Churchill Management Group

Monthly Market Update

February 6, 2018

TACTICAL STRATEGIES

PREMIER WEALTH TACTICAL & PREMIER WEALTH TACTICAL CORE

Rest assured, we are monitoring the market and our indicators very closely. While in this environment it is possible that you may see us raise some level of cash, it's important to keep the following in mind.

After a prolonged period of calm one-way action, (311 sessions without a 3% decline!), volatility appears to be back. The major indices have fallen sharply to begin the month with a drawdown of 9-10% already. Most of the pullback happened over two days with the DJIA falling 665 points on Friday followed by a record 1175 points on Monday. While the 1175 points is a large number, it is important to remember that in percentage terms, the 4.6% decline barely cracks the top 100 in history. In fact, while investors have been accustomed to the historically low volatility environment over the last year, volatility is quite normal. It is not unusual for declines like this to be followed by rallies, regardless of the ultimate direction of the markets. However, it may be time to get more defensive the technical structure has weakened. Whether the market finds its legs or ends up in a Bear Market, it is always a process. That should give us an opportunity to adjust our exposure.

The new year got off to a strong start with one of the best Januaries in decades, as the Dow (+5.8%), S&P 500 (+5.6%) and NASDAQ (+7.4%) all showed big gains for the month. But that run-up, on top of a bull cycle that is now nearly nine years old, left the markets extremely stretched. February has kicked off with our first real sell-off in over a year, prompted by a rise in yields that has 10-year treasuries trading at four-year highs.

On the technical side, while sentiment and fundamental indicators remained at elevated levels, breadth confirmed the market highs reached last month. Every bear cycle since the 1980s was preceded by a breadth divergence, but we have yet to see one in the current environment. The rally has been broad, with the vast majority of stocks participating. Leading sectors (Tech and Financials) have been holding up well even through Monday, although we have noted that the

number of stocks making 52-week lows has picked up. The big change is that some shorter-term moving averages have been broken while some trendlines are being tested.

In terms of fundamentals, corporate earnings have been very positive. With over 50% of S&P 500 companies reporting Q4 numbers, 75% delivered positive earnings surprises and 80% showed positive revenue surprises, according to Factset. The newly passed reductions in corporate tax rates should continue to drive profits. Unemployment remains low, while valuations are still historically high. The Federal Reserve, now chaired by Jerome Powell, has been ramping up its balance-sheet tapering and raising interest rates, with three more hikes expected this year.

We have been in a later-stage technical rally. Of course, with the recent volatility, this may change. With Monday's sell-off, the technical indicators are now mixed but most leaders have held up well. The market faces potential headwinds, including any missteps by the Fed (i.e., raising rates and reducing its balance sheet too aggressively) and any disruptive geopolitical events. For now, one view is that the market has begun a consolidation phase and is digesting the recent gains. Such behavior is healthy and to be expected. However, since our fundamental and sentiment indicators are already at riskier levels, should our technical gauges turn negative or our individual positions and leading stocks break down further, we may take a more defensive stance. But for now, it's too early to tell if the uptrend has more legs or if it will stumble into an extended correction.

TACTICAL OPPORTUNITY

2018 got off to a solid start, and despite the choppiness and selling pressure we've seen over the last two weeks, the portfolio is looking good, boosted by good starts in the new year by Netflix, Amazon, Workday, and Mastercard. We will continue to monitor market volatility closely, but for now we are comfortable staying mostly fully invested, with perhaps some minor selling.

FULLY INVESTED

ETF SECTOR ROTATION

After already moving out of the consumer holdings a couple of months ago, there were no significant changes in January. The model unfortunately exited the Consumer Discretionaries, which have rallied behind Amazon, but is happily out of Staples, which have lagged. Along with Discretionaries, Health, Tech and Financials have all outperformed since the start of the year. We

remain overweight in each, along with Materials and Industrials. Utilities got off to the worst start, down 5% for the year, along with Energy, which is now lagging. We are underweight in both. For the broad markets, growth continues to outweigh Value, and Large caps are slightly outperforming Small caps. We continue with a green light on our international holdings.

EQUITY GROWTH AND VALUE

For the past two years, our mantra has been "doing as little as possible pays the best." Housing and Industrial holdings have been a bit weak, but have been offset by Tech, Healthcare and Amazon. The plan for now is to stick with our aforementioned mantra.

EQUITY DIVIDEND INCOME

No significant changes to the portfolio so far this year. The group has held up relatively well despite the recent rise in interest rates, as the Fed voted in three hikes last year in March (1.0%), June (1.25%) and December (1.5%). Utilities holdings have been under pressure as a result of those rate increases, but were offset by the rock star performances of AbbVie, Boeing and Lockheed to start off the year.

For a full description of each strategy, please click here.

Best regards,

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