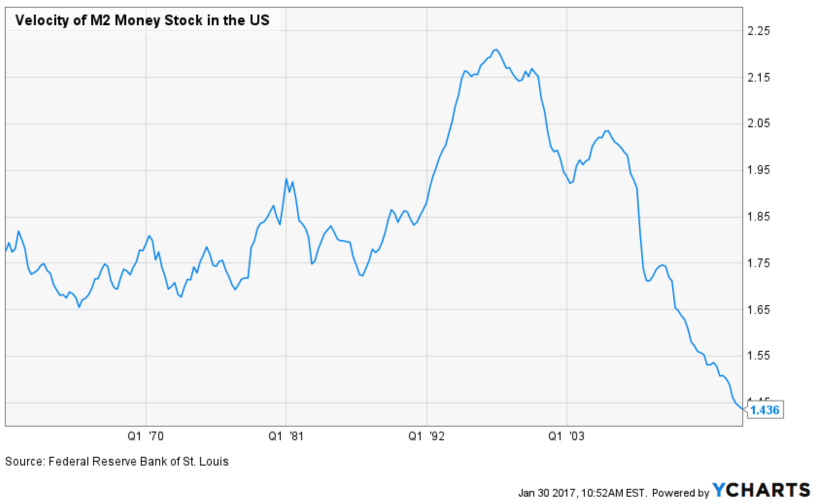
Monthly Newsletter

February 2017

COMMENTARY

So far in 2017, one of the more interesting charts we've been watching is the velocity of money. Velocity of money is defined as the rate at which money is exchanged from one transaction to another and how much a unit of currency is used in a given period of time, as explained in the following two examples.



Situation 1 - Person A has one dollar and decides to spend it on a widget or service that Person B makes or provides (transaction 1). Now Person B has that dollar and decides they want to spend it on something from Person C (transaction 2). Person C now has that dollar and spends it (transaction 3). This would equal a velocity of three and that one dollar financed $3 worth of transactions over a given time period.

Situation 2 - Person A still spends the dollar and gives it to person B (transaction 1). Person B spends that dollar (transaction 2), but person C decides not to spend that dollar. In situation 2, the velocity is only two and financed just $2 worth of transactions.

So how do we apply this to our current economic state? We believe the velocity of money will be an indicator of confidence coming back to individuals and businesses. When these groups have monetary confidence, we expect more money will be spent on goods and services, which will increase transactions. Right now the velocity of money is at the lowest level since 1959. We don't need to see the velocity of money get back to its historical average (1.83) to make a difference, but we want to see it turn higher and start making its way back to that level. This chart offers a long-term view and opportunity for the markets that will likely play out over 5 - 15 years. Ultimately, as people and businesses begin to feel more confident, the US economy and the stock market will benefit.

For the better part of December and January, the market has been pretty quiet. After Trump secured the presidential election, the market rallied upwards, pricing in the possibilities of positive economic agendas (tax cuts, infrastructure spending, and deregulations, for example). Is the market waiting to learn more details before it moves from here?

Is the market waiting to hear what the Federal Open Market Committee (FOMC) is going to say next? Maybe the market is still digesting this recent earnings cycle? Whatever the case may be, it's short-term in our view, and our long-term views remain positive.

(cont. on reverse)

ECONOMIC HIGHLIGHTS

S&P 500	2,278.87
DJIA	19,864.09
NASDAQ	5,614.79
Oil	$52.81/barrel
Gold	$1,211.40/ounce
10 Year Treasury Yield	2.45%
Unemployment	4.7%
GDP	1.9%
Consumer Price Index (CPI)	+0.3% 12 month change: +2.1%
Core CPI	+0.2% 12 month change: +2.2%

☺ **ISM Manufacturing Index** - This composite index indicates the overall factory sector had a very strong December, coming in at 54.7 (above 50 is good and below 50 is bad). After struggling for most of 2016, it's positive to see the factory sector improving on its first report in 2017.

😐 **GDP** - After very strong third quarter GDP numbers, the first estimate on fourth quarter numbers were on the low side of the consensus range, coming in at 1.9% annualized.

☹ **Europe** - All signs point to the U.K. leaving the European Union's single market and negotiating individual topics as it seeks the best possible outcome on each. These negations could greatly affect growth in Europe. Does the EU play hardball?

(cont.)

Many economic and technical indicators point to a bullish economy and stock market. US large cap stocks have been performing well the last two years and we expect this to continue but also believe that small- and mid-caps are positioned to take the lead as risk appetite increases. An improving economy and strong balance sheets for US consumers and businesses should continue to drive the economy forward. One negative feature of a strong economy is a strong dollar, which can cause headwind for large multinational companies. This is another reason we see small-cap companies as well-positioned, as they tend to be less effected by a strong dollar. Sector-wise, we are bullish on Technology, Industrials, and Financials, but are cautious in Utilities, Health Care, and Consumer Staples; in addition, Brexit still looms over Europe and international developed markets. We are maintaining our defensive approach with our product selection in international developed markets, and are in wait-and-see mode for more news and information before we make additional changes. We are looking for fair negotiations between the U.K. and European Union, and believe that Quantitative Easing should improve balance sheets for consumers and businesses (similar to the US). Emerging markets valuations look very attractive, and we do believe there will be an opportunity to benefit from these valuations, but again we are in a wait-and-see mode regarding Trump and his policies on trade agreements. Treasury yields are trading at 2.45% and are up over a percent from the lows in July (1.33%). Our fixed income positions have been weighted towards low duration, which historically tend to do better in a rising interest rate environment; we believe this is still the best positioning, as we think rates have more room to go. Quantitative easing from banks around the world has held interest rates below what we believe they should be. We continue to be tactically underweight to government bonds and overweight to corporate, high yield, floating rate, and global bonds. With our daily monitoring we'll continue to rebalance models when they fall outside their target threshold.

Economic Highlights

Index	3 Mo	1 Yr	3 Yr	5 Yr
S&P 500	7.76	20.04	10.85	14.09
MSCI EAFE	4.34	12.59	1.17	6.52
BarCap Agg Bond	-2.04	1.45	2.59	2.09

Data as of 1/31/2017. Investments cannot be made directly into an index.

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