



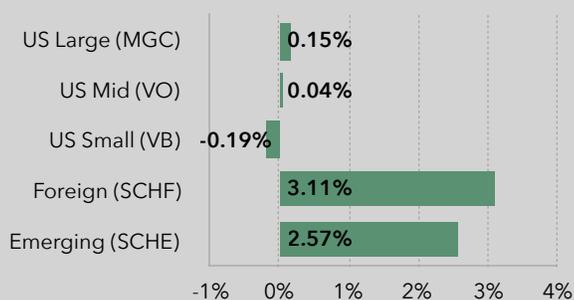
March 2017

Economic Data

- Only 98,000 jobs were added in March, because weather; the unemployment rate fell two-tenths to 4.5%, the lowest level since April 2007
- Existing home sales were soft, down 3.7% in February
- Year-over-year inflation (CPI) rose to 2.74% in February, which we expect will be the top for the near-term
- Retail sales growth fell to 0.1% in February, with motor vehicle sales continuing to decline

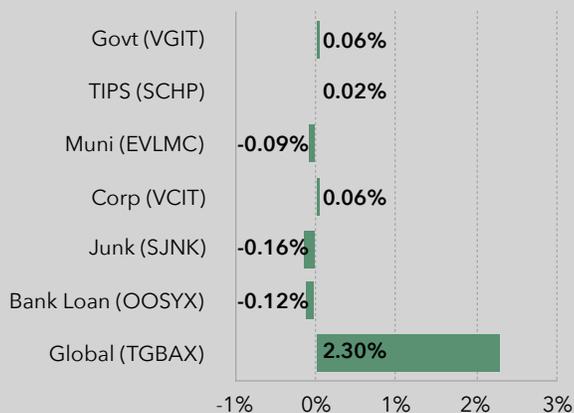
Stocks

March Returns



Bonds

March Returns



Alternatives

March Returns



Performance data provided by Morningstar.

The brain uses two systems to process information. The first type is intuitive but lazy, rapidly forming judgements with no conscious input. The second system is slow, reflective, and is not guided by emotions. It is that second system – type 2 – that we want in control of our investment portfolios.

Peak Auto

Twelve years ago I moved away from the U.P. of Michigan (located just north of da bridge, just south of heaven) to what I thought was the biggest city in the world at the time... Minneapolis. This exciting and vibrant place introduced me to so many new and exciting things. Butter sculptures, hamster tunnels, and cheeseburgers with the cheese *inside* the meat! There were even these things called hipsters, who served the sole purpose of making my beer choices seem cool and kitschy, instead of economically motivated.

The most foreign thing about my new environment, though, was public transportation. This place had buses. Lots of them. And it even had a light rail train that ran from downtown to the airport and the Mall of America. I grew up in Michigan, where the closest thing we had to public transportation was the Detroit People Mover. There are many reasons why the People Mover gets mocked, but for me it's the simple fact that the furthest any one station is from any other station on the loop is about three-quarters of a mile, which only takes about 15 minutes if you are walking. A lap on the People Mover, on the other hand, takes about 16 minutes.

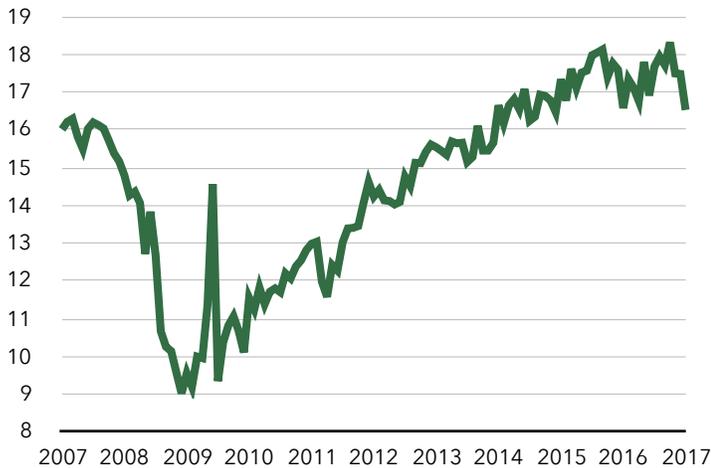
There have been and are many forces at work, I'm sure, as to why public transportation isn't yet a viable alternative to owning a car in Michigan, but our love affair with cars and an economy that relies on making them might be number one. My dad worked for GM for thirty years, and mom did a couple stints there as well. We had more cars in our garage and driveway than we had members of the family. I grew up loving cars.

So when I thought about getting rid of my car, it was scary at first. Before deciding to go through with it, I tried to go a month without using it. I survived without much trouble, so at the end of the month I got rid of my 1996 Oldsmobile Bravada. For you younger folk, Oldsmobile is a defunct division of GM that's primary function was to take Chevrolets and Pontiacs and just slap a different badge on them and pretend like they designed a whole new vehicle. My Bravada, for example, was just a Chevy Blazer with ribbed cladding on the body panels and a different grill.

According to AAA's 2016 *Your Driving Costs* study, the average cost of vehicle ownership in the U.S. is \$8,558 (includes financing costs, depreciation, maintenance, tires, gas, insurance, license & registration). The decision to go without a vehicle may have reasonably saved me \$100,000 over the course of the past twelve years. Yes, I realize there were bus passes and taxi rides and Ubers, but there are also things like parking costs and speeding tickets that weren't addressed in the above figure. So there.

I thought I was ahead of the curve on this one, and the trend would be for others to follow my example. It made sense. More people are living in cities where there is public transportation, and the emergence of the sharing economy brought us things like Uber and Lyft. Soon everyone would be abandoning their cars!

Light Weight Vehicle Sales (Millions, Annual Rate)

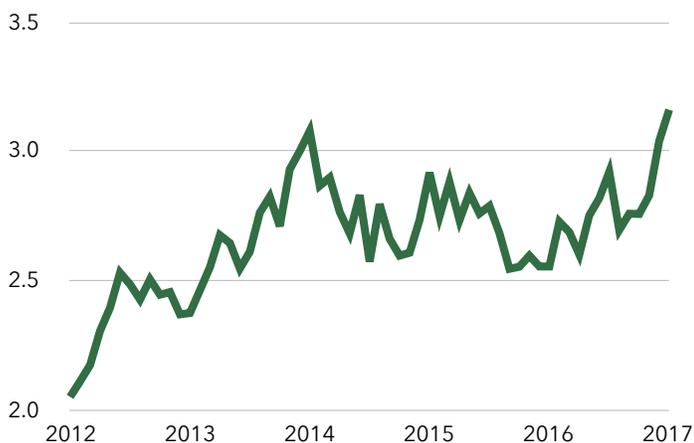


Source: U.S. Bureau of Economic Analysis

But it didn't really happen that way. Sure, sales fell off a cliff in '08, but we were in a recession. And millennials haven't been buying as many cars as my generation did at their age, but that's mostly because they can't afford it.

Sales have steadily marched upward for the past eight years, but it appears we may have hit an inflection point. The annual rate of light vehicle sales has fallen a sharp 9.77% over the past three months, and dealer inventories are rising.

Auto Inventory/Sales Ratio



Source: U.S. Bureau of Economic Analysis

I believe there is a case to be made that the auto cycle's peak is behind us. Worse yet, there is the potential for a mini debt crisis tied to all the subprime loans that have been written to drive auto sales to this point. Delinquency rates are now at their highest levels since 2009, according to Fitch.

According to Experian and Morgan Stanley Research, the average loan term length has increased six months over the past seven years. In the 4th quarter of 2016, the average new car loan was termed out to 68 months and average used car loans were termed out to 63 months. The problem this often creates is the vehicle depreciates faster than the loan amortizes, resulting in negative equity. In these situations, one of three things will typically happen

- The car owner continues making payments on a vehicle that is worth less than what is owned on it
- The car owner stops making payments, as more than one million Americans have already chosen to do, according to the Financial Times analysis of TransUnion data
- The car owner trades the car in for another vehicle, and the negative equity is tacked on to the new loan, compounding the problem (I believe this at least partially explains the graph below)

Average Amount Financed for New Car Loans at Finance Companies



Source: Board of Governors of the Federal Reserve System (US)

Binge Box

A Series of Unfortunate Events

Neil Patrick Harris, or NPH as this national treasure is affectionately referred to, stars in the television adaptation of the children's novel series written by Daniel Handler under the pen name Lemony Snicket. The show devotes two hour-long episodes to each book in the series, with the first season covering the first four of 13 books. This effectively makes it the equivalent of four feature length films.

The stories are engaging, the writing is enjoyable, and the acting is fun to watch, but what really makes this series is the set designs. I'm not sure I've ever praised a work of film or television for that before, but Bo Welch did just an amazing job on this! The sets are a fanciful display of his creativity and imagination.

I expect to see more headlines about this in the next year or two. It could cause a lot of pain for companies like Santander Consumer Holdings USA (ticker: SC) and Ally Financial (ticker: ALLY) that built their businesses around automobile financing.

Portfolio Positioning

The S&P 500 hit an all-time high a hair above 2,400 to kick off the month of March, but has been in a mild downward trajectory since. There are a lot of risks out there to choose from:

- According to Yardeni Research, S&P 500 companies spent 101.3% of their operating earnings on share buybacks and dividends in the 4th quarter of 2016. It should be self-evident as to why this is not sustainable
- Trump tax reform not looking good after failed repeal of Obamacare
- War with Syria? North Korea?
- Brexit is official as Theresa May has triggered Article 50 and officially begun the two-year negotiation of the UK's departure from the EU
- The French presidential election commences on April 23, and an unlikely yet plausible Le Pen victory has markets nervous

In light of all this, we remain dialed back on risk in portfolios.

Ryan P. Layton, CFA

p: 612-810-2230

e: ryan@emeraldspark.com

Tactical Asset Allocation					
Asset Class	Heavy Under-weight	Under-weight	Neutral	Over-weight	Heavy Over-weight
Cash				●	
Fixed Income		●			
Core Domestic		●			
TIPS					●
US High Yield	●				
Bank Loans				●	
Foreign Bonds			●		
Equities		●			
Large Cap		●			
Mid Cap		●			
Small Cap		●			
Developed Intl.		●			
Emerging		●			
Alternatives				●	
Real Estate		●			
Commodities					●
Hedging					●

About EmeraldSpark

EmeraldSpark Investments, LLC is a Registered Investment Adviser based in Chicago, IL. We were founded by Ryan P. Layton, CFA in 2015 to provide outsourced investment management services to community bank trust departments and independent trust companies, as well as fiduciary investment management for select individuals. Our investment process blends the foundations of Modern Portfolio Theory with the latest research in the field of behavioral finance. We specialize in asset allocation and investment due diligence to help provide our clients with investment strategies personalized to match their specific goals and risk comfort zone.

This Newsletter has been prepared by EmeraldSpark Investments. Information contained within has been obtained from sources believed to be reliable, but we do not guarantee its accuracy, completeness or fairness. Views and opinions expressed are for informational purposes only and do not constitute a recommendation by EmeraldSpark Investments to buy, sell, or hold any security. Views and opinions are current at the time of writing and may change. Before acting on this material, you should consider whether it is suitable for your particular circumstances and, if necessary, seek professional advice. Past performance is not indicative of future results. **NOT FDIC INSURED | NOT BANK GUARANTEED | MAY LOSE VALUE**

