



Richard Bernstein, Chief Executive and Chief Investment Officer

Richard Bernstein Advisors

Richard Bernstein Advisors LLC (RBA) is an independent investment adviser focusing on longer-term investment strategies that combine top-down, macroeconomic analysis and quantitatively-driven portfolio construction. We strive to be the leading provider of innovative investment solutions for investors, and our competitive edge is our research-driven macro style of investing.

Our top-down macro approach differentiates our firm from the more common, traditional bottom-up approach of most asset managers. Our extensive array of macro indicators allows us to construct portfolios for clients that are innovative, risk-controlled, and focused on overall portfolio construction instead of individual stock selection.

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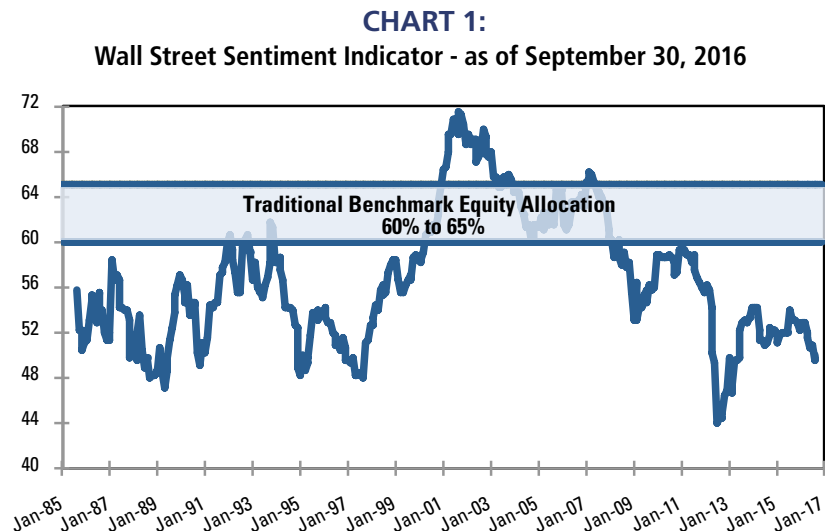
It Ain't Just the Fed

It seems unprecedented to us that the US stock market is in the 7th year of a bull market and investors generally remain too fearful to invest in equities. The data clearly show that not only are individual investors cautious, but so are pensions, endowments, foundations, and hedge funds. Investors are typically quite bullish by this time in the bull market, but that does not appear to be the case today.

Our "Year Ahead" report for 2016 was titled "Mute the TV" www.rbadvisors.com/images/pdfs/2016-Mute the TV.pdf. We highlighted last December that 2016 was a Presidential election year, and that investors could potentially be overwhelmed by political propaganda. The key to investing in 2016 would be investors' ability to sift through all the election-related noise and invest based on fundamentals.

Our guess is that few investors realize that the S&P 500® has appreciated more than 15% in the past year (through September 30), and those that realize stocks have performed so well feel that an impending bear market will be worse because it hasn't happened yet. It is inconceivable to investors that the US bull market has been and continues to be justified by fundamentals.

This overwhelming bearish sentiment is supported by data. All the groups mentioned above have been net sellers of equities during this bull cycle according to data from Bank of America/Merrill Lynch¹. In addition, Chart 1 points out that Wall Street has been recommending that portfolios have underweighted positions in equities throughout the bull market. This may be more typical than one might at first realize; Wall Street also recommended underweighting equities throughout the entire bull market of the 1980s and 1990s.



Source: Richard Bernstein Advisors LLC. ¹BofAML Equity Client Flow Trends, 8/23/16

Blaming, not crediting, the Fed for the bull market?

It has been popular among bearish observers to blame the bull market on the Fed. They feel the Fed is artificially pumping up asset prices. First, we think such comments constitute a rather obvious sentiment barometer. Investors do not believe the stock market should appreciate, but the bull market continues to defy their bearish forecasts. Rather than altering their asset allocations, investors have so much conviction in their fears that they are actually “blaming” the Fed for a bull market. This is highly unusual because historically investors thanked the Fed, rather than blamed the Fed, for bull markets. The constant negative consensus regarding equity returns suggests the current bull market could still have a considerably longer life than most investors expect.

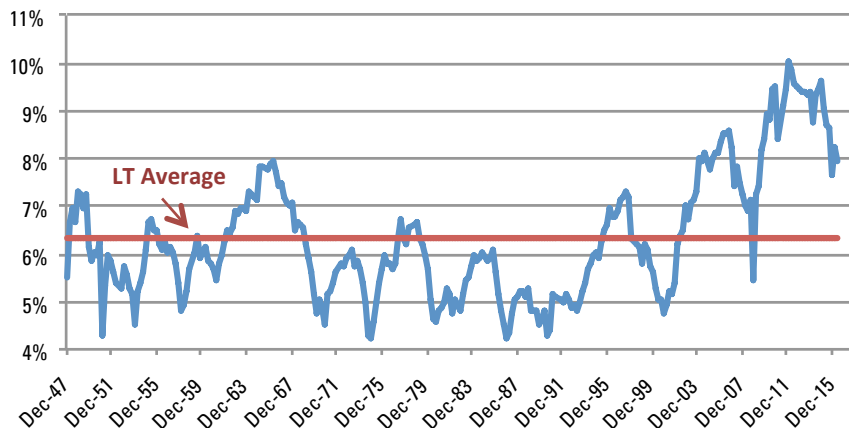
Don’t forget earnings!

Many investors have dismissed our bullish views because they believe there is nothing fundamental behind the bull market. This is simply not true. Fundamentals have improved dramatically, and have been a major support to the bull market.

Chart 2 shows corporate profits’ proportion of GDP through time. Although there are some quirks to these particular figures, one should focus on the trends in the data rather than on the numerical figures. As one can see, corporate profits became the largest proportion of GDP ever in history. One certainly would have been bullish a decade ago if one had posited that corporate profits would be the fastest growing portion of national income.

The chart strongly supports the notion that the bull market is not solely attributable to the Fed simply inflating the value of financial assets. Rather, it suggests that the constitution of the current bull market is much more normal than bulls would suggest. Most bull markets are comprised of the combination of central bank liquidity, improving fundamentals, and negative sentiment. All three have been present during this bull market.

CHART 2:
US Corporate Profits *as a Percentage of GDP
(4Q 1947 – 2Q 2016)



Source: Richard Bernstein Advisors LLC, BEA
 *US Corporate Profits after tax with IVA and CC Adjustments

When do bear markets start?

We recently read yet another article of a famous investor risking his entire hedge fund on massively bearish positioning. Although we don't for a second doubt that there will be bear markets in the future, such extreme pessimism seems premature to us until the typical bear market signals begin to appear.

The three major signs that the probability of a bear market is increasing have historically been:

- 1. The Fed and other central banks withdrawing liquidity from the global economy.**
- 2. Profits recession.**
- 3. Overly bullish sentiment.**

None of these are present today. Although the Fed is considering raising interest rates for the second time in this tightening cycle, there is little evidence that global liquidity will be constrained. Rather than entering a profits recession, the US profits cycle is in a recovery phase and the stock market's leadership has shifted away from defensive sectors toward cyclical ones. Chart 3 shows S&P 500® sector performance since the February market trough. As we pointed out earlier, sentiment remains quite bullish as it is very hard to find any data that suggests investors are euphoric about investing in US stocks.

CHART 3:
S&P 500® Sector Performance from Feb 11th Market Trough



Source: Bloomberg Finance L.P

It's just a bull market. Get over it.

When we formed Richard Bernstein Advisors in 2009, we highlighted that we thought the US equity market was entering one of the biggest bull markets of our careers. The current bull market is now the second longest bull market in the post-war era, and we still feel the bull market will be one for the record books by the time it is over.

The notion that the only reason the stock market has appreciated is because of the Fed seems blatantly untrue to us, and ignores the significant improvement in fundamentals during this cycle. Investors will eventually get over their fears and realize that it is simply a bull market, but that doesn't seem to be happening yet. For the time being though, fear continues to dominate.

If you would like to learn more about how these views are incorporated into RBA's portfolios, please contact your local RBA representative (http://www.rbadvisors.com/images/pdfs/Portfolio_Specialist_Map.pdf).

INDEX DESCRIPTIONS:

The following descriptions, while believed to be accurate, are in some cases abbreviated versions of more detailed or comprehensive definitions available from the sponsors or originators of the respective indices. Anyone interested in such further details is free to consult each such sponsor's or originator's website.

The past performance of an index is not a guarantee of future results.

Each index reflects an unmanaged universe of securities without any deduction for advisory fees or other expenses that would reduce actual returns, as well as the reinvestment of all income and dividends. An actual investment in the securities included in the index would require an investor to incur transaction costs, which would lower the performance results. Indices are not actively managed and investors cannot invest directly in the indices.

S&P 500®: Standard & Poor's (S&P) 500® Index: The S&P 500® Index is an unmanaged, capitalization-weighted index designed to measure the performance of the broad US economy through changes in the aggregate market value of 500 stocks representing all major industries.

About Richard Bernstein Advisors

Richard Bernstein Advisors LLC is an independent investment adviser. RBA partners with several firms including Eaton Vance Corporation and First Trust Portfolios LP, and currently has \$3.1 billion collectively under management and advisement as of September 30th 2016. RBA acts as sub advisor for the Eaton Vance Richard Bernstein Equity Strategy Fund and the Eaton Vance Richard Bernstein All Asset Strategy Fund and also offers income and unique theme oriented unit trusts through First Trust. RBA is also the index provider for the First Trust RBA American Industrial Renaissance® ETF and the First Trust RBA Quality Income ETF. Additionally, RBA runs ETF asset allocation SMA portfolios at UBS, Merrill Lynch, Morgan Stanley Smith Barney and on select RIA platforms. RBA's investment insights as well as further information about the firm and products can be found at www.RBAdvisors.com.

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