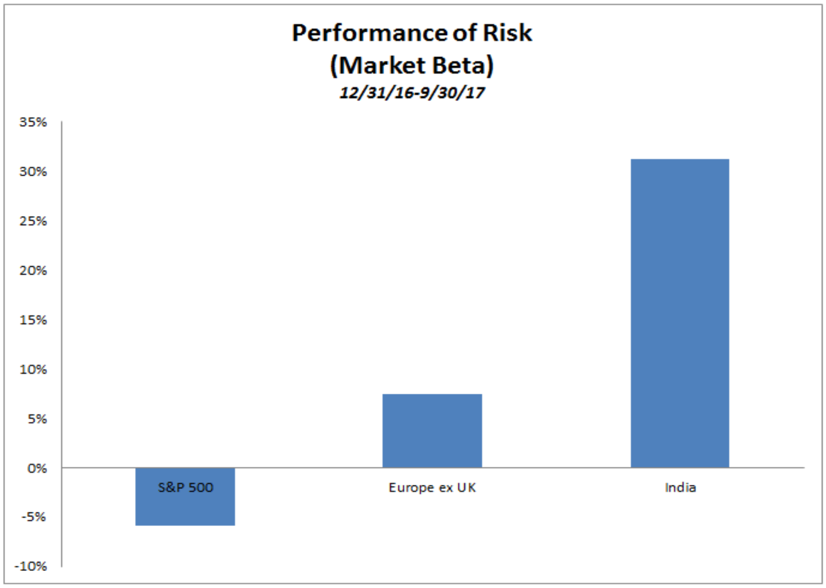
"The word 'risk' derives from the early Italian risicare, which means 'to dare'. In this sense, risk is a choice rather than a fate."

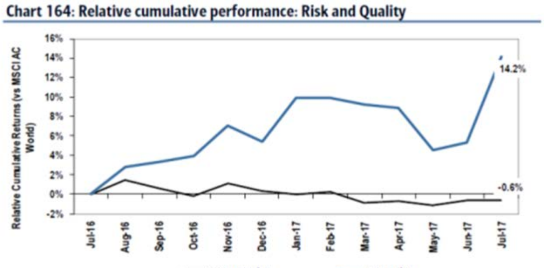
- Peter Bernstein, author of "Against the Gods: The Remarkable Story of Risk"



Source: Ned Davis Research

Peter Bernstein was an interesting person who after graduating from Williams College in 1951, took over his father's wealth management business where he managed multi-billion dollar investment portfolios for institutions and individuals. After resigning, he became the first editor of *The Journal of Portfolio Management*, a widely read publication for investment managers. In time he began to write books as an American financial historian and perhaps his most popular work was his 1988 book highlighted above, which chronicled the history of measuring business and investment risk .

Chart 164: Relative cumulative performance: Risk and Quality

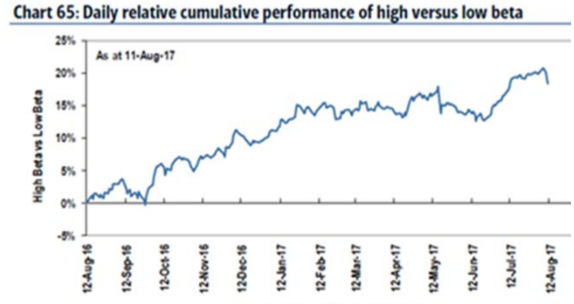


Source: BofA Merrill Lynch Global Quantitative Strategy, MSCI, IBES, Worldscope, Exshare, S&P, Bloomberg

How much risk one takes is a choice and is an essential part of investing, and it's helpful to understand when one is taking more (or excessive or reckless) risk and when one is not. In 2017, one of the interesting facets of the global equity markets has been the willingness to take risk depending on the geography.

As seen in the chart above, owning riskier or higher beta stocks has helped investors win outside the U.S. but not within the U.S. Moreover, moving beyond developed markets into emerging markets such as India, it has paid to take more risk in one's portfolio as it has been especially additive to returns. The charts to the left and right from Merrill Lynch confirm Ned Davis Research's observation as over the past year, owning more risk (or risk defined as higher beta relative to a given market) has won versus quality (in the chart to the left).

Chart 65: Daily relative cumulative performance of high versus low beta



Source: BofA Merrill Lynch Global Quantitative Strategy, MSCI, IBES

Relative Weekly Performance of "Non Earners" Relative to the MSCI World Index

Source: Bloomberg

The move to risk appears to have accelerated in the third quarter of 2017. Another way of assessing risk is how have stocks that don't earn profits performed relative to the index? A glance at the chart above that shows the weekly performance (outperformance in green) of "non earners" has accelerated in the past quarter.

What are the reasons for the divergence in U.S. based risk returns and the acceleration of non-earners' performance in the third quarter? Strategists such as Merrill Lynch which have their "Risk-Love" indicator point to the synchronized global recovery where virtually every developed country is reporting positive gross domestic product increases, low market volatility, narrow credit spreads, and low worldwide interest rates. Perhaps the appetite for taking risk in U.S. risk assets is less appealing given the recent and prospective hikes in the Federal Funds rate? Regardless, the amount of risk embedded in investment portfolios and where those investments are located have impacted relative returns in 2017. Since their inception, Sterling Equity Opportunity portfolios tend to have lower risk characteristics relative to the market (in part, by investing in profitable companies) and strive to outperform through stock selection to provide clients with "above average returns with below average risk."

As always, thank you for your interest and trust managing your investments.

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