Investment Update

Second Quarter 2017

The strong start to the year continued for stocks and bonds as both performed well again in the second quarter. International stocks are outpacing domestic stocks, partially due to the dollar weakening against several foreign currencies, and the stocks of larger US companies are doing better than their smaller counterparts. After recovering sharply in 2016, oil retreated to bear market territory in June falling more than 20% year-to-date, as that market struggles to find equilibrium between supply and demand in an era of lower prices.

Equity Markets (Total Return)	2Q17	1-Yr
Dow Jones Industrials	4.0%	22.1%
S&P 500	3.1%	17.9%
S&P Mid-Cap	2.0%	18.6%
S&P Small-Cap	1.7%	22.5%
MSCI All-Country World	4.0%	18.2%
MSCI Foreign Developed Markets	6.1%	20.3%
MSCI Foreign Emerging Markets	6.3%	23.8%
US Bond Markets	**2Q17**	**1-Yr**
Barclays US Govt/Credit Intermediate	0.9%	-0.2%
Barclays US Govt/Credit Long	4.4%	-1.1%
BAML Municipal Intermediate	1.3%	0.1%

Federal Reserve

In June the Fed raised interest rates 25 basis points for the second time this year and fourth time since 2015. While yields on Treasuries maturing inside of one year have risen throughout the year in anticipation of these moves, the yield on the 10-year Treasury was down as many as 25 basis points relative to the end of 2016 until it rallied slightly at the end of the quarter. Occasionally misunderstood is the fact that the Fed only controls a very short-term market rate of interest. It has no direct influence over longer-term Treasuries which trade on inflation and growth expectations and thus can move in the opposite direction of the Fed as they have this year, or not at all. “Curve flattening,” when shorter-term yields get closer to longer-term yields as we are seeing now, is often seen in the later innings of an economic expansion. However it is a more benign phenomenon than when the yield curve inverts, with short-term yields actually higher than long-term rates, which often closely proceeds an economic recession.

Foreign central banks were late to employ the most accommodative policies that the Fed did in the aftermath of the financial crisis, and only now are they seriously starting to discuss unwinding them. While our stock market appears to be taking recent Fed rate increases in stride, foreign markets appear to be grappling with the thought of a world without easy money just as our market did several years ago.

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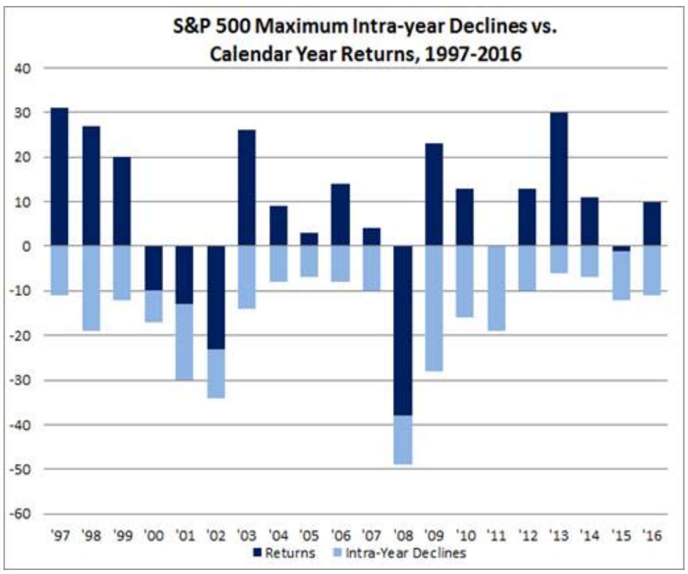
United States

So much else of what was said in our last quarterly update still stands that it nearly could have been relabeled for the second quarter. With a steady rotation of which sectors are out, and under-performing the rest, overall volatility continues to be low as investors have stayed in the market and the returns simply offset each other. Progress on the Republicans' legislative agenda has stalled as the formation of inter, and even intra, party coalitions has proven difficult. The stock market continues to do well thanks to an improving global economy, and low domestic inflation which suggests that the Fed will be continue to be slow in tightening. There also appears to be an acceptance of the status quo as expectations for significant change have fallen since the election. While corporate profits certainly would benefit from lower tax rates and less regulation, companies have been operating in the current environment for many years.

Brief History of Market Drops & Annual Returns



We thought the chart shown here was very interesting and worthy of some discussion for our readers. Graciously sourced from JP Morgan Asset Management, it shows S&P 500 price returns for the last 20 years, as well as the largest peak-to-trough decline that occurred during each year. Even though the market was up in 15 of those 20 years, the average intra-year decline was *over 16%*. If one includes data back to 1980 in the calculation, which allows us to see the long bull market of the 1980s and 1990s, the average decline is still just over 14%.

We know that many have the sense that the stock market is due for a fall, whether because it has done too well for too long and is expensive; because of the chaos in Washington; or the threat of unpredictable geopolitical events. Some of this nervousness is understandably, but likely subconsciously, borne out of the experiences of the two significant bear markets which occurred in the past 20 years. While we cannot predict if any one particular fear will prove prescient, we can see in this chart that material declines are inevitable. Even in the very negative years shown on this chart, at a certain point in the year things were actually even worse. It is imperative to understand that your reaction when declines do come can often determine long-term investing success. Employing an appropriate asset allocation allows you to survive such declines without feeling the need to abandon a sound investment strategy by locking in losses simply because the market has fallen so uncomfortably far below its recent highs.

The information contained in this investment update has been taken from sources which we deem reliable. We do not represent that it is accurate or complete, and it should not be relied upon as such. Any opinions expressed herein reflect our judgment at this date and are subject to change.

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