to future years, which can then be used to offset capital gains.
- Sale of primary home – owners are permitted a one-time life exclusion on the appreciated value of the primary home when it is sold, wherein you do not pay a tax on the appreciation of value from the original purchase price (plus improvements).
- Asset exchanges to defer taxes – use of 1031, 1035 tax exchanges should be reviewed before changing real estate or annuity investments into another like-kind investment. Why pay taxes before you start to use the value of the investment?

There are many more valuable tax reducing strategies. Check with your tax accountant well in advance of the year-end. Understand tax strategies before making important financial decisions, as paying taxes reduce the asset value. As we work with clients, while we are not tax CPAs, we are very aware of taxes being a big enemy to clients' wealth goals. We pursue and advocate utilizing tax reducing strategies to boost your path toward growing your net worth. Tax minimization actions are prudent, legal pursuits. You should be tax aware with your financial decisions.

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