2017 Weekly Portfolio Manager Commentary

October 27 , 2017

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ECONOMIC HIGHLIGHTS

U.S. Durable Goods Orders increased 2.2% for the month of September, and increased 8.3% year-over-year. Core capital goods (ex-transportation) represented most of the gains. U.S. New Single Family Home Sales came in at a very strong 667,000 unit annualized rate versus 555,000 expected. Finally, U.S. Real GDP growth was a strong 3.0% for the third quarter of 2017 versus +2.5% consensus.

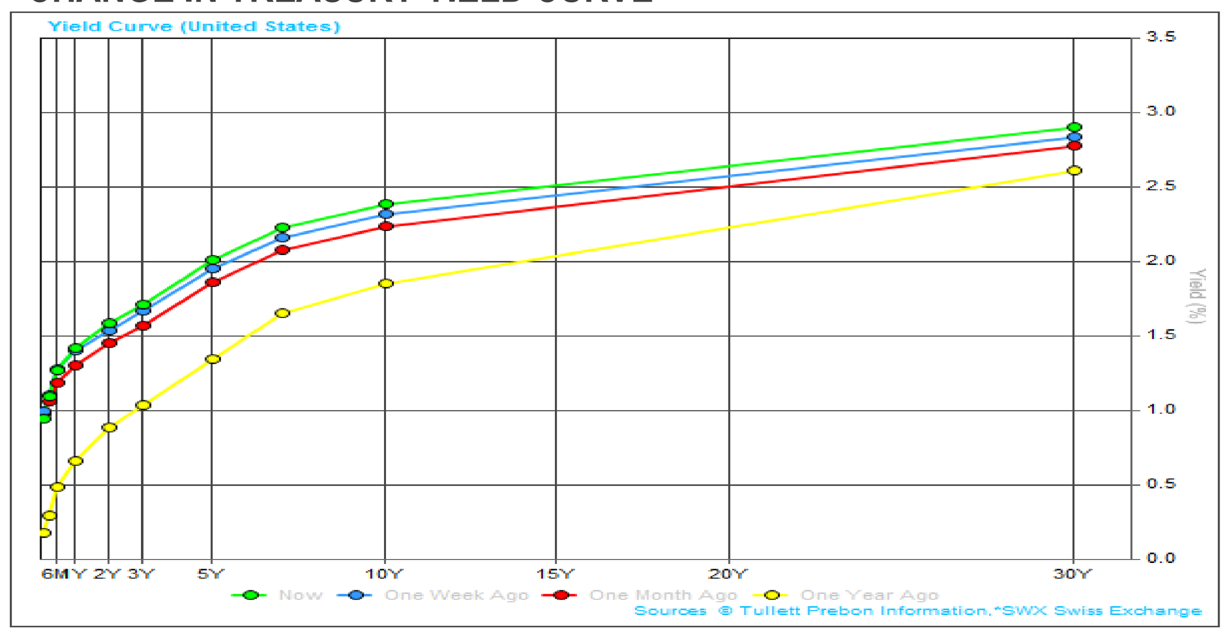
FIXED INCOME

Treasuries rose in price last Friday, pushing yields down from seven-month highs, on a report that President Donald Trump is leaning toward nominating Federal Reserve Governor Jerome Powell to lead the U.S. central bank, a move that would signal continuity for monetary policy in the world's biggest economy. Benchmark ten-year yields fell five basis points to 2.41% at the end of trading, and the Bloomberg dollar index pared gains. Yields had touched the highest since March earlier on Friday, weighed down by a stronger-than-forecast U.S. growth report for the third quarter and as speculation percolated that Trump might still choose economist John Taylor, who's seen as more hawkish than current Chair Janet Yellen. Powell, however, is seen as likely to maintain Yellen's gradual approach to lifting rates and unwinding the Federal Reserve's $4.5 trillion balance sheet. Policymakers' latest projections point to a rate hike in December and three more by the end of next year. "It's almost more about John Taylor than it is about Powell, reversing some of the likelihood that Taylor would be taking the reins," said Michael Lorizio, a senior trader at Manulife Asset Management, which oversees $370 billion. "Powell, while he may differ from Yellen a bit in terms of regulation, in terms of the forward guidance, they would be taking a similar path." Gains in Treasuries were led by the belly of the curve. Five-year yields fell five basis points to 2.03%, pushing the yield curve from five to thirty years to the steepest in two weeks. Futures volumes surged as traders adjusted to the speculation that Powell was on the cusp of the nomination.

CURRENT GENERIC BONDS YIELDS

TREAURIES		AGENCIES		CORPORATES		MUNICIPALS	
3 mo	1.09%	3 mo	1.14%	3 mo	1.40%	3 mo	0.87%
6 mo	1.27%	6 mo	1.24%	6 mo	1.48%	6 mo	0.91%
1 yr	1.41%	1 yr	1.40%	1 yr	1.58%	1 yr	0.98%
2 yr	1.59%	2 yr	1.61%	2 yr	1.83%	2 yr	1.12%
5 yr	2.03%	5 yr	1.90%	5 yr	2.42%	5 yr	1.53%
10 yr	2.41%	10 yr	2.77%	10 yr	3.14%	10 yr	2.20%
30 yr	2.92%	30 yr		30 yr	3.88%	30 yr	3.28%

CHANGE IN TREASURY YIELD CURVE



EQUITY

INDEX RETURNS	LAST WEEK	YTD
Dow Jones Industrials	0.45%	20.87%
S&P 500 (Large Cap)	0.23%	17.16%
S&P 400 (Mid Cap)	0.27%	12.09%
Russell 2000 (Small Cap)	-0.06%	12.28%
NASDAQ Composite	1.09%	25.62%
MSCI EAFE (International)	-0.23%	21.79%
iShares Real Estate	-1.51%	6.28%

U.S. Equities finished trading for the week on a high note after outstanding earning releases surpassed Wall Street expectations. Tech continued their remarkable run with several of the large cap names notching all-time highs. On the flip side, materials and consumer staples trailed the market.

The major indices notched another positive week as the S&P 500 ticked higher to extend its weekly streak to seven weeks of positive gains.

Big tech names such as Amazon (AMZN), Google (GOOGL), Microsoft (MSFT), and Intel (INTC) released extremely positive earnings that propelled the respective names to 52-week highs. CVS announced that they were in talks to acquire AET, which propelled Aetna up nearly10%.

Consumer Discretionary names performed well, particularly in the restaurant and leisure sub industry. Retailers, on the other hand, came under pressure especially after JC Penny (JCP) released lackluster earnings. Industrials trailed as airlines weighed on the sector. Healthcare came under pressure as earnings from biotech names disappointed and worries about the spread of the “Amazon Effect” weighed on drug stores.

Despite the political ping pong taking place on the national airwaves, a republican failure to pass tax reform (which seems increasingly unlikely) will not be enough to derail the bull market according to Barron’s. The markets may drop 5% but it is increasingly clear that the stock market run since the election is not built on tax reform. According to FactSet, 55% of companies in the S&P 500 have reported earnings and have notched a growth rate of 4.7%, which has exceeded expectations.

ASSET ALLOCATION

CURRENT SENTIMENT	
Cash	Neutral
Short Fixed Income	Neutral
Intermediate Fixed Income	Neutral
Inflation-Adjusted Fixed Income	Unfavorable
High Yield Fixed Income	Neutral
International Fixed Income	Neutral
Equity Income	Favorable
Large Cap Equity	Favorable
Mid Cap Equity	Favorable
Small Cap Equity	Neutral
International Equity	Neutral
Emerging Markets Equity	Favorable
Real Estate	Favorable
Commodities	Unfavorable

Below is a summery of our current stance on most asset classes:

Cash - Holding as little as possible given the miniscule yields in money market instruments. Any exposure is for defensive positioning.
Short Term Bonds - Relative to Intermediate Bonds, the reduced duration is preferable given the outlook for higher interest rates.
Intermediate Term Bonds - The current trading range of intermediate bonds warrants a neutral position with limited upside potential. Some opportunities still remain present in spread products.
Inflation-Adjusted Bonds - Low inflation expected in near-term providing zero real return.
High Yield Bonds - Spreads have tightened; however, still remain attractive versus Treasuries.
International Bonds - Emerging market bonds offer good diversification qualities while providing higher yield opportunities relative to domestic fixed income.
Equity Income - High quality and higher-dividend-paying companies remain attractive for long-term investors given their favorable risk-adjusted profile and current yield curves.
Large Cap Stocks - A favorable weighting is recommended. Growth has reemerged as a more favorable style and should be overweighed versus Value.
Mid Cap Stocks - Mid cap exposure along with a value tilt is preferred. Mid cap stocks continue to provide the "sweet spot" of market capitalization - large enough to provide stability, but small enough to be more nimble.
Small Cap Stocks - In broad market corrections, small cap stocks will suffer most with increased volatility. However, a recent divergence of relative strength between small caps and large caps warrants a neutral exposure.
International Stocks - Given most foreign investment is in developed markets and European countries, until sovereign debt concerns are alleviated, an underweight to neutral weight is recommended.
Emerging Market Stocks - Stronger balance sheets, less debt, and better growth potential make emerging markets more fundamentally attractive than developed countries longer-term. Recent relative performance versus developed markets support the stronger fundamental backdrop and positions have been added.
Real Estate - Pricing has stabilized and long-term valuations appear attractive. Real Estate has performed well of late and should continue to be a strong alternative to other asset classes.
Commodities - Global demand should support higher prices if the global recovery remains on track. Although, volatility will be higher and commodities will be susceptible to short-term price shocks, if used in conjunction with other asset classes, risk can be reduced substantially to a diversified portfolio. However, used alone is not recommended as the short-term outlook is not favorable.