

Quarterly Client Update

2018 Q4

December 31, 2018



NorthCoast 
Asset Management

President's Post Insight from NorthCoast President & CEO, Dan Kraninger

“To different minds, the same world is a hell, and a heaven.” - *Ralph Waldo Emerson*



I was in Epcot on New Year's Eve last week (I know I may need my head checked) and as I was sitting in England enjoying a Bass beer, I watched as a mid-40s man began yelling at a trash collector. He was screaming simply because there were no seats available. His meltdown lasted about 2-3 minutes, and then he seemed to come back to his senses, relent to the fact that the park was packed and that this was supposed to be the happiest place on earth.

What has amazed me for decades is to see similar fits take place on Wall Street. Group think takes over most often when motivated by fear or greed. Appropriate to cite our partner, Bill O'Neil, who often said, "the market is human nature on parade."

When I wrote my 3rd quarter letter I really didn't expect my comments about market declines to be that timely. But in the 4th quarter we saw the Dow decline -18.8% and the S&P 500 -19.7% (high to low). So by my count, since 1900 the market has now corrected 154 times. A correction is anywhere between -5% to -19.9%. That means the frequency is a little over once a year and interestingly the average length of recovery from the bottom is 4 months. We have 118 years of data that suggest people freak out, hit the panic button, and then regret the decision 4 months later. And despite all of this information, why do investors continue to fall into this pattern? It's because they fear things will worsen.

20 times since 1900 markets went beyond -19.9% and fell into bear markets. Bear markets last longer and decline more. The key, as I mentioned three months ago, is differentiating between the two. Two dimensions that we find very useful in making that decision when prices decline like this is macro-economic data and valuation measures. Together they make up 50% of our market forecast and right now both are ok. On the macro front: jobs - good; GDP - good; inflation - good; industrial production - good. On the valuation front: everything is better after the decline; comparing the market to alternatives like bonds - good; P/E multiples - better. Our view of the market right now is one that looks like 2011 or 2015. If the Fed slows and if the U.S. makes a deal with China, the bulls could even be let loose. Take a look at the table below for some additional comparisons.

	2011 Q3	2015 Q3	2018 Q4
	Spanish and Italian debt plummet on fear of default Stand and Poor (S&P) downgrades U.S. debt rating from AAA to AA+ Unemployment rate disappoints at 9.1%	Chinese economic growth slows Oil drops below \$30 per barrel Russel 2000 Index drops into bear market down -22% from its previous high	U.S. - China trade dispute Government shutdown Rising interest rates Brexit negotiations
S&P 500 Index	5/11/11 - 2/2/12	7/21/15 - 4/15/16	8/30/18 - 12/31/18
Days to Reach Bottom	154	143	?
Days to Recover	123	63	?
Total Days	276	206	?
Worst Day	-6.6%	-3.9%	-3.3%
Max Drawdown	-18.6%	-13.0%	-19.7%

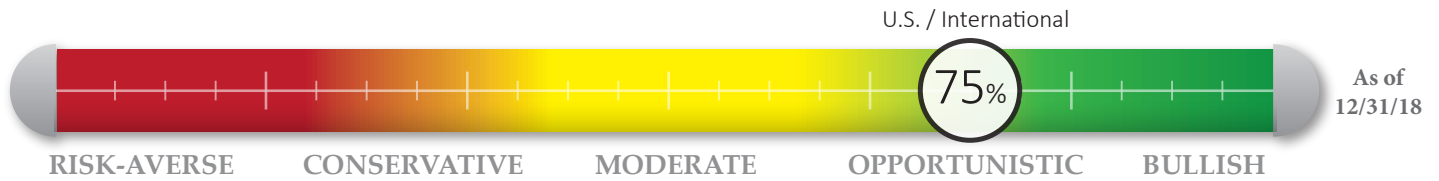
Source: Bloomberg. Past Performance is not indicative of future results. All investments involve risk, including loss of principal.

We, of course, are data dependent. We measure daily and adjust if needed along the way. But, as of now, we are optimistic about market gains in 2019. Indicators are betting that this correction is more like the temper tantrum in Disney... burning hot and then recovering to recognize the economy is good and prices are reasonable.

Let's say good bye to 2018 - a year of digesting previous gains, a year where cash was king and nothing made money - bonds, stocks, alternatives nor commodities. I'm proud that our flagship tactical strategies delivered a market-beating result but it's hard to be enthusiastic when other strategies struggled. As always, thank you for your business and best wishes for a happy, healthy, and prosperous 2019.

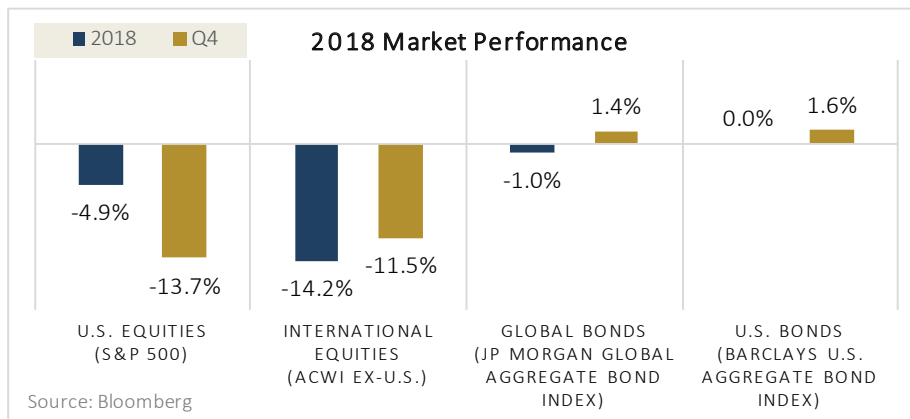
NorthCoast Navigator

The NorthCoast Navigator is a market "barometer" displaying NorthCoast's current equity outlook. This aggregate metric is determined by multiple data points across four broad dimensions including Technical, Sentiment, Macroeconomic, and Valuation indicators. The daily result determines equity exposure in our tactical strategies.



What happened in the 4th quarter?

Rising interest rates, a stronger dollar and continued escalation of trade conflicts with China could have all attributed to falling stock prices as investors reevaluated their outlook on future growth. Along with the stock market's decline was an unusual concurrent drop in bond prices, putting most diversified portfolios in a difficult position. The third quarter's earnings season brought about some fears that corporate earnings may have peaked as the effects of the corporate tax cut faded and general concerns over the economy were raised. Major U.S. indices such as the S&P 500 and Dow Jones Industrial Average suffered their worst December since 2008. The Federal Reserve raised the target rate by 0.25% at their December meeting, continuing to push interest rates higher. The move typically leads to higher consumer and business lending rates, therefore escalating concerns of slowing future economic growth. Though not enough to erase the monthly and yearly losses, stocks moved higher in the final week of the year.



Moving into 2019

NorthCoast entered December with 30% cash in its U.S. tactical equity strategies and reached a high cash level of 35% after the 1st week of trading. Then we marginally increased our equity exposure as valuations became more attractive along with the lack of real economic data warranting a substantial decline. We enter 2019 approximately 75% invested in our U.S. and international tactical equity strategies. We will keep a close eye on any major developments along with key economic data and Q4 earning reports released in the coming weeks.

TECHNICAL

The S&P 500 Index declined through traditional support levels as the 50-day, 100-day and 200-day moving averages are -6%, -9% and -9%, respectively. The VIX (volatility) increased to its highest level in 2018 to 25.4.

SENTIMENT

Investment flows into U.S. index fund SPY were slightly negative while the AAI investor survey (a contrarian indicator) saw a major increase in bear market sentiment, up to 50.3 from 39.5 last month.

MACROECONOMIC

Unemployment rate remained at multi-year low of 3.7%, while the economy continued to add jobs, +155,000 in November. Industrial production rose 0.6% and wage growth (average hourly earnings) increased 3.1% over the previous year.

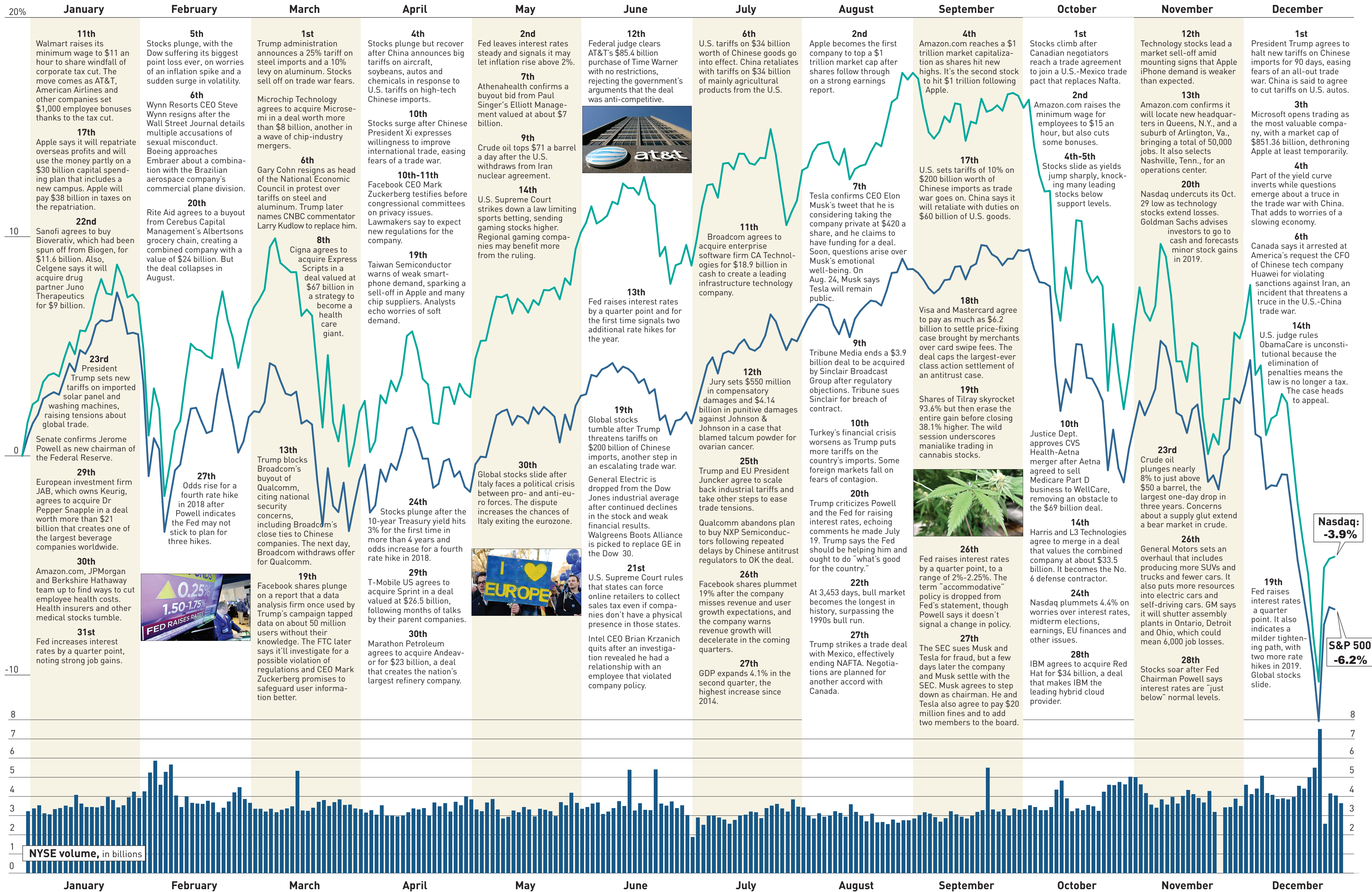
VALUATION

Equity valuations (S&P 500 P/E multiples) declined to 17.1 with Forward P/E to 15.4, their lowest levels in over a year. Rising interest rates presented competitive opportunities as investors sought higher yield in new bond offerings.

Data as of 12/31/2018. Data provided by Bloomberg, NorthCoast Asset Management.

2018: Volatility Came Back In Force As The Market Corrected Twice

Trade wars, interest rates and other worries overshadowed a strong year for profits and the economy



Strategy Performance

NorthCoast offers a suite of active investment strategies designed to meet the individual goals and objectives of the investor. Our dedicated advisory team will work with you to construct a portfolio catered to your needs.

	STRATEGY	OVERVIEW	2018	
Risk-Adjusted "Tactical"	Designed to first analyze market risk then determine the desired asset allocation and security selection	CAN SLIM*	Tactical All-Cap Growth	-2.1%
		CAN SLIM* <i>International</i>	Tactical All-Cap International Growth	-10.8%
		CAN SLIM* <i>Global</i>	50% CAN SLIM* / 50% CAN SLIM* International	-6.4%
		Tax-Managed	All-Cap U.S. Growth	-4.2%
		Tactical Growth •	Tactical Global Asset Allocation	-9.2%
		U.S. Sector Select Hedged •	Tactical U.S. Sector Allocation	-2.0%
		International Select Hedged •	Tactical Country Rotation	-2.1%
Growth	Seek to generate growth returns greater than the respective market benchmark	Legends Value	All-Cap Value	-17.5%
		United Portfolio	50% Legends Value / 50% CAN SLIM*	-10.1%
		Vista	All-Cap Growth	-16.1%
		Global Select •	Global Country Allocation	-10.2%
		U.S. Sector Select •	U.S. Sector Rotation	-9.4%
		International Select •	International Country Allocation	-15.5%
		Emerging Market Select •	Emerging Market Country Allocation	-14.0%
Core	Designed to meet the broad goals of growth and income and serve as the 'core' of a portfolio	Diversified Core •	Global Asset Allocation	-7.4%
		Diversified Growth •	Global Asset Allocation	-8.7%
		CAN SLIM*: <i>Growth & Income</i>	75% CAN SLIM* / 25% Bond ETFs	-2.2%
		CAN SLIM*: <i>Balanced</i>	50% CAN SLIM* / 50% Bond ETFs	-2.2%
Income	Designed to generate yield and returns through traditional and non-traditional income sources	Core Fixed Income •	Conservative Income	-1.8%
		Tactical Income •	Dynamic Income	-3.8%
		Aggressive Income	Aggressive Income	-2.2%
Alts	Aim to generate returns that are independent of the equity and fixed income markets	Zero Beta	Liquid Alternatives	-4.7%

• = ETF Managed Strategy

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Returns are presented net-of-fees. Net-of-fee returns are reduced by trading costs and the portfolio's actual management fee. Valuations are computed and performance is reported in U.S. dollars. A complete list of composite descriptions is available upon request. Policies for valuing portfolios, calculating performance, and preparing compliant presentations are available upon request. To obtain a compliant presentation for the associated strategy, please contact one of our advisors at 800.274.5448.

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