FINANCIAL PROSPERITY vs. GLOBAL TENSION

Market Review **MAY 2017**

Militaristic campaigns show up frequently in today's headlines. For example, the US military recently performed an airstrike on a Syrian airbase in response to alleged chemical weapon use by the Syrian government. The airstrikes apparently further soured the relationship between the United States and Russia. Shortly thereafter, the US military dropped a large bomb on an Islamic State complex in Afghanistan. And, if that wasn't enough display of power in one month, the North Korean government continued to pester the free world with ballistic missile tests. North Korea has vowed to perform even more tests in retaliation to greater economic sanctions.

Coincidentally, investors sought out wealth preservation at the climax of military activity. Gold prices rose to $1,284 per ounce when news was released that aircraft carriers were making their way to the Korean peninsula. The price of gold has since retreated. Likewise, US treasury yields sunk to 2.18% as buyers pushed prices higher. Headline treasury yields now trade near 2.30%.

By contrast, European markets exhibited more optimism after the first-round of French voting closed. Emmanuel Macron was victorious with 24%. His competitor, Marine Le Pen, came in a close second with 21%. Mr. Macron is now expected to beat Ms. Le Pen in the second round and bring greater stability to French politics and the European Union. Right after the first-round results, the largest 600 European stocks advanced 3%. Also, yield spreads between French and German government bonds narrowed suggesting more confidence for the region's future.

On the other side of the Atlantic, first quarter US GDP showed only 0.7% growth from the previous quarter. Consumer spending increased at a sluggish rate of 0.3% despite higher consumer confidence. Households were found to cut large purchases on items like cars and refrigerators. Cuts to government spending and a reduction to business inventories also dragged down the growth number. Business investment and exports contributed the most to last quarter's economic expansion. Investments and exports grew 9.4% and 5.8%, respectively. Year-over-year, real economic growth still paces at about 2%. Personal consumption expenditures, a popular price index, indicated that prices rose at a 2% annual rate once the impact of food and energy were removed from the data. The Federal Reserve is about to wrap up a two-day policy meeting. They are expected to leave key interest rates unchanged.

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Investors pursued the trend of buying US stocks once companies began reporting first quarter profits. Of the largest 500 US companies that have already reported, over two-thirds grew profits in comparison to the same reporting period from last year. Companies that overlap the technology and consumer cyclical space had some of the best results. Those shares helped send some stock indexes up to new highs. Unfortunately, some defensive named stocks and big auto makers saw their sales and profits drop.

Republicans and Democrats recently agreed to keep the government open through September on a 1.1 trillion-dollar spending bill. Now legislatures begin to focus on key pieces of legislation that are important to the economy. Health care reform is back on the agenda and then tax policy. President Trump recently laid out his administration's tax plan. It contained a massive cut to the corporate tax rate from 35% to 15% and gave companies the ability to fully-deduct their cost of capital in year one. The plan is to pay for itself by eliminating corporate tax expenditures and improved economic growth. Government figures suggest that public debt could grow another $2 trillion from such a plan. An increase of debt on that magnitude will require support from Democrats. That could be a tough sell for the Republicans.

Market Movers

Foreign assets persisted to deliver outperformance in the month of April. US dollar weakness and some risk-taking following the first round of French voting bolstered the foreign asset category. The Core Allocation models have benefited from their foreign positions. Moreover, the Core Allocation models continue to deliver superior excess returns above their primary benchmarks, the Morningstar World Allocation and Morningstar Tactical Allocation. The positions set-forth at the beginning of the year by the Investment Team continue to provide favorable results. The team remains committed to diligently monitoring markets, economic data, and world scenarios as new information becomes available. So far, no material events have required a change to the allocations implemented at the beginning of the year.

Asset Categories	*Monthly*	*YTD*
US STOCKS	0.86%	4.73%
FOREIGN STOCKS	3.09%	12.82%
US BONDS	0.66%	1.94%
FOREIGN BONDS	1.09%	4.40%
HARD ASSETS	-0.25%	0.33%
HYBRIDS	1.05%	5.27%

*DATA USED IS SOURCED FROM MORNINGSTAR®

US STOCKS traded down by mid-April when geo-militaristic tensions rose. However, by the end the month, US stocks made gains as corporate earnings came into season. Investors saw the earnings results by the largest US companies as a favorable sign for prosperity. Large-Caps (VUG, VTV) were the best performers. The category edged out a one percent return while Mid-Caps and Small-Caps followed closely behind.

FOREIGN STOCKS again offered the best monthly returns. Foreign Small/Mid-Caps (VSS) gained over four percent. Large-Caps (VEA) and Emerging Markets (VWO) each earned over two percent. Prospective stability for France's EU membership and a depreciating dollar gave a lift to the foreign category. Our added weight to Emerging Markets has provided significant value. Maintaining a sizeable position in foreign equity has also been an important driver for our models' returns.

US BONDS have given modest returns without sizable market volatility, despite all the hype over rising interest rates. The asset category is up nearly two percent this year on strong institutional demand. Obvious winners are High Yield (JNK) and High Quality Corporate (VCIT) bonds, which are up over three and two percent, respectively. The trend since last year's election has been to buy risk. In addition, our unconventional investment in Long-Term Treasury (TLT) has added value relative to shorter-term maturities.

FOREIGN BONDS have performed even better than domestic bonds. Narrowing spreads on government and emerging market debt stay in theme following lower geo-political risks and better macro-economic data. The European Central Bank still supports European bonds by electing to keep target interest rates low. Our increased allocation to Emerging Market debt (PCY) has provided enhanced results and diversification relative to developed market bonds.

HARD ASSETS continue to deliver important diversification benefits relative to traditional stocks and bonds. Energy has been a drag on the category. OPEC's scheduled production cuts have been uneventful to the price of oil. Our position in Master Limited Partnerships (AMJ) bucked the oil trend and delivered positive returns. Precious Metals (IAU) rose by mid-month, but then retreated and finished the month with a small gain. For the full year, Precious Metals and Global Real Estate (RWO) have done well for the Core Allocation strategies.

HYBRIDS continue to earn consistent and favorable returns. The category has outperformed traditional bonds rather significantly over the last month and since the beginning of the year. Convertible Debt (CWB) and Variable Preferred Stock (VRP) allow us to manage interest rate risk and participate in risk-buying market trends.