# MARKET COMMENTARY

Sept 6, 2017

U.S. stocks ended a volatile and traditionally weak August with a five-day rally that pushed the S&P 500 fractionally above breakeven to extend positive returns for a 10th straight month. Volatility returned to Wall Street with the S&P 500 experiencing four separate sessions with moves of 1% or greater (two up and two down), ending months of relative calm. Worldwide investors were challenged by a series of unprecedented provocations by North Korea as Kim Jung Un ordered a resumption of ballistic missile launches, the latest of which flew over Japan, and was said to be a direct warning against Guam, the U.S. territorial Pacific island. Investor sentiment was also tested by Hurricane Harvey's deluge of record-setting rainfall in the greater Houston region and northward along a coastal path into southwest Louisiana. Harvey's disastrous and deadly outpouring, the worst rainfall event in U.S. history, knocked out upwards of 25% of U.S. refinery operations and spiked gasoline prices by nearly 14%. Yet solid corporate earnings, prospects for meaningful tax reform and an accelerating economy helped stave off bearish selling. Global markets also were energized by an upward revision of second quarter U.S. GDP growth from 2.6% to 3% and an increase in July consumer spending along with wage and salary gains.

Within the S&P 500, 6 of its 11 major sectors advanced in August, led by Technology (+3.47%), Utilities (+3.25%) and Healthcare (+1.85%). Energy (-5.18%) and Telecom (-3.02%) declined the most last month. On a YTD basis, Technology (+26.56%) and Healthcare (+19.13%) remain this year's best performing sectors, while Energy (-15.07%) and Telecom (-7.93%) once again are the only sectors that remain negative in 2017. Large cap stocks, as measured by the S&P 500, performed best in August, outperforming small and mid cap companies. Small cap companies, as measured by the Russell 2000 Index, fell 1.27% last month, while the Russell Mid Cap Index declined 0.78%. Large cap stocks also gained the most this year, up 11.9% YTD versus 8.73% for mid caps and 4.42% for small caps. Growth stocks outperformed value stocks in August, with the Russell 1000 Growth Index up 1.83%, while the Russell 1000 Value Index fell 1.16%. The outperformance in growth stocks has continued to widen on a year-to-date basis, with growth shares advancing 19.17% YTD, while value stocks trailed with a 4.81% YTD gain.

Hurt by the euro rising to a two-year high against the dollar, the MSCI EAFE Index, a broad performance measure of global developed markets outside the U.S. and Canada, underperformed relative to domestic equities last month, falling by 0.04%. Germany's DAX Index (-0.51%) fell for a third month in a row. In contrast, the MSCI Emerging Markets Index outperformed the U.S., posting a 2.23% gain in August. The MSCI All Country World Index excluding the U.S. rose 0.56% last month and 19.37% YTD.

Turning to bonds, prices on benchmark 10-year U.S. Treasury notes rallied in August, sending its yield lower by 18 basis points to end the month at a 2017 low of 2.118%. The Bloomberg Barclays U.S. Municipal Bond Index gained 0.76% last month, underperforming relative to the Bloomberg Barclays U.S. Aggregate Bond Index for only the second month since November 2016. The Aggregate Bond Index, a broader measure of U.S. investment grade bonds, advanced 0.9%. At the other end of the credit risk spectrum, the Bloomberg Barclays U.S. Corporate High Yield Index, a proxy for below-investment grade corporate bonds, slipped 0.04% in August, trimming its YTD gain to 6.05%.

Source: Tower Square Investment Management ®

## SUMMARY OF MAJOR ECONOMIC INDICATORS

| INDICATOR | LAST REPORT DATE | VALUE* | 6-MO. TREND | COMMENTS |
|---|---|---|---|---|
| U.S. Real GDP (ann. rate) * | Q2 2017 | 3.0% | ↑ | Second quarter GDP was revised up to 3.0%, after increases in personal consumption expenditures and nonresidential fixed investments were larger than previously estimated. |
| Global Real GDP Growth (ann. rate; Source: IMF) | Q2 2017 | 3.5% | n/a | The prospects for stronger global growth in 2017 are led by expectations of more robust global demand, reduced deflationary pressures and optimistic financial markets. |
| Non-Farm Employment Growth | Aug 2017 | 156,000 | ↓ | The U.S. added 156,000 jobs in August, with the largest gains occurring in manufacturing and construction. Wage growth was weak for the month, with average hourly earnings up only 0.1%. |
| Unemployment Rate | Aug 2017 | 4.4% | ↓ | The unemployment rate ticked up from its 16 year low in July. The labor force participation rate was unchanged and has shown little movement over the past year. |
| ISM Manufacturing Index | Aug 2017 | 58.8 | ↔ | Manufacturing activity expanded at its fastest pace in 6 years. The factory sector is on an undeniable upswing but construction spending saw an unexpected drop to a 9 month low. |
| ISM Non-Manufacturing Index | Aug 2017 | 55.3 | ↔ | Activity in service-related industries rebounded in August after the prior month's cooling-off period. Most sub-indices followed a similar pattern as the headline number. |
| Capacity Utilization | July 2017 | 76.7 | ↔ | Capacity utilization for the industrial sector was unchanged in July, remaining 3.2% below its long run average. Utilization for both mining and utilities increased, while manufacturing decreased. |
| Consumer Price Index (CPI, SA) | July 2017 | 0.1% | ↑ | The increase in CPI was led by gains in the indexes for shelter, medical care, and food, while the energy index declined slightly. The index for all items less food and energy also increased 0.1%. |
| Producer Price Index (Finished Goods, SA) | July 2017 | -0.1% | ↑ | Producer prices edged down in July, led by a 0.2% decrease in prices for final demand services. The index for final demand good also decreased slightly in July. |
| Leading Economic Indicators Index (LEI) | July 2017 | 0.3% | ↑ | A large negative contribution from housing permits was more than offset by gains in the financial, new orders, and sentiment indicators. |
| 10-year Treasury Yield | July 2017 | 2.12% | ↓ | The 10-year Treasury yield decreased by 14 basis points, as worries of a nuclear conflict with North Korea and a possible government shutdown pushed investors into safer assets. |

*NOTE: The "Value" column shows the most current level or change over the prior month or quarter.

## GLOBAL CAPITAL MARKETS: RETURNS AND PRICE LEVELS

| | August Close | August | Year- to-Date | 1 year | 3 years | 5 years |
|---|---|---|---|---|---|---|
| **US Indices** | | | | | | |
| Dow Jones 30 | 21,948 | 0.65% | 13.01% | 22.29% | 11.46% | 13.70% |
| S&P 500 | 2,472 | 0.31% | 11.93% | 16.23% | 9.54% | 14.34% |
| Nasdaq | 6,429 | 1.43% | 20.34% | 24.73% | 13.30% | 17.40% |
| Russell 2000 | 1,405 | -1.27% | 4.42% | 14.91% | 7.67% | 13.15% |
| **International Indices** | | | | | | |
| MSCI EAFE (Developed) | 7,609 | -0.02% | 17.50% | 18.19% | 3.31% | 8.97% |
| MSCI EM (Emerging) | 2,355 | 2.27% | 28.62% | 24.99% | 2.75% | 5.67% |
| **US Fixed Income** | | | | | | |
| Bloomberg Barclays US Aggregate | --- | 0.90% | 3.64% | 0.49% | 2.64% | 2.19% |
| Bloomberg Barclays US TIPS | --- | 1.06% | 2.38% | 0.46% | 0.98% | 0.25% |
| **Commodities and Real Estate** | | | | | | |
| Bloomberg Commodity Index | 172 | 0.40% | -2.72% | 2.99% | - 12.27% | - 10.14% |
| Crude Oil ($/bbl) | --- | $47.23 | $53.72 | $44.70 | $95.96 | $96.47 |
| DJ US Select REIT | 9,529 | -0.79% | 1.48% | -3.13% | 7.03% | 8.67% |

**Sources:** Bloomberg, MSCI. Non-US index returns are shown in US Dollar terms and are considered to be currency unhedged. Total returns include dividend and income accruals and price changes. Returns for three and five years are annualized and assume the reinvestment of interest and dividend payments. Investors cannot invest directly in any of the above indices. The performance of any index is not indicative of the performance of any investment and does not take into account the effects of inflation and the fees and expenses associated with investing.

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GLOSSARY
*The **Bloomberg Barclays Capital U.S. Aggregate Bond Index**, which was originally called the Lehman Aggregate Bond Index, is a broad based flagship benchmark that measures the investment grade, US dollar-denominated, fixed-rate taxable bond market. The index includes Treasuries, government–related and corporate debt securities, MBS (agency fixed-rate and hybrid ARM pass-throughs), ABS and CMBS (agency and non-agency) debt securities that are rated at least Baa3 by Moody's and BBB- by S&P. Taxable municipals, including Build America bonds and a small amount of foreign bonds traded in U.S. markets are also included. Eligible bonds must have at least one year until final maturity, but in practice the index holdings has a fluctuating average life of around 8.25 years. This total return index, created in 1986 with history backfilled to January 1, 1976, is unhedged and rebalances monthly.*
*The **Bloomberg Barclays US Municipal Bond Index** covers the USD-denominated long-term tax exempt bond market. The index has four main sectors: state and local general obligation bonds, revenue bonds, insured bonds, and pre-refunded bonds. Many of the sub-indicies of the Municipal Index have historical data to January 1980. In addition, several su-bindicies based on maturity and revenue source have been created, some with inception dates after January 1980, but no later than July 1, 1993. Eligible securities must be rated investment grade (Baa3/BBB- or higher) by Moody's and S&P and have at least one year until final maturity, but in practice the index holdings has a fluctuating average life of around 12.8 years. This total return index is unhedged and rebalances monthly.*
*The **Bloomberg Barclays US Corporate High Yield Index** measures the USD-denominated, non-investment grade, fixed rate, taxable corporate bond market. Securities are classified as high yield if the middle rating of Moody's, Fitch, and S&P is Ba1/BB+/BB+ or below, excluding emerging market debt. Payment-in-kind and bonds with predetermined step-up coupon provisions are also included. Eligible securities must have at least one year until final maturity, but in practice the index holdings has a fluctuating average life of around 6.3 years. This total return unhedged index was created in 1986, with history backfilled to July 1, 1983 and rebalances monthly.*
*The **CBOE Volatility Index® (VIX®)** is a key measure of market expectations of near-term volatility conveyed by S&P 500 stock index option prices. Introduced in 1993, the VIX Index has been considered by many to be the world's premier barometer of investor sentiment and market volatility.*
*The **MSCI EAFE** is designed to measure the equity market performance of developed markets (Europe, Australasia, Far East) excluding the U.S. and Canada. The Index is market-capitalization weighted.*
*The **MSCI Emerging Markets** is designed to measure equity market performance in global emerging markets. It is a float-adjusted market capitalization index.*
*The **MSCI ACWI Excluding the U.S.** is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of developed and emerging markets without the inclusion of the United States. The MSCI full ACWI consists of 46 country indexes comprising 23 developed and 23 emerging market country indexes. The developed market country indexes included are: Australia, Austria, Belgium, Canada, Denmark, Finland, France, Germany, Hong Kong, Ireland, Israel, Italy, Japan, Netherlands, New Zealand, Norway, Portugal, Singapore, Spain, Sweden, Switzerland, the United Kingdom and the United States. The emerging market country indexes included are: Brazil, Chile, China, Colombia, Czech Republic, Egypt, Greece, Hungary, India, Indonesia, Korea, Malaysia, Mexico, Peru, Philippines, Poland, Qatar, Russia, South Africa, Taiwan, Thailand, Turkey* and United Arab Emirates.*

*The **Russell 1000 Growth Index** measures the performance of the large-cap growth segment of the U.S. equity universe. It includes those Russell 1000 Index companies with higher price-to-book ratios and higher forecasted growth values.*
*The **Russell 1000 Value Index** measures the performance of the large-cap value segment of the U.S. equity universe. It includes those Russell 1000 Index companies with lower price-to-book ratios and lower forecasted growth values.*
*The **Russell 2000 Index** measures the performance of the small-cap segment of the U.S. equity universe and is a subset of the Russell 3000 Index representing approximately 10% of the total market capitalization of that index. It includes approximately 2000 of the smallest securities based on a combination of their market cap and current index membership.*
*The **Russell 3000** Index measures the performance of the largest 3,000 U.S. companies representing approximately 98% of the investable U.S. equity market.*
*The **Russell Mid Cap Index** measures the performance of the mid-cap segment of the U.S. equity universe and is a subset of the Russell 1000 Index. It includes approximately 800 of the smallest securities based on a combination of their market cap and current index membership. The Russell Midcap represents approximately 31% of the total market capitalization of the Russell 1000 companies.*
*The **S&P 500** is a capitalization-weighted index of 500 stocks designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries.*
*The **Dow Jones Industrial Average** is a price-weighted average of 30 significant stocks traded on the New York Stock Exchange and the NASDAQ.*
*The **NASDAQ Composite Index** includes all domestic and international based common type stocks listed on The NASDAQ Stock Market. The NASDAQ Composite Index is a broad-based capitalization-weighted index.*
*The **U.S. Dollar Index** is a weighted geometric mean that provides a value measure of the United States dollar relative to a basket of major foreign currencies. The index, often carrying a USDX or DXY moniker, started in March 1973, beginning with a value of the U.S. Dollar Index at 100.000. It has since reached a February 1985 high of 164.720, and has been as low as 70.698 in March 2008.*