July 2017

Quarterly Commentary

This past quarter has seen a continuation of positive market trends with equity returns in the low-to-mid single digit range. Confidence remains high despite all the histrionics coming from Washington. Economic growth around the world continues to improve while domestic trends have not changed much despite last fall's elections. The Federal Reserve recently raised the overnight rate to 1%-1 ¼%, and maintained they will begin to normalize the Fed's balance sheet this year which is a clear signal that they expect modest improvement in the underlying economy.

We've been suggesting for a while now that in the current low growth, low interest rate environment, equities could reasonably be expected to rise at a pace similar to the underlying earnings growth rate. We've felt that rising interest rates would hold back any potential PE multiple expansion as multiples have already reached historically high levels. We've also been optimistic that underlying economic growth was strong enough to support 5%-10% earnings growth. For the most part, economic and market dynamics continue to generally fit within this framework. Therefore, we still expect that equities will achieve 10%-type returns for the year; the S&P has made a good start in that direction.

We have all been reading how a handful of large-cap growth stocks -- Facebook, Amazon, Apple, Netflix, Google (the FAANG stocks) plus Tesla and a few others -- have been responsible for a disproportionate share of the market's appreciation so far this year. For some of those stocks (Apple and Google, for example), the gains are a fair reflection of their cash flows and revenue growth, but we believe that the price gains in many of the other highfliers are attributable to unsustainable expectations about future earnings on the part of investors . This makes us uncomfortable and so we have mostly chosen to avoid these stocks.

While investing always involves interpretation of future events, our client portfolios have seen their returns come from underlying earnings and cash flow growth, not speculation about what the future may bring. We believe our conservative total-return strategy supported by dividends will provide greater downside protection should the market take another turn down. We always want to be cognizant of potential risks and of how our portfolios are positioned in order to protect our clients' assets in the event of such a downturn.

We've been surprised at how tame the markets have been this year given the continued political angst and the changing geopolitical landscape. We would caution that the markets have been unnaturally calm, and while we remain cautiously optimistic, we will be looking for potential market dislocations to create opportunities during the balance of the year. Yet, we're also still hopeful that the Trump administration will be able to enact some business-friendly changes which could be a catalyst for the markets. Our long term perspective continues to favor equities over bonds, but we have modest expectations for the balance of the year.

Disclosure Statement

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