

# CAPITAL MARKET REVIEW

Second Quarter 2017



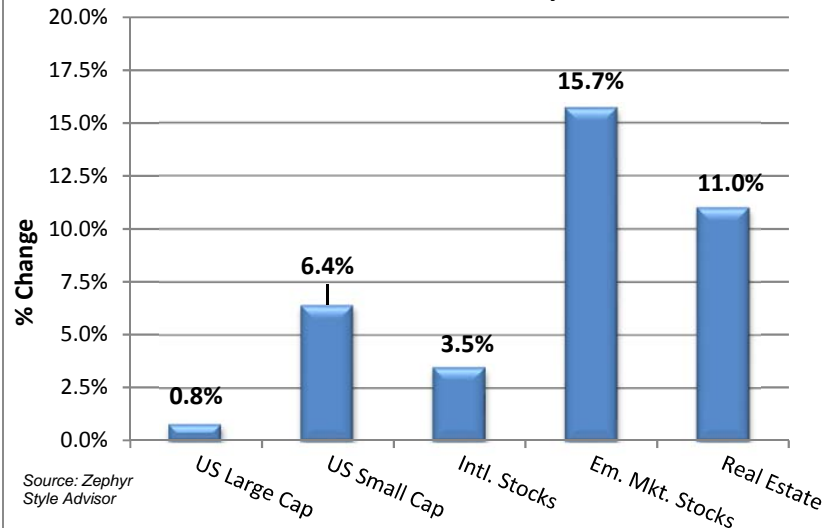
# The Economy

**The lost decade.** Back in 2010 there was a great deal of talk about how the United States stock market had gone nowhere for a decade. Between the busting of the technology bubble and the 2008 financial crisis it is somewhat of a miracle that stock returns were actually flat. Ignored in all that talk was the fact that the decade had been a very good one for international investing, especially in emerging markets.

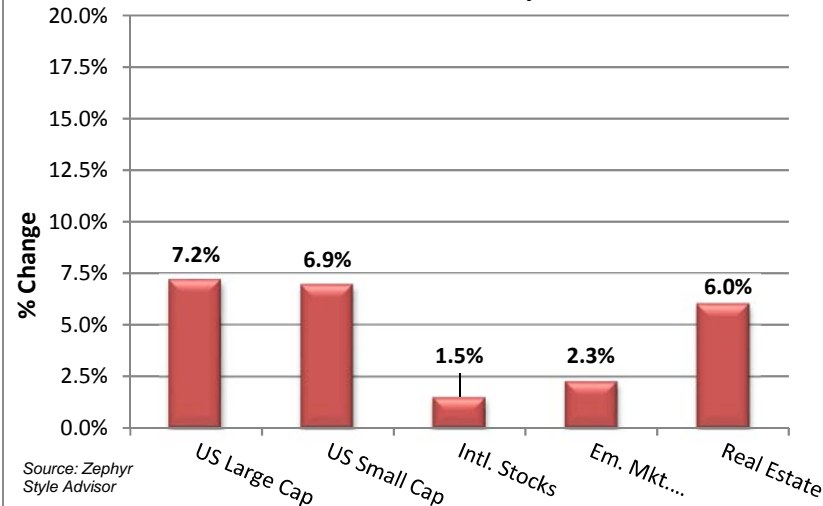
Fast forward seven years and we now find ourselves at the top of a very old bull market in US stocks. In the meantime the return for the international benchmark, MSCI EAFE, over the last decade has been 1.5 percent annualized. The rest of the world has now experienced a lost decade.

Markets move in long term trends. Are we at the end of the US bull market or the beginning of an international bull market? Only time will tell for sure but the possibility cannot be ignored. The EAFE is up 14.22 percent year to date versus 9.34 for the S&P 500. Emerging market stocks as measured by the MSCI EM are up 18.60 percent. Global diversification is working once again and if history is a guide this could go on for some time.

### 10 Year Returns, 2010



### 10 Year Returns, Current



10 year return figures annualized. Performance as of November 2010 and June 2017  
 Indices used are S&P 500 (US Large Cap), Russell 2000 (US Small Cap), MSCI EAFE (International Stocks), MSCI Em (Emerging Markets Stocks), and Nareit Equity (Real Estate)

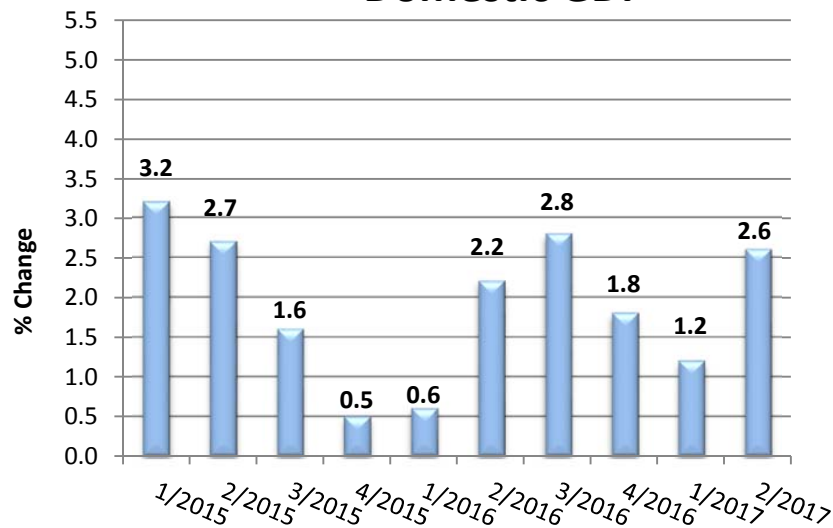
# The Economy

The 1st quarter 2017 GDP growth came in at 1.2 percent and second quarter's first estimate is 2.6 percent. The optimism for more pro-growth policies has waned because of doubts about the administration's ability to get their policies through congress.

The official unemployment rate dropped to 4.4 percent in June. The labor market is continuing to grow in strength.

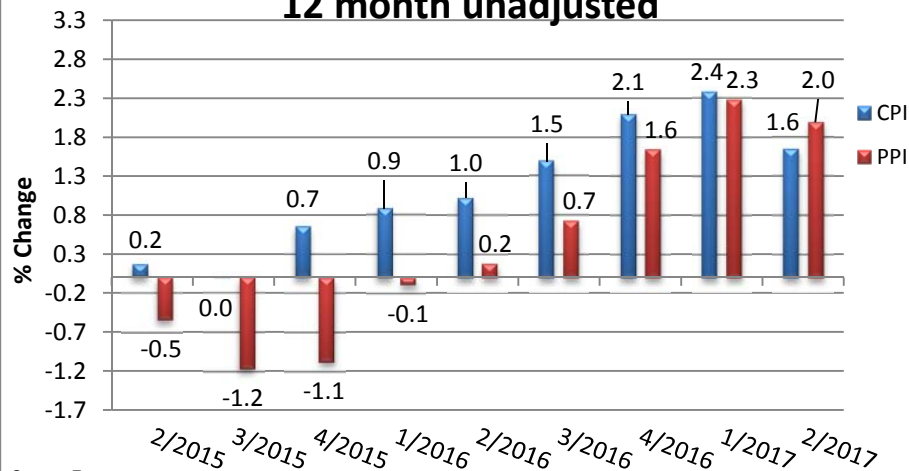
Inflation had kicked up but the latest readings are showing no growth. The Fed continues to raise rates and is unlikely to change course even with inflation showing signs of slowing.

## Domestic GDP



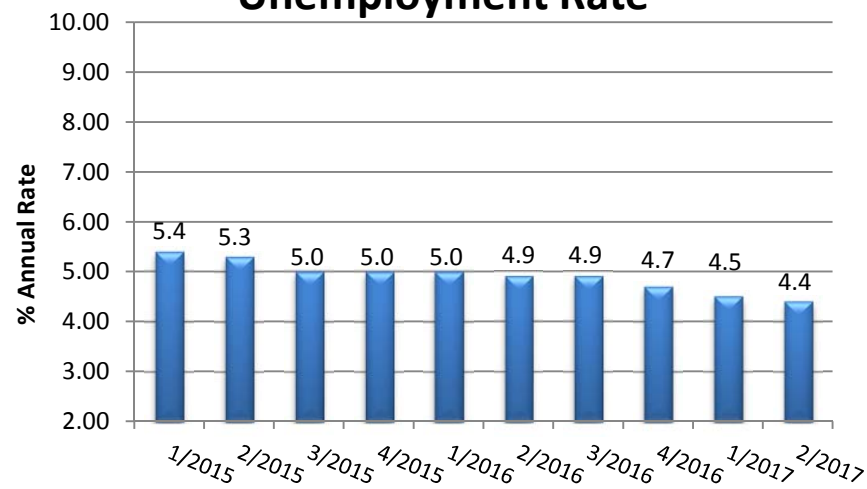
Source: Factset

## Inflation Indicator 12 month unadjusted



Source: Factset

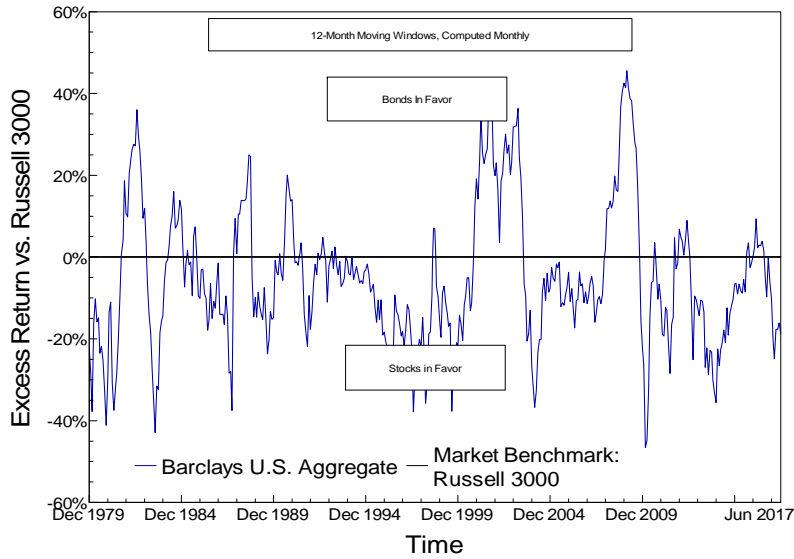
## Unemployment Rate



Source: Factset

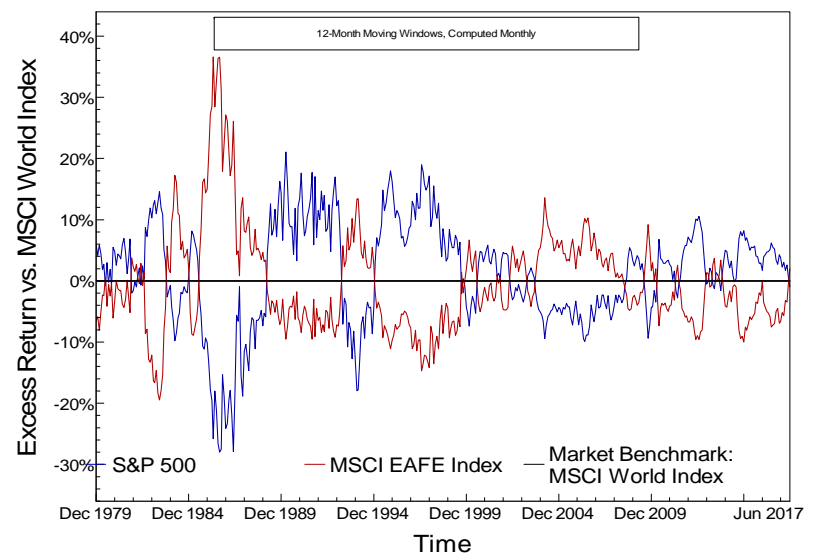
### Bonds vs. Stocks

Zephyr StyleADVISOR: Iron Capital Advisors



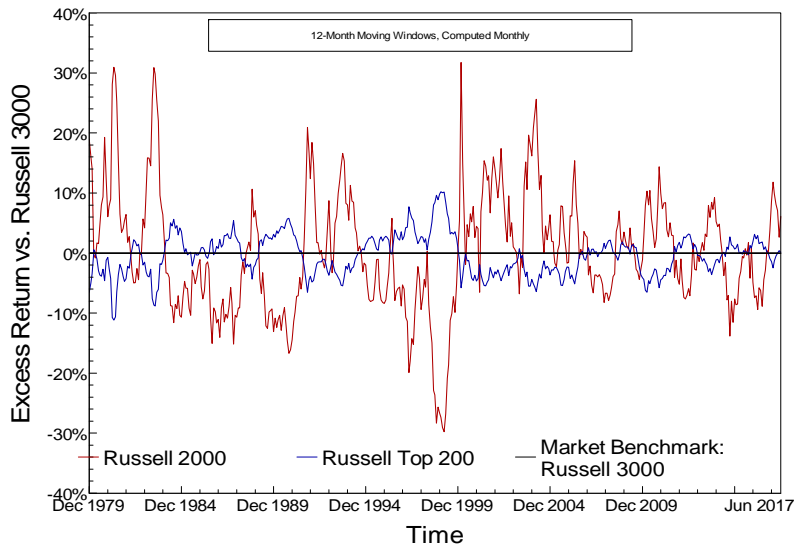
### International Vs. Domestic

Zephyr StyleADVISOR: Iron Capital Advisors

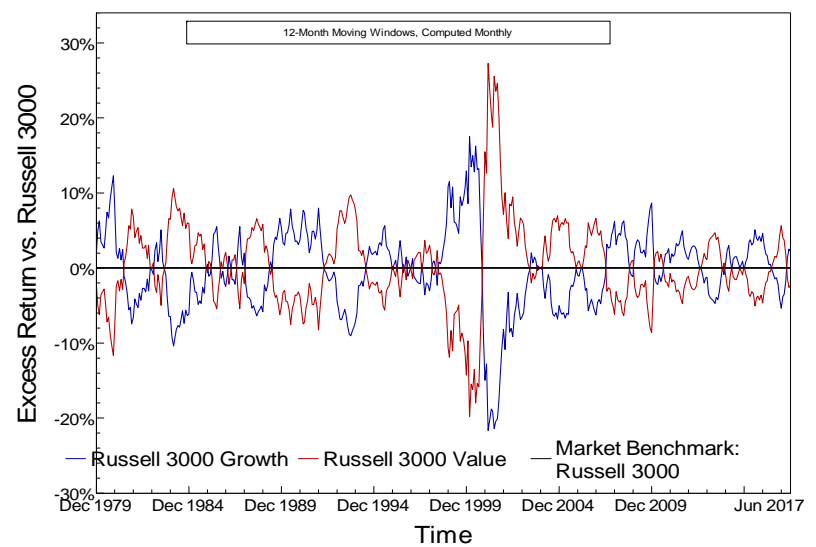


### Large vs. Small

Zephyr StyleADVISOR: Iron Capital Advisors



### Value vs. Growth



# Domestic Equity Markets

**The rally continues.** For the quarter the S&P 500 was up 3.09 percent. Growth outpaced value for the second quarter in a row. The Russell 1000 Growth index finished up 4.67 percent, while its value counterpart was up 1.34 percent. Small companies held their own with the Russell 2000 index finishing up 2.46 percent.

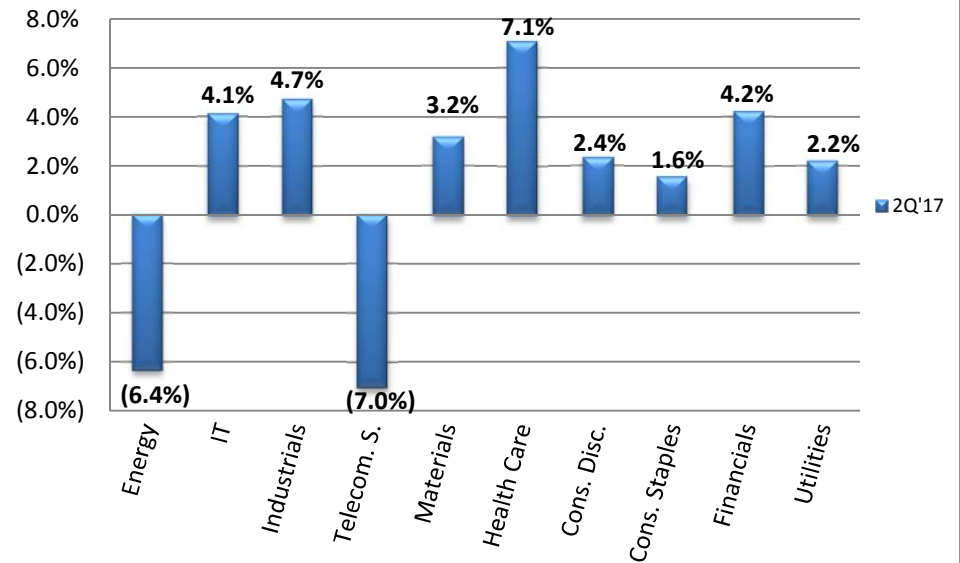
Health care led the way, followed by industrials, financials and technology. That is a pretty broad based market move and active managers were for the most part rewarded.

Telecoms and energy were the worst place to be. Oil dropped, although it never really got below the current trading range and telecoms are seeing pricing pressure on the mobile front.

## Domestic Indices Three Months Ending June 30, 2017

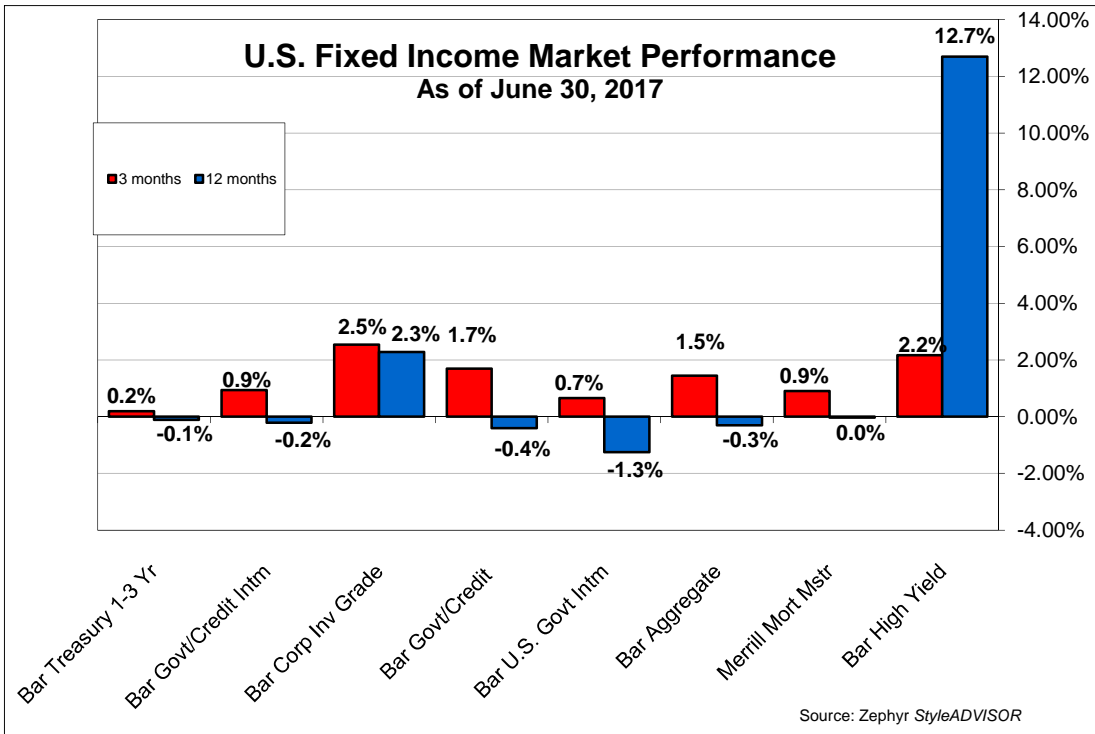
	Yield	Price/Earnings	Price/Book
S&P 500	1.90%	21.7	3.07
Russell 1000 Gr	1.33%	26.3	6.53
Russell 1000 Val	2.34%	19.5	1.98
Russell Midcap	1.62%	25.4	2.72
Russell 2000 Gr	0.68%	64.7	4.43
Russell 2000 Va	1.93%	32.1	1.49

## S&P GICS Sector Returns



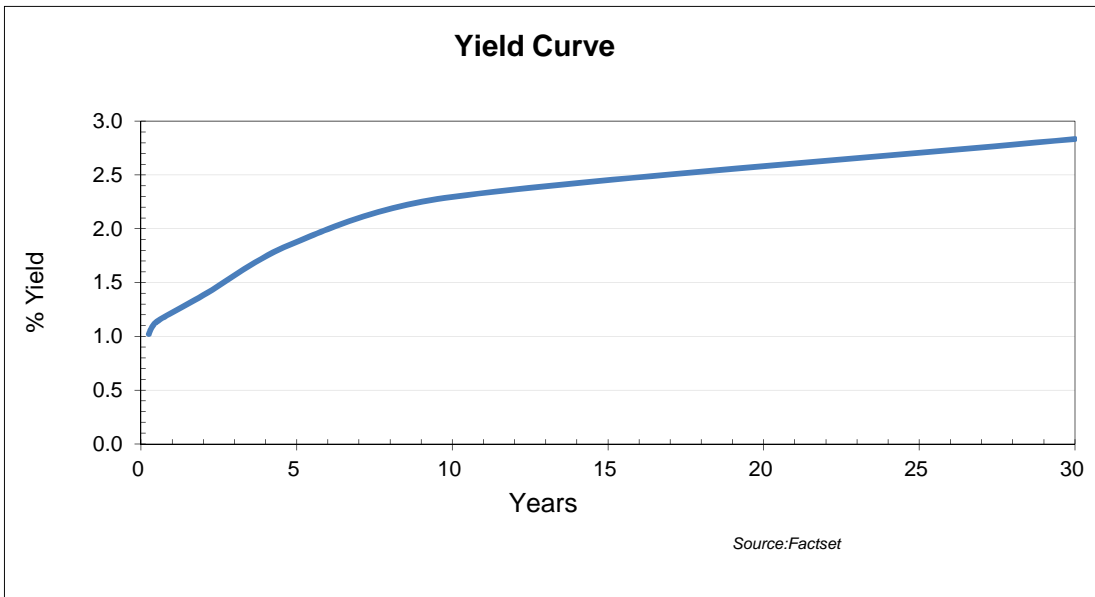
Source: Factset

# DOMESTIC FIXED INCOME MARKET



Bonds rose slightly during the quarter. The Barclays US Aggregate Bond index ended up 1.45 percent. High yield bonds ended the quarter up 2.16 percent.

Interest rates remain in a trading range even with the Fed continuing to raise their base rate. Last quarter the 10 year yield was 2.39 percent and now it is 2.3 percent. There is lots of noise but not much real movement.



## Yield Curve as of June 30, 2017

Time to Maturity	Interest Rate
3 Month	1.02
6 Month	1.13
2 Year	1.38
5 Year	1.88
10 Year	2.30
30 Year	2.83

# INTERNATIONAL MARKETS

**International stocks led the way.** The EAFE index finished up 6.37 percent and the MSCI Emerging Markets index ended the quarter up 6.38 percent.

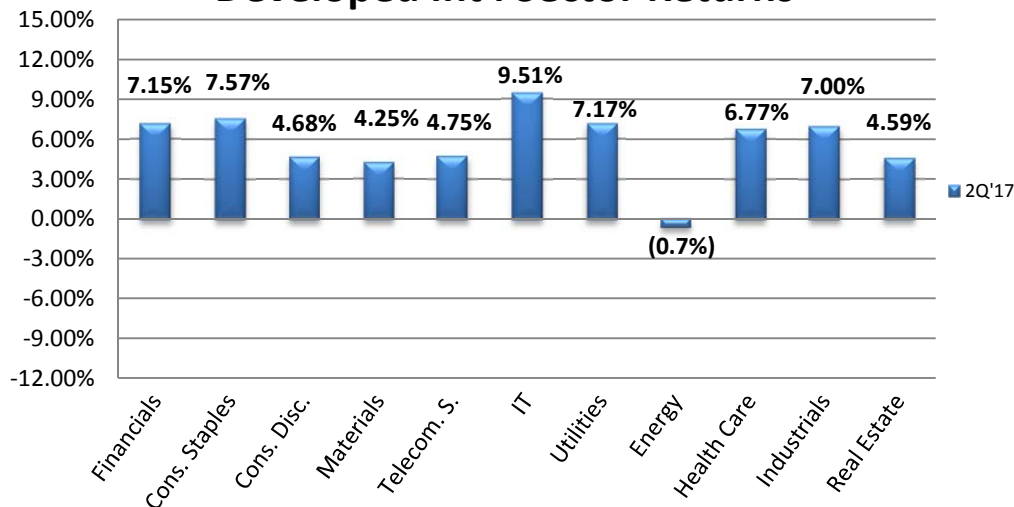
Much of this move was based on currency. The Europe markets were up 7.73 percent for US investors but only 2.14 percent in local terms. The ECB is following the Fed's lead and beginning to reverse its easy policy. At the same time the growth friendly policies in the US have not materialized. This has led to an increase in the Euro.

Currency movements tend to balance out over the longer term. More importantly our work indicates that while the market price of international stocks has increased, their valuations have actually gotten more attractive. This means that company earnings are actually growing faster than the stock prices. We have gone through a decade of US dominance, this is a sign that the trend may be shifting towards international.

## MSCI Country Returns Three Months Ending June 30, 2017

	Return US\$ (%)	Return Local Currency (%)	Currency Effect(%)
Austria	22.05%	14.46%	7.59%
Belgium	5.53%	-1.04%	6.57%
Denmark	15.39%	8.18%	7.21%
Finland	14.35%	7.23%	7.12%
France	9.86%	3.02%	6.84%
Germany	6.92%	0.27%	6.65%
Ireland	3.84%	-2.62%	6.46%
Italy	9.59%	2.77%	6.82%
Netherlands	8.06%	1.87%	6.19%
Norway	4.77%	2.18%	2.59%
Portugal	4.07%	-2.40%	6.47%
Spain	8.09%	1.36%	6.73%
Sweden	9.05%	3.02%	6.03%
Switzerland	9.41%	4.68%	4.73%
UK	4.74%	0.83%	3.91%
<b>Europe Total</b>	<b>7.73%</b>	<b>2.14%</b>	<b>5.59%</b>
Australia	-1.81%	-2.35%	0.54%
Hong Kong	7.19%	7.63%	-0.44%
Japan	5.23%	6.10%	-0.87%
New Zealand	8.07%	3.18%	4.89%
Singapore	5.27%	3.75%	1.52%
<b>Pacific Total</b>	<b>3.95%</b>	<b>4.40%</b>	<b>-0.45%</b>
Brazil	-6.61%	-2.54%	-4.07%
Canada	0.82%	-1.82%	2.64%
China	10.66%	11.03%	-0.37%
Greece	34.01%	25.66%	8.35%
Hungary	19.37%	12.04%	7.33%
India	2.91%	2.44%	0.47%
Indonesia	8.75%	8.77%	-0.02%
Korea	10.26%	12.81%	-2.55%
Mexico	7.31%	3.13%	4.18%
Poland	13.81%	6.53%	7.28%
Russia	-9.81%	-6.00%	-3.81%
Thailand	2.53%	1.36%	1.17%
<b>Emerging Markets</b>	<b>6.38%</b>	<b>6.68%</b>	<b>-0.30%</b>

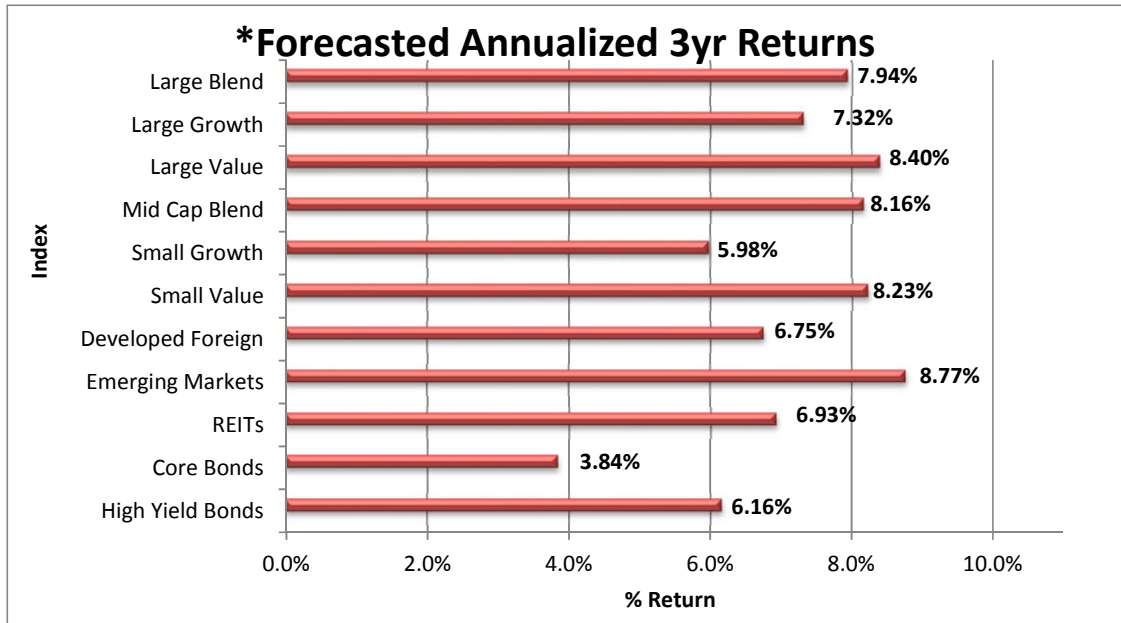
## Developed Int'l Sector Returns\*



Source: Harbor Capital

\* MSCI EAFE Index

## Market Forecast



**The rally remains due for a pause.** The rotation back to growth reflects the lack of confidence in the administration's ability to get anything done. The hope for more growth friendly policies needs to be fueled by some actual policies. We remain optimistic for the year but would not be surprised if we have a short-term slow down.

Emerging markets still look attractive and the rally in international stocks should have more legs.

Bonds remain our biggest concern over the long term and will until the yield on the 10 year treasury exceeds 3 percent. The run in high yield bonds will likely slow down, but not stop.

### Indices Three Months Ending June 30, 2017

	Yield	Frwd Earnings Yield	**Hist. Return	***Hist. Risk Prem. + RF Rate
Large Blend	1.90%	7.61%	10.22%	6.11%
Large Growth	1.33%	6.22%	9.99%	6.11%
Large Value	2.34%	8.71%	10.28%	6.11%
Mid Cap Blend	1.62%	7.17%	11.54%	6.11%
Small Growth	0.68%	3.61%	8.03%	7.11%
Small Value	1.93%	7.18%	10.74%	7.11%
Developed Foreign	2.79%	9.59%	5.48%	4.24%
Emerging Markets	2.00%	10.11%	10.00%	5.74%
REITs	3.72%	5.94%	10.49%	4.68%
Core Bonds	2.56%	2.56%	6.37%	3.01%
High Yield Bonds	6.06%	6.06%	8.29%	4.18%

\* Weighted average using 40% earnings yield, 30% historic return and 30% historic risk premium + RF rate

\*\*Annualized 29 Yr return

\*\*\*Hist. risk premium of domestic and international equity as defined by Zephyr Style Advisor's GFD Long Term Index database except for REITs and High Yield which are based on average 20 year rolling returns of the NAREIT Equity REIT Index and the Barclays Corporate High Yield Index minus the average 20 year rolling returns of the 3-month T-Bill and scaled using proprietary data. The Current 3-month T-Bill yield (as of 06-30-2016) is added back to each risk premium.



## SELECTED INDEX RETURNS - PERIODS ENDING June 30, 2017

	Quarter	Year-to-Date	One Year	Three Years	Five Years	Ten Years
<b>US EQUITIES</b>						
Broad Stock Market - Russell 3000	3.02%	8.93%	18.51%	9.10%	14.58%	7.26%
Large Stocks - S&P 500	3.09%	9.34%	17.90%	9.61%	14.63%	7.18%
Dow Jones Industrial Average	3.95%	9.35%	22.12%	11.01%	13.45%	7.57%
Medium-Size Stocks - Russell Mid-Cap	2.70%	7.99%	16.48%	7.69%	14.72%	7.67%
Small Stocks - Russell 2000	2.46%	4.99%	24.60%	7.36%	13.70%	6.92%
Small Value Stocks- Russell 2000 Value	0.67%	0.54%	24.86%	7.02%	13.39%	5.92%
Small Growth Stocks- Russell 2000 Growth	4.39%	9.97%	24.40%	7.64%	13.98%	7.82%
Large Value Stocks - Russell 1000 Value	1.34%	4.66%	15.53%	7.36%	13.94%	5.57%
Large Growth Stocks - Russell 1000 Growth	4.67%	13.99%	20.42%	11.11%	15.30%	8.91%
<b>US FIXED INCOME</b>						
1-3 Yr Treasury (Gov't) Bonds - Barclays Capital	0.19%	0.46%	-0.11%	0.70%	0.64%	1.96%
US Government Bonds Int - Barclays Capital	0.66%	1.20%	-1.25%	1.47%	1.07%	3.39%
US Corporate Inv Grade Bonds - Barclays Capital	2.54%	3.80%	2.28%	3.61%	3.96%	5.79%
Government/Credit (Corp) Bonds - Barclays Capital	1.69%	2.66%	-0.41%	2.62%	2.29%	4.57%
Int Govt/Credit (Corp) Bond - Barclays Capital	0.94%	1.73%	-0.21%	1.92%	1.77%	3.87%
US Aggregate Bond Market - Barclays Capital	1.45%	2.27%	-0.31%	2.48%	2.21%	4.48%
Mortgage Master - Merrill Lynch	0.90%	1.37%	-0.03%	2.15%	1.98%	4.34%
US Corp High Yield Bonds - Barclays Capital	2.17%	4.93%	12.70%	4.48%	6.89%	7.67%
<b>INTERNATIONAL (Measured in US Dollars)</b>						
Non-US Stocks - MSCI EAFE	6.37%	14.22%	20.83%	1.61%	9.18%	1.50%
World Stocks (includes US) - MSCI World	4.22%	11.02%	18.86%	5.83%	12.01%	4.56%
European Stocks - MSCI Europe	7.73%	15.93%	21.81%	0.34%	9.44%	1.23%
Japanese Stocks - MSCI Japan	5.23%	10.11%	19.58%	5.87%	9.86%	1.42%
Asian Stocks (Ex-Japan) - MSCI Pacific ex-Japan	1.58%	13.55%	19.58%	1.38%	6.86%	3.83%
Chinese Stocks - MSCI China	10.66%	24.96%	32.34%	8.29%	9.20%	4.24%
Indian Stocks - MSCI India	2.91%	20.53%	17.47%	4.27%	9.03%	3.06%
Emerging Markets - MSCI EM	6.38%	18.60%	24.17%	1.44%	4.33%	2.25%
Int'l Gov't Bonds -Citi World Gov't Bond (Non USD)	3.81%	5.91%	-5.01%	-2.20%	-0.80%	3.21%
<b>REAL ESTATE</b>						
FTSE NAREIT Equity-Reits Index	1.52%	2.70%	-1.70%	8.36%	9.52%	6.00%
<b>SHORT TERM INTEREST RATES</b>						
T-Bills	0.18%	0.30%	0.46%	0.20%	0.15%	0.51%

Note: Returns for periods longer than 12 months are annualized.