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Market Commentary **Summer 2017**

Stealthily Higher

A convergence of positive economic influences around the globe has continued to drive US equity markets to new highs through the first half of 2017. Over the first six month stanza, the broad US equity market, as measured by the Russell 3000 index, closed up just over +8.9% and has continued to pierce through +11.0% at this writing. The seismic leadership shift in US stocks, which we alluded to in our Spring commentary, remained virtually intact as large cap stocks continued to outpace mid and small caps, while growth style investing remained on its torrid pace over value propositions across the capitalization spectrum. Looking back, the only equity sector that materially underperformed during 1H17 was energy; this after an outsized comeback in 2016. We suspect its nonparticipation is related to the recent price volatility of spot crude oil prices which have traded in the range of $42-55/bbl. Unfortunately, for the MLP infrastructure asset class, oil price volatility seems to have overshadowed increasing volume production levels, which have grown by some +22% year over year. Hence we remain very confident in the infrastructure space and believe it remains attractively priced.

On the flip side of the equity markets, the US bond markets remained largely intact despite what was thought to become a hangover from the Fed's two post-election rate increases. Following what was an unnerving spike in bond yields that carried over well into the first quarter, the benchmark 10-year treasury yield has since moderated, closing the second quarter at +2.31% down from a high of +2.62% in mid-March. Meanwhile, high quality intermediate-term tax exempt bonds, as measured by Barclays 10-Year Muni index posted a solid +4.2% total return while similar maturity and credit quality corporates registered +2.3%. High yield bonds posted +4.9%.

On the international front, equity markets quietly continued to outpace US stock performance, spurred on by both central bank accommodation and currency shifts. By the end of the second quarter, developed stock markets, as measured by the MSCI EAFE index, posted a robust +14.2% return on the year-to-date while emerging market stocks posted a torrid +18.6% over the same period.

So why, all of a sudden, do we find ourselves in a US and global economy that appears to be moving in tandem, i.e. gaining noticeable traction and sending world stock markets to elevated levels or new highs? We suspect there are many narratives to explain the pleasantries behind the momentum, including the notion that global central bank policies, now long in the tooth, may finally have jump-started what has been an excruciatingly sluggish post-recession growth period. Equally as important though, at least right now, has been the recent shift in currency valuations. For example, in the European Union increasingly healthy economic activity has resulted in a resurgence of consumer confidence highlighted by a 12% surge in the Euro, despite the politics surrounding the Brexit. Meanwhile, here in the US, the dollar has tumbled from its post-election

peak by almost 10% to a 13 month low. This move sparked a host of immediate benefits for the international community, as well as for the US itself.

On the international front, foreign demand for US goods and services has surged. Repatriation of US dollars, always a concern for emerging markets - many of whom remain dependent on foreign investment - is less likely to occur as the currency remains soft. This drives up confidence within those same economies. The cost of world oil, itself moderating in price, and which is traded in US dollars (aka petrodollars) is less taxing on world economies, allowing for a re-allocation of capital to more productive ends within those economies.

But the benefits of dollar softening has not been lost on corporate America. For US exporters, top line revenue growth, profitability, and earnings - which have been on an upward trajectory for several quarters now - continue to be enhanced by better FX conversion rates and little or no accompanying inflation. It is this earnings expansion that has helped take the "edge" off our outlook on the current stock market highs. That said, it is the sustainability of these same earnings which is so important to the longer-term support of these current market levels.

Notwithstanding remarkably low unemployment, robust activity, and surging equity markets, the Federal Reserve remains baffled by the fact that inflation has ebbed and remains under target. As of this writing, Janet Yellen has signaled a growing reluctance to raise the Fund's rate before year end, and even then the probability of a third increase this year has softened to under 50%, at least for the time being. This prospective pause seems to be reinforcing our current financial momentum.

With that, many financial pundits have resurrected the expression that we have entered another "Goldilocks"- like market cycle where things seem to be just about right and where market downside risk could only be triggered by political stupidity, scandal, or unforeseen geopolitical risk. While we all bask in the summer sun of August, our hope is that these "things remain just right".