WOLVERINE INVESTMENTS
YIELD-ENHANCED STRATEGIES

December 19, 2016

"The Holiday Season is when you buy this year's gifts with next year's money"

While we could not identify the author for the above caption, given what's been happening in the ebullient stock market lately, the same sentiment could be attributed to today's giddy investor who unabashedly began shopping the market on November 9th based purely on the ***hope*** of things to come. Hope that Congress will go along with Donald Trump and support a massive infrastructure spending project. Hope that a convoluted tax system will be reformed to be more favorable to corporate America. Hope that government regulations and bureaucracy will be rolled back to make it easier to transact business. Among others, any one of these hoped for initiatives might justify the marking up of this year's abundant stock market values.

What the markets seem to be confirming is that the soon-to-be political reality will be a long-term positive for the U.S. economy – but we'd be lying were we to say that we anticipated a Trump victory ***coupled*** with a Republican-controlled House and Senate. Regardless of where your opinion rests with the candidates or the election outcome, sweeping policy changes are looming and markets are celebrating the gifts of the season with little regard for how such policies will be legislatively debated and signed into law. So who, or more accurately, ***where***, has the money come from to pay for the stock market's recent immediate gratification.

As the so-called *"re-allocation trade"* aptly suggests, there has been a tumultuous shift away from *"safe"* fixed income investments into *"riskier"* equity investments. As part of this *"risk on"* trade, a panic among short-sellers to cover their borrowed positions has added fuel to the fire that ignited the election tinderbox. What cannot be ascertained as of this writing is whether any new money is being allocated to the stock market. One thing is for sure, flexible and uncorrelated strategies that do not abandon the generation of income will continue to have a key role in effectively navigating the changing tide of the markets.

Renewed Case for Convertible Securities Strategies

Unchanged in our investment approach is our commitment to boosting portfolio income through the significant use of convertible securities when constructing our client portfolios. Likewise, our pledge to sound risk management remains a cornerstone of our investment philosophy. To that end, how do we see the anticipated environment affecting our strategies?

There are three broad themes that we feel will impact the overall markets and ultimately the rational for our use of convertible securities – ***the Federal Reserve's policy to methodically move away from an accommodative monetary policy; President-elect Donald Trump's move to 1600 Pennsylvania Avenue; and the end of the 35 year bull market in bonds.***

While we cannot do each of the above themes justice without an exhaustive doctoral dissertation, we can observe potential opportunities for employing convertibles as our preferred investment vehicle. For example, a rising rate environment should prompt the growth of convertible issuance as corporations will, ostensibly, move away from traditional debt financing to keep their cost of capital as low as possible. Further, convertibles have historically been less sensitive during periods of rising rates. The advent of *"Trumponomics"* will not forestall the return of market volatility. To the contrary, while we view Trump's proposed policies as a *net positive* for business (and ultimately the economy), asset classes which have traditionally offered an element of safety during times of volatility will face downside pressure. This begs the question, *"Where does the conservative investor go to seek a modicum of safety?"*

For the better part of 60+ years, yields on highly rated corporate bonds and U.S Treasuries have ranged from 4-8%, and we believe that we have begun the climb back into this range – putting pressure on valuations. As such, we believe our strategies will offer a superior alternative to traditional fixed income, and that we are well-positioned to withstand the anticipated gyrations to the overall economy. As validation of our thinking, we cite a recent recommendation from Jeffrey Saut, Chief Investment Strategist for Raymond James, on the role of convertible securities in the current environment, *"As the Trump Era unfolds, convertibles offer a unique solution for improving the diversification and positive asymmetry of a portfolio."*

Making the best of a good mess!

In closing, we couldn't resist quoting the inimitable Andy Rooney, when he quipped, *"One of the most glorious messes in the world is the mess created in the living room on Christmas Day."* Rooney then astutely observed, *"Don't clean it up too quickly!"* The analogy could easily apply to the state of today's divided political landscape. To be kind, it's been a bit of a mess the past year. But if the markets are saying anything, they are telling us to ***have***

faith, ***embrace the mess***, and ***trust*** that the American system of free enterprise will lead us to a more secure and prosperous economic future. While there will be doubters for sure, we are optimistic.

We are sincerely thankful to our clients, friends and colleagues who make our ongoing success possible. As always, we welcome any input and collaboration with you, especially if there have been any significant changes to your risk tolerance level, investment objectives, return expectations or investing criteria to better reflect what you would like to accomplish in your investment portfolio.

Sincerely yours,

John M. Babyak
President & Chief Investment Officer