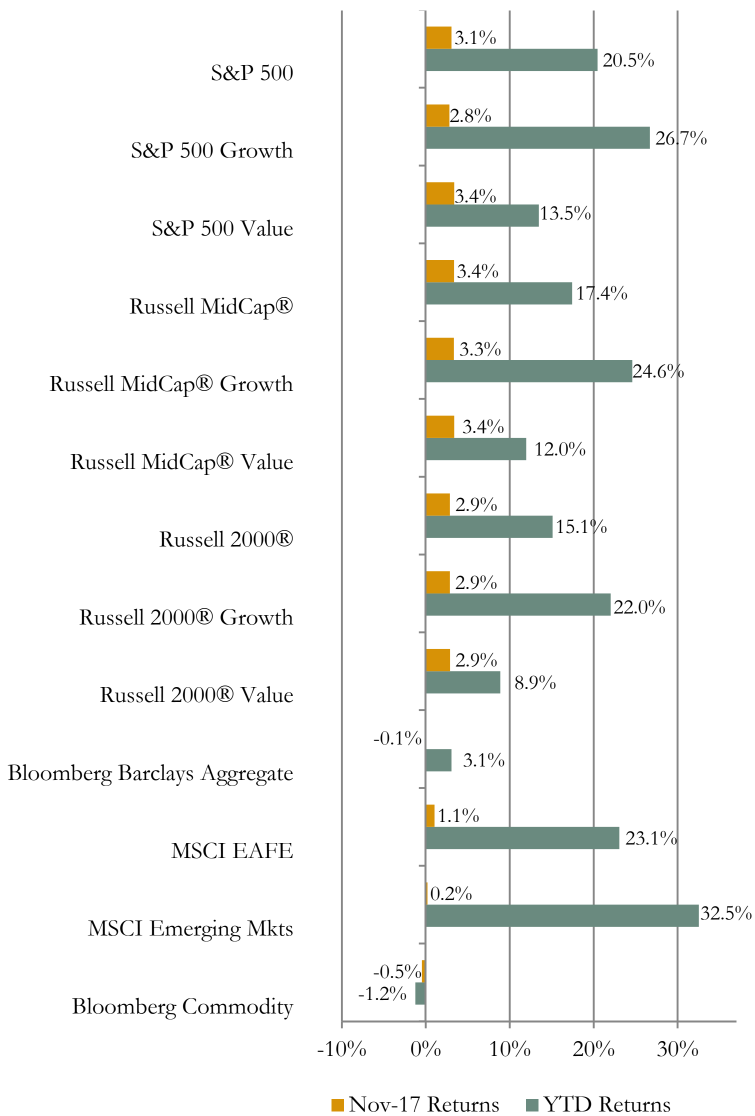
Monthly Market Summary – November 2017

Another month, more equity market highs. During early November the Dow Jones Industrial Average, S&P 500, and Nasdaq Composite each hit new all-time highs. In Europe, the STOXX 600 reached a 2-year high, in Japan, the Nikkei reached a 25-year high, in Taiwan, the Taiex hit a 27-year high, in Hong Kong, the Hang Seng reached a 10-year high, and in Australia the benchmark index hit a 9-year high. Global equities did experience a mid-month sell-off led by declines in technology and momentum stocks that have had sizeable gains during 2017. Profit-taking could have been the main factor in the sell-off. Uncertainty about the U.S. tax reform bill and some weaker earnings announcements in Europe also contributed to the sell-off. Equity markets rebounded later in the month on positive earnings reports and progress being made toward passage of the tax reform bill in the Senate. Major U.S. equity indices advanced to hit more record highs and finished the month with positive returns. Interestingly, November was the 13th consecutive month that the S&P 500 index has posted a positive return. It is only the second time the index has posted a gain for 13 consecutive months. The other 13-month gain streak was in 1959.

Market Indices – November 2017



Most bond yields rose slightly (and prices declined) during the month on the expectation for a rate hike by the Federal Reserve (Fed) in December. The bond market took the nomination of Jerome Powell as the next Federal Reserve Chair in stride as he is seen as a centrist and is expected to continue the current monetary policy path. There were two significant moves in commodity markets during November. The first was the 5.6% increase in the price of crude oil due to political events, a drawdown in inventories, and extension of the production cut agreement by the Organization of Petroleum Exporting Countries (OPEC) and non-OPEC countries. The second significant move was the sharp drop in industrial metals prices on concerns about weakening demand from China.

Much of the data reported during November continued to point to generally improving economic fundamentals around the world. In the U.S., third quarter gross domestic product (GDP) growth was revised higher to 3.3%, which is the highest rate of growth since 2014. Other significant reports include a drop in the unemployment rate to a 17-year low of 4.1%, new home sales reaching a 10-year high, the

Institute of Supply Management's non-manufacturing index increasing to 60.1 - which was the highest reading since August 2005 - and the index of leading indicators increasing 1.2%, which was double the increase that analysts had expected. Outside the U.S., euro area third quarter GDP growth was 0.6% on a quarter over quarter basis, which was above expectations. Japan's third quarter GDP grew 0.3% boosted by increased exports. Brazil appears to be emerging from a severe recession and posted positive GDP growth at 0.1%. Another sign of economic improvement in Brazil is the 6.4% gain in retail sales which was the highest increase since April 2014. One country that had lower data reports was China where industrial output, retail sales, and construction spending declined modestly as the government attempts to transition the economy to higher quality growth and reduce risks to the financial sector.

In U.S. equity markets, mid-capitalization (cap) stocks outperformed large-cap stocks and both outperformed small-cap stocks. There was a sector rotation during the month especially among large-cap stocks that resulted in value outperforming growth by a small margin. Investors moved out of technology stocks into consumer staples, consumer discretionary, financials, and industrials. The moves were likely due to taking profits in stocks that have had high double-digit gains this year and moving into sectors that are seen as benefiting from the tax cuts included in the tax reform bill that is moving through Congress.

International equity indices posted gains for November, but lagged U.S. equity index returns. The MSCI EAFE index of developed international stocks had a return of 1.1% and the MSCI Emerging Markets (EM) index posted a return of 0.2% on a U.S dollar basis. Currency movements had a positive impact on November returns since both the EAFE and EM indices had a small negative return on a local currency basis. Growth stocks outperformed value stocks in both the EAFE and EM. Value sectors such as energy, materials, industrials, and utilities had the lowest returns while consumer related and healthcare had the highest returns. Just as in the U.S., the technology sector was weak in the EM index as investors rotated away from some of the top performing stocks for the year. On a geographic basis, Japan had the best return among developed international countries on several strong economic reports. Returns in the European region were mixed with strong economic and earnings news boosting equity markets in Germany and France while political issues pressured equity prices in Italy, Spain, and the U.K. In the emerging markets index, Russia had the highest return boosted by higher crude oil prices. China also had a positive return. Technology heavy economies such as Taiwan had among the lowest returns but Chile posted the worst performance among EM countries with a decline of almost 12% due to results in the presidential election.

U.S. bond market returns were mostly negative for the month leading the Bloomberg Barclays U.S. Aggregate Bond index to post a return of -0.1% for November. Treasury bond yields rose (and prices declined) across the maturity range, except for the longest maturity bonds, due to solid economic data and on expectations for a rate hike by the Federal Reserve in December. Investment grade corporate and municipal bond prices generally trended lower with Treasury bonds. A sizeable amount of new bond issuance also pressured corporate and municipal bond prices during the month. Perhaps the most significant news in the fixed income markets for the month was the mid-month sell-off in the high yield bond sector. The sell-off was mainly due to weak earnings guidance from some of the largest high yield issuers particularly in the telecom and healthcare sectors along with concerns about the potential for new limits on interest deductibility in a new tax bill. However, the high yield sector recovered much of the decline later in the month as investors' demand for yield increased.

The Bloomberg Commodity index had a return of -0.5% for November. Petroleum was the only major sub-index we track that had a positive return for the month. Crude oil prices jumped to levels last reached in 2015 due to various factors. These factors included arrests of Saudi Arabian officials and members of the royal family, higher demand drawing down inventories, and a new agreement by OPEC and various non-OPEC countries including Russia to limit production through 2018. The industrial metals sub-index was down over 4% due to concerns about weakening demand from China. The livestock sub-index had the sharpest drop of almost 6% due to excess supply.

Vogel Consulting, LLC (Vogel) Tactical Recommendations

We made a change to our tactical recommendations to move to an overweight position in non-U.S. equities by overweighting exposure to emerging markets equity. We continue to be positive on the outlook for U.S. and developed international equities as we see support for corporate earnings growth due to positive global economic growth momentum since most economic data continues to be solidly in expansionary territory and inflation remains muted. However, after the improvements that have been seen in various economic data in the U.S., Europe, and Japan, we expect the rate of future improvement may be lower. In contrast, various emerging markets regions appear to still be earlier in the economic cycle. Therefore, even though emerging markets stocks have had sizeable price gains this year, we expect a higher rate of economic and profitability growth in emerging markets than in developed markets in the coming year which supports our overweight recommendation. Our view is that recent improvements in emerging markets fundamentals mark the beginning of a longer-term period of improvement after a multi-year period of underperformance. Not only are emerging market economies benefiting from global economic growth, various structural and political reforms are being implemented and various countries have just recently begun to implement stimulative fiscal and monetary policies such as interest rate cuts in contrast to developed countries which are either reducing their stimulus policies or considering when to implement reductions.

We continue to recommend an equal weight to U.S. large-cap, mid-cap, and small-cap stocks. Also, we continue to favor equities over bonds and retain our underweight recommendation for fixed income investments. Our underweight recommendation is because the return expectation for bonds is modest due to the low level of yields and the prospects for yields to move higher (and prices lower) if inflation picks-up and the Fed continues to hike its policy rate as it has suggested. Within fixed income we continue to recommend a focus on short to intermediate term bonds. We also continue to favor non-Treasury bonds for the yield advantage they provide. We continue to favor hedge fund strategies over fixed income for the lower expected volatility portion of portfolios but also recommend an underweight allocation to hedge funds. Since our expectation is for a moderate rate of inflation to continue, we recommend an equal weight to real assets. We would not be surprised if financial markets experience bouts of volatility as more details emerge about any fiscal, monetary, or political policy changes or if there are delays in implementing these actions. Therefore, we continue to recommend using periods of market strength to raise any cash needed to support spending needs over the coming 12-24 months.