Economic Review

As expected the Federal Reserve (Fed) raised the federal funds rate by 0.25% at their June meeting to 1-1.25%. This move continues their march to a 2% policy normalization target range. The Fed also anticipates beginning a balance sheet normalization program this year by reducing bond holdings, provided that the economy continues to evolve favorably. Additionally, the Fed released results of its 7th annual supervisory bank stress test showing that even during a severe recession, our large banks would remain well capitalized allowing them to lend throughout the economic cycle.

Entering its ninth year, the US economic expansion continues as real gross domestic product (real GDP) increased at an annual rate of 1.4% in the first quarter. In the fourth quarter of 2016, real GDP increased 2.1%. The current expansion is the third longest in US history but it has been disappointingly weak, averaging only 2.1% growth a year, weaker than any other recovery since at least 1949.

The Conference Board Leading Economic Index (LEI) continued upward, suggesting the economy is likely to remain on its long-term trend of about 2% growth for the remainder of the year. The improvement was widespread among the majority of the leading indicators, except for housing permits which fell again. Unemployment declined to 4.3% in May down ½% since January. The number of unemployed persons stands at 6.9 million. The labor force participation rate declined in May but has shown no clear trend over the past 12 months.

The Consumer Price Index (CPI) decreased slightly in May to an annual rate of 1.9% according to the Bureau of Labor Statistics. The CPI has averaged 1.6% over the past 10 years.

Although consumer confidence slipped in June to its lowest level since Trump was elected, the overall level still remains quite favorable according to the University of Michigan Surveys of Consumers. It was the best half-year Sentiment Index average since the second half of 2000. Increasing uncertainty about future prospects for the economy has thus far been offset by the resurgent strength in the personal financial situation of consumers.

Financial Markets Review: Domestic Stock Market

The Dow Jones Industrial Average, S&P 500, and the NASDAQ all continued to advance in the second quarter. The Dow closed at 21,349.63 for a 3.32% return and the seventh straight quarter of gains. The S&P 500 finished the quarter with a gain of 5.53% (excluding dividends), to 2,423.41. The NASDAQ finished up 3.86% to 6,140.42, but did drop in June for the first monthly decline since October 2016 as technology struggled.

Health care was the best performing S&P sector in the second quarter, climbing 7.10%. Industrials added 4.73% and financials were up 4.25%. The two negative sectors in the second quarter were telecom services down 7.05% and energy, dropping 6.36%.

Among capitalizations, mid- and small-cap stocks lagged large-caps with the S&P MidCap 400 Index rising 1.97% and the S&P Small Cap 600 Index returning 1.71%. Year-to-date small caps significantly trail large caps.

With respect to style, growth continued to dominate value in the second quarter. For the year-to-date growth has crushed value by 9.33%, according to Russell.

The top-performing stocks in the Dow Jones Industrial Average for the second quarter included McDonald's (+18.17%), Caterpillar (+15.85%), and UnitedHealth Group (+13.05%). Detractors were IBM (-11.66%), General Electric (-9.36%), and Verizon (-8.39%).

The best performers for the second quarter among S&P Dow Jones industry groups were toys (+19.2%), electronic office equipment (+14.9%), and airlines (+14.2%). Repeating among the worst performers were oil equipment & services (-16.1%) and exploration & production (-9.4%).

The price-earnings level of the S&P 500 is somewhat worrisome, trading significantly above historical valuation averages at 25.63 (per Barron's) although multiples have backed off slightly from the last quarter's close.

Expectations of real structural and fiscal policy reforms coming from the Trump administration look increasingly unlikely for 2017. The market continues to move forward against a backdrop of an improving economy and earnings growth, lofty market valuations, trade frictions, inflation expectations, political partisanship, potential late year tax cuts, and ever present global tensions.

	Total Returns (6/30/17)			Annualized Returns (6/30/17)		
Category/Style	2nd Quarter	Year-to-Date	One Year	Three Years	Five Years	Ten Years
S&P 500	3.09	9.34	17.90	9.61	14.63	7.18
S&P Midcap 400	1.97	5.99	18.57	8.53	14.92	8.56
S&P Small Cap 600	1.71	2.79	22.47	9.32	15.47	8.44
Russell 1000 Large Cap Growth	4.67	13.99	20.42	11.11	15.30	8.91
Russell 1000 Large Cap Value	1.34	4.66	15.53	7.36	13.94	5.57
Russell 2000 Small Cap Growth	4.39	9.97	24.40	7.64	13.98	7.82
Russell 2000 Small Cap Value	0.67	0.54	24.86	7.02	13.39	5.92

Source: Frank Russell Company, Standard and Poor's

International Stock Markets

MSCI EAFE Index of developed markets continued to advance in the second quarter gaining 6.12%. Eurozone confidence rose to the highest level since the financial crises as economic growth picked up and concerns about a European Union break up diminished with Nationalist political parties losing momentum.

With a strengthening global economy as the framework, emerging markets jumped 6.27% as measured by the MSCI Emerging Markets Index. Year-to-date emerging markets are ablaze, rocketing 18.43%. Frontier markets added 6.13%.

Euro- area manufacturing expanded at the strongest pace in over six years. The Stoxx Europe 600 Index edged down 0.46% to 379.37 at quarter's close. Germany's DAX Index nudged up 0.10% to 12,325.12. And although they marched to different drummers the French and English markets fared about the same in the second quarter. Macron as expected won the Presidency, but France's CAC-40 Index barely moved losing just 0.04% to 5,120.68. Prime Minister May suffered a surprising defeat losing her majority, but similarly the UK London FTSE 100 Index ended the quarter down 0.14% to 7,312.72.

In Asia, the Dow Jones Asia-Pacific TSM Index gained 4.99% to finish the quarter at 1,624.81. Japan's manufacturing outlook improved in the second quarter and the Japan's Nikkei stock average added 5.94% to 20,033.43. In emerging markets China's Shanghai Composite Index drifted down 0.93% to 3,192.43.

The Americas DJ Americas index was ahead 2.24% to 582.63. Brazil's Sao Paulo Bovespa Index declined -3.20% to 62,899.97, Canada's S&R/TSX composite index dropped 2.35% to 15,182.19 and Mexico's IPC All-Share Index, ended the quarter at 49,857.49 advancing 2.71%.

Top performing countries for the quarter (in $US) included Latvia (+40.3%), Nigeria (+35.3%), and Greece (+27.1%). Laggards included Qatar (-11.2%), Lebanon (-10.7%), and Russia (-9.3%). The dollar gained 1.03% against the yen, ending the period at 112.54 (JPY/USD). The dollar fell 6.75% versus the euro, ending the quarter at .8752(EUR/USD).

World Bond Markets

The pickup in yields abated somewhat in the second quarter. The Barclays U.S Aggregate Bond Index returned 1.45%. The Barclays Municipal Index rose 1.96%, while the Barclays U.S. Treasury TIPS Index slid -0.40%. The U.S. 10-year note yield dipped slightly to 2.30% from 2.39% at first quarter's end. The 7-day yield on retail money funds trended higher to 0.80% according to the Crane 100 Money Fund index. Yields on foreign bonds were little changed in the second quarter, with the 10-year bond yield up just 0.03% in both Germany (0.37%) and Canada (1.62%). Yields were motionless in Japan and the UK at 0.06% and 1.15% respectively.

Commodities

Commodities descended in the second quarter posting a 3.00% loss for the period as measured by the Bloomberg Commodity Index. Gold was little changed for the quarter, ending off just 0.53% to $1,240.70 per troy ounce. An abundance of oil production hindered prices and crude dropped 9.01% to $46.04/barrel. The Baker rig count dropped for the first time in 24 weeks. Gasoline ended the quarter at $2.24/gallon which is a 4.15% decline since the beginning of the year.

Mutual Funds/Exchange-Traded Funds

The June 30 release from the Investment Company Institute showed that the combined assets of the nation's mutual funds increased $1.5 trillion (9.1%) over the last twelve months to $17.4 trillion. Interestingly, the number of mutual funds actually fell by 60 to 8,073 over the past year. Over the same period, the number of Exchange-traded funds (ETF) phenomenal growth continued with the number of funds climbing by 115 to 1,762 and assets increased by $694 billion (31.4%) to $2.8 trillion.

MUTUAL FUNDS OVERVIEW AS OF JUNE 30, 2017

	Total Returns			Annualized Returns		
Category	2nd Quarter	Year-to-Date	One Year	Three Years	Five Years	Ten Years
Municipal Bond Intermed.	1.68	3.03	-0.83	2.53	2.54	3.67
Short Taxable Bond	0.56	1.20	1.23	1.08	1.31	2.47
Intermed. Taxable Bond	1.48	2.56	0.95	2.23	2.47	4.34
Long Taxable Bond	3.86	6.21	1.09	5.12	4.92	7.38
High Yield Bond	1.73	4.09	10.79	3.01	5.70	6.04
World Bond	2.07	4.42	1.89	0.30	1.72	4.02
Small-Cap Stock	1.51	3.21	20.94	5.69	12.73	6.14
Mid-Cap Stock	1.92	6.25	17.41	5.45	12.99	6.10
Large-Cap Stock	2.89	8.62	17.17	7.57	13.34	6.21
World Stock	5.09	12.87	18.00	4.53	10.58	3.79
Foreign Stock	6.26	14.45	19.13	1.21	7.83	0.99
Natural Resources	-4.44	-3.51	6.88	-8.25	0.36	-1.35
Real Estate	1.84	2.87	-0.63	7.25	8.48	5.18

Source: Morningstar Category Returns, Morningstar, Inc.

Important definitions and disclosures

The opinions and material presented are provided for informational purposes only. No person or system can predict the market. Neither asset allocation nor diversification guarantee a profit or protect against a loss. All investments are subject to risk, including the risk of principal loss. There is no assurance that the investment goals and process described herein will consistently lead to successful investing. Asset allocation and diversification do not eliminate the risk of experiencing investment losses. The investment return and principal value of an investment will fluctuate, and an investor's shares, when redeemed, may be worth more or less than their original cost. Funds that invest in stocks of small-cap or mid-cap companies involve additional risks. The securities of these companies may be more volatile and less liquid than the securities of larger companies. Funds that invest in international securities involve special additional risks. These risks include, but are not limited to, currency risk, political risk, and risk associated with varying accounting standards. Investment in emerging markets may accentuate these risks. Alternative strategies, including those used in mutual funds, have risks that may substantially increase the potential for loss. Bonds are subject to interest rate risk. Bonds have interest rate risk and credit risk. As interest rates rise, existing bond prices fall and can cause the value of an investment to decline. Changes in interest rates generally have a greater effect on bonds with longer maturities than on those with shorter maturities. Funds that hold bonds are subject to declines and increases in value due to general changes in interest rates. Credit risk refers to the possibility that the issuer of the bond will not be able to make principal and/or interest payments.

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Gross Domestic Product (GDP) is a measure of output from U.S factories and related consumption in the United States. It does not include products made by US companies in foreign markets. The **Federal Open Market Committee** (FOMC), a committee within the Federal Reserve System is charged under United States law with overseeing the nation's open market operations (i.e., the Fed's buying and selling of United States Treasury securities). **Real Gross Domestic Product** (real GDP) is a macroeconomic measure of the value of economic output adjusted for price changes (i.e., inflation or deflation). The **S&P/Case-Shiller Home Price Indices** are the leading measures of U.S. residential real estate prices, tracking changes in the value of residential real estate both nationally as well as in 20 metropolitan regions. **Consumer Price Index (CPI)** measures prices of a fixed basket of goods bought by a typical consumer. It is widely used as a cost-of-living benchmark and uses January 1982 as the base year. **Manufacturing ISM Report** is a monthly report based on a national survey of purchasing managers that tracks month-over-month changes in new orders, production, employment, supplier delivers and inventories for the manufacturing sector. The **University of Michigan Consumer Sentiment Index** is a consumer confidence index published monthly by the University of Michigan. The index is normalized to have a value of 100 in December 1964. Each month at least 500 telephone interviews are conducted of a continental United States sample (Alaska and Hawaii are excluded). Fifty core questions are asked. **S&P 500 Index** is an index of 500 of the largest exchange-traded stocks in the US from a broad range of industries whose collective performance mirrors the overall stock market. The **Dow Jones Industrial Average** is a widely watched index of 30 American stocks thought to represent the pulse of the American economy and markets. The **NASDAQ** is an index that tracks the cumulative results on a market capitalization basis of all stocks trading in the NASDAQ system. An investment concentrated in sectors and industries may involve greater risk and volatility than a more diversified investment. The **S&P SmallCap 600 Index** (S&P600) covers roughly the small-cap range of US stocks, using a capitalization-weighted index. The index covers roughly three percent of the total US stock market. The **S&P MidCap 400 Index** (S&P400) is a stock market index from S&P Dow Jones Indices. The index serves as a barometer for the US mid-cap equities sector and is the most widely followed mid-cap index in existence. To be included in the index, a stock must have a total market capitalization that ranges from roughly $750 million to $3.3 billion. The **Russell 1000 Index** is a capitalization-weighted price-only index which is comprised of 1000 of the largest capitalized US-domiciled companies whose common stock trade in the United States on the New York Stock Exchange, American Stock Exchange and NASDAQ which are included in the Russell 3000 Index. This large cap market-oriented Index is highly correlated with the S&P 500 Index. **Russell 2000 Index** is a market-value-weighted index representing the 2,000 smallest companies in the Russell 3000 index, representative of the US small capitalization securities market. **Price-earnings (P/E) ratio** is a measure of valuation for a company or a collection of companies such as an index; it is calculated by dividing the market value per share by the earnings per share. **Morgan Stanley Capital International Index** (MSCI) EAFE is a market capitalization-weighted index of the leading stocks in Europe, Australasia and Far East. Membership of the index is selected by MSCI and designed for leading stocks roughly to match market sector weights. The **MSCI Emerging Markets Index** is an index created by Morgan Stanley Capital International (MSCI) that is designed to measure equity market performance in global emerging markets. It is a float-adjusted market capitalization index that consists of indices in 21 emerging economies: Brazil, Chile, China, Colombia, Czech Republic, Egypt, Hungary, India, Indonesia, Korea, Malaysia, Mexico, Morocco, Peru, Philippines, Poland, Russia, South Africa, Taiwan, Thailand, and Turkey. **International investing** involves special risks, including the possibility of substantial volatility due to currency fluctuation and political uncertainties. The **STOXX Europe 600 Index** is derived from the STOXX Europe Total Market Index (TMI) and is a subset of the STOXX Global 1800 Index. The **CAC 40 Index** is a benchmark French stock market index. The index represents a capitalization-weighted measure of the 40 most significant values among the 100 highest market caps on the Paris Bourse (now Euronext Paris). The **DAX Index** is a blue chip stock market index consisting of the 30 major German companies trading on the Frankfurt Stock Exchange. The **FTSE 100** is a share index of the 100 companies listed on the London Stock Exchange with the highest market capitalization. The **DJ Asia-Pacific Index** represents the leading stocks by dividend yield traded in the Asia/Pacific region. The **Nikkei Index** is a stock market index for the Tokyo Stock Exchange (TSE). The **Shanghai Composite Index** is a stock market index of all stocks (A shares and B shares) that are traded at the Shanghai Stock Exchange. The **MSCI Frontier Markets Indexes** provide broad representation of the equity opportunity set while taking investability requirements into consideration within each market. MSCI classifies 34 countries as Frontier Markets, 26 of which are included in the MSCI Frontier Markets Index. **Barclays Aggregate Bond Index** is made up of the Lehman Brothers Government/Corporate Bond Index, Mortgage-Backed Securities Index, and Asset-Based Securities Index, including securities that are of investment grade quality or better, have at least one year to maturity, and have an outstanding par value of at least $100 million. The **Barclays Municipal Bond Index** is a market value weighted index of investment grade municipal bonds with maturities of one year or more. The **Barclays Capital US Government Inflation-Linked Bond Index** (US TIPS) measures the performance of the TIPS market. TIPS form the largest component of the Barclays Capital Global Inflation-Linked Bond Index. Inflation-linked indices include only capital indexed bonds with a remaining maturity of one year or more. **Bloomberg Commodity Index:** is a world-production weighted total return index, including reinvested dividends, measuring investor returns from a fully-collateralized commodity futures investment. Due to market fluctuation, the commodities represented by this index may experience loss of invested principal and are subject to investment risk. The **Investment Company Institute** (ICI) is the national trade association of US investment companies, which includes mutual funds, closed-end funds, exchange-traded funds and unit investment trusts. An investment in a money market fund is not insured or guaranteed by the FDIC or any other government agency. Although a money market fund seeks to preserve the value of your investment at $1.00 per share, it is possible to lose money by investing in the fund. An exchange-traded fund (**ETF**) is a security that tracks an index, a commodity or a basket of assets like an index fund, but trades like a stock on an exchange. Indexes are unmanaged and investors cannot invest directly in an index.

Morningstar Category Returns are composed of the average return for the funds in each Morningstar category over the indicated time period. Categories are defined by Morningstar based on holdings statistics. The category returns are adjusted for survivorship bias, meaning they include all investments even if liquidated, merged or otherwise now obsolete. The returns also include funds that were in a given Morningstar category, but have since changed to another category.