LESA SROUFE & CO INC.
VALUE ADVISORS

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**2016 Update and Outlook**

The year 2016 was dominated by politics and central banks, not just in the U.S., but around the world. The biggest surprise was the election of political outsider, Donald Trump to the U.S. presidency. While many pundits cried disaster, investors must have sensed opportunity as the U.S. broad stock market indexes ended the fourth quarter considerably higher, with most of the performance coming after November $8^{th}$. Yet again, 2016 was a year in which the U.S. focused broad market indexes outperformed much of the rest of the world. What did change is that value oriented stocks broadly outperformed growth oriented stocks, both big and small. This change in trend benefitted our model portfolios, which are value focused and have a significant weighting in smaller publicly traded companies. We gave back some gains during the fourth quarter of 2016, as precious metals stocks declined after a sharp recovery during the first eight months of the year.

We believe the long trend of declining U.S. interest rates has ended after a 35-year bond bull market. The surprise rotation in 2017 may be out of the popular large U.S. dividend oriented stocks, forcing their current high valuations down and their dividend yields higher. The U.S. dollar measurably strengthened relative to other currencies during the year. That trend may also end, as inflation picks up and if as we expect, the U.S. Federal Reserve is reluctant to raise interest rates commensurately. Any sustained period of rising inflation usually results in declining stock valuations relative to earnings. It is very possible that even if the U.S. real GDP picks up from its modest 2% rate of annual growth experienced in recent years, the U.S. broad stock market indexes may not follow. The much publicized march to “Dow 20,000” (so close) has provided a psychological boost to investors, but doesn’t ensure any follow on. The Opportunistic Value Equity Strategy with its significant cash reserves has some cushion in the event of a market decline. LSC’s one-third weighting in non-U.S. based companies would benefit from a rotation of investor interest into international stocks, long the laggards relative to the U.S. stock market. Their value proposition remains attractive.

During the quarter, we added two new stocks to the portfolio, China Mobile Limited and New York Community Bancorp. We added to two current stock positions, St. Joe Company and AngloGold Ashanti. We sold two stocks in the portfolio, Tidewater Inc. and Washington Federal. China Mobile is the world’s largest mobile telecom provider. It is priced at a discount to its U.S. counterparts, yet operates in a market (China) that is not yet saturated with data using cell phone subscribers. We believe China Mobile’s financial strength and conservative management strategy will serve shareholders well. We purchased New York Community Bancorp after the stock declined because of investor disappointment over its planned acquisition of Astoria Financial and its simultaneous dividend cut. Since then, the acquisition has been terminated, allowing more financial flexibility, in our opinion. We added to our position in AngloGold Ashanti after the precious metals sector declined markedly in the latter part of the year. We had reduced our position in the stock earlier in the year as the precious metals producers experienced significant gains. We added to our position in St. Joe Company. Activity in St. Joe's real estate development business appears to be picking up, which should bode well for this gulf coast real estate developer. We sold Tidewater, the operator of towing vessels to the offshore oil industry. Management has indicated that its inability to come to a new loan covenant agreement with its lenders may result in the company filing for bankruptcy. We also sold Washington Federal, the Seattle based regional bank. The stock has benefitted from an exuberant local economy and more recently, rising interest rates. We now regard Washington Federal as fully priced.

Last year at this time, we expected a rotation of investor interest into value oriented stocks from growth stocks (that did happen). We expect more of the same. We also expected non-U.S. markets to outperform the U.S. We expect that to (finally) happen in 2017.

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