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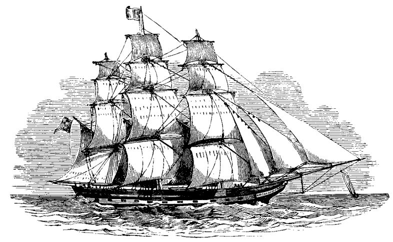

Pilot Capital Management
Quarterly Investment Commentary

Date:	January 15, 2017
From:	Greg Staub, CFA, Ph.D.; Matthew Staub, CFA
To:	Pilot Capital Clients & Friends

Dear Clients and Friends,

Your reports for the fourth quarter of 2016 are enclosed. This letter gives a review of the quarter and briefly summarizes our current investment views.

Fourth Quarter 2016 Market Review

Market/Index	2015 Close	As of Sep. 30th	2016 Close	*Quarter Change*	Year-to-Date Change
DJIA	17425.03	18308.15	19762.60	*7.94%*	13.42%
S&P 500	2043.94	2168.27	2238.83	*3.25%*	9.54%
Russell 2000	1135.89	1251.65	1357.13	*8.43%*	19.48%
Global Dow	2336.45	2459.66	2528.21	*2.79%*	8.21%
Fed Funds	0.25% - 0.50%	0.25% - 0.50%	0.50% - 0.75%	*25 bps*	25 bps
10-Yr Treasury	2.26%	1.59%	2.44%	*85 bps*	18 bps

The year 2016 likely will be remembered for the election of Donald Trump as the 45th president of the United States and for the Brexit vote. This year also saw the Fed raise interest rates for the first time since last December, noting that the labor market has continued to strengthen and that economic activity has been expanding at a moderate pace since midyear. While inflation remains below the Fed's target of 2.0%, the Federal Open Market Committee expects inflation to rise to its target level over the medium term on the heels of anticipated improvements in energy and import prices and continued labor strengthening. Equities began the year hitting the skids as receding oil prices and a plummeting Chinese stock market pushed stock prices down and bond prices up. By midyear equities had recovered, despite Great Britain's decision to exit the European Union. Following the results of the presidential election, stocks surged to new highs. Whether this trend continues in 2017 remains to be seen following President-elect Trump's first few months in office.

Investment Commentary

The Trump Effect

Two events dominated the investment news in the fourth quarter of 2016. The first was Donald Trump’s surprising victory in the U.S. Presidential election accompanied by Republicans maintaining control of both houses of Congress. The unanticipated ‘Trump rally’ that followed boosted all types of risk assets, with financials and small cap stocks leading the way. This rally surprised many (including us, to an extent) but digging deeper into the market’s rationale and viewing the rally in the context of President-elect Trump’s policies, it should not be all that surprising. Many pundits say that Trump is an unknown and this represents a danger to the economy. We have spent a great deal of time examining the President-elect’s economic agenda since the election. If he is able to accomplish these economic goals, American businesses can look forward to:

- A less restrictive regulatory environment
- A more level playing field in international business
- Lower tax rates (or at least not the higher rates proposed by the opposition)

When viewing the rally as a response to expectations of lower regulation, lower taxation, and pro-growth/reflationary policies, the ‘Trump rally’ is not irrational by any means. We remain optimistic about the prospects for the U.S. economy, but are still concerned about stocks which remain either fairly-valued or somewhat overvalued depending on the asset class/sector under consideration. By no means of analysis are U.S. stocks cheap. We would be a buyer, however in any correction of more than 5-10%.

Rising Interest Rates

The other event worth noting was the Federal Reserve’s decision to raise the Federal Funds Rate 25 bps to a target range of 0.50% - 0.75%. While hardly a surprise, the decision did put markets on notice that the Fed is serious about allowing market data to drive its decisions. The economy is certainly no longer in crisis mode and the Fed is entirely justified in slowly moving toward a more normal level of short term rates. We expect one or two quarter point hikes this year which will create some serious headwinds for investment grade bond markets.

We have been managing the fixed income portion of our managed portfolios to a lower duration (less sensitive to interest rate changes) for some time now. This strategy has now started to bear fruit with marked outperformance compared to the benchmark U.S. Aggregate Bond Index. Our fixed income allocations were also helped by a major upward move in lower-quality corporate bonds. This move was sufficient to drive prices on lower-grade corporates higher to the point where we have reduced our exposure in this area by roughly one third. The proceeds from this move were invested in total return bond funds whose management teams share our concerns about rising interest rates. If we see additional price appreciation in high yield bonds, we will continue to reduce positions.

Value vs. Growth

Beginning in the fourth quarter of 2016 and continuing to date we have also seen significant outperformance to the S&P 500 from our value equity managers. Dodge & Cox Stock (DODGX) and Oakmark Select (OAKLX) were up 14.5% and 13.5% respectively in the prior three months (as of this writing) compared to 6.5% for the S&P 500. This represents the most substantial outperformance of value versus growth in a decade. We view this as both long overdue and sustainable and plan no changes in the structure of our equity allocations.

We were very pleased with the performance of our managed portfolios in the fourth quarter and look forward to the coming year. We wish all our clients and friends a very happy and prosperous New Year.

Thank you for your continued trust and confidence in Pilot Capital Management. As always, should there be any questions, please don't hesitate to contact us.

Sincerely,

Greg Staub, CFA, Ph.D.
President

Matthew Staub, CFA
Vice President