

Q4 2017 Economic Commentary and Market Update

Index Performance as of: 12/31/2017

	<u>3 Month</u>	<u>YTD</u>	<u>1 Year</u>	<u>3 Year</u>	<u>5 Year</u>	<u>10 Year</u>
Russell						
3000 Value	5.08	13.19	13.19	8.71	13.95	7.19
3000	6.34	21.13	21.13	11.12	15.58	8.60
3000 Growth	7.61	29.59	29.59	13.51	17.16	9.93
1000 Value	5.33	13.66	13.66	8.65	14.04	7.10
1000	6.59	21.69	21.69	11.22	15.71	8.59
1000 Growth	7.86	30.21	30.21	13.78	17.33	10.00
Mid Cap Value	5.50	13.34	13.34	9.00	14.68	9.10
Mid Cap	6.07	18.52	18.52	9.58	14.96	9.11
Mid Cap Growth	6.81	25.27	25.27	10.29	15.31	9.10
2000 Value	2.05	7.84	7.84	9.54	13.01	8.17
2000	3.34	14.65	14.65	9.95	14.12	8.71
2000 Growth	4.59	22.17	22.17	10.28	15.21	9.19
Standard & Poors						
S&P 500	6.64	21.83	21.83	11.41	15.79	8.50
Consumer Disc	9.87	22.98	22.98	12.81	17.64	13.52
Consumer Staples	6.49	13.49	13.49	8.43	13.28	10.07
Energy	6.02	-1.01	-1.01	-0.18	2.78	1.16
Financials	8.63	22.18	22.18	13.89	18.22	3.78
Health Care	1.47	22.08	22.08	8.28	17.62	11.02
Industrials	6.05	21.03	21.03	11.92	16.72	8.63
Information Technology	9.01	38.83	38.83	18.74	20.90	11.90
Materials	6.93	23.84	23.84	9.80	12.20	6.17
Real Estate	3.22	10.85	10.85	6.26	9.68	7.46
Telecom Services	3.61	-1.25	-1.25	8.03	7.68	5.07
Utilities	0.21	12.11	12.11	7.45	12.62	6.31
Other U.S. Equity						
Dow Jones Industrial Avg.	10.96	28.11	28.11	14.36	16.37	9.28
Wilshire 5000 (Full Cap)	6.37	21.00	21.00	10.91	15.43	8.63
International Equity - Broad Market						
MSCIEAFE	4.23	25.03	25.03	7.79	7.90	1.94
MSCIEM	7.44	37.28	37.28	9.10	4.35	1.68
MSCIFrontier Markets	5.61	31.86	31.86	5.01	9.27	-1.35
MSCIACWI	5.73	23.97	23.97	9.29	10.80	4.65
MSCIACWIEx USA	5.00	27.19	27.19	7.83	6.80	1.84
MSCIAC Asia Ex Japan	8.23	41.72	41.72	10.72	7.95	3.82

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International Equity - Country Region						
MSCI Brazil	-1.99	24.11	24.11	6.55	-2.68	-3.15
MSCI BRIC	6.61	41.75	41.75	11.21	5.21	-0.22
MSCI China	7.62	54.07	54.07	12.73	9.90	2.98
MSCI Europe	2.21	25.51	25.51	6.69	7.37	1.34
MSCI India	11.82	38.76	38.76	8.69	8.87	0.49
MSCI Japan	8.49	23.99	23.99	11.62	11.16	3.17
MSCI EM Latin America	-2.34	23.74	23.74	3.80	-3.20	-1.67
MSCI Russia	4.26	5.20	5.20	19.28	-1.68	-6.09
Fixed Income						
Barclays U.S. Aggregate	0.39	3.54	3.54	2.24	2.10	4.01
BofAML 3-Month T-Bill	0.28	0.86	0.86	0.41	0.27	0.39
Barclays U.S. Gov't	0.05	2.30	2.30	1.40	1.28	3.23
Barclays U.S. Credit	1.05	6.18	6.18	3.63	3.24	5.42
Barclays High Yield Corp.	0.47	7.50	7.50	6.35	5.78	8.03
Barclays TIPS	1.26	3.01	3.01	2.05	0.13	3.53
Barclays Global Aggregate	1.08	7.39	7.39	2.02	0.79	3.09
Barclays Gbl Agg Ex USD	1.63	10.51	10.51	1.77	-0.20	2.40
JPM GBI-EM Global Div	0.82	15.21	15.21	2.53	-1.55	3.56
JPM EMBI Global	0.54	9.32	9.32	6.83	3.75	7.06
JPM EMBI Global Div	1.16	10.26	10.26	7.11	4.58	7.29
Fixed Income-Tax Exempt						
Barclays Municipal	0.75	5.45	5.45	2.98	3.02	4.46
Barclays Municipal 3 Yr	-0.77	1.56	1.56	0.94	1.07	2.36
Barclays Municipal 5 Yr	-0.70	3.14	3.14	1.71	1.83	3.54
Barclays Municipal 7 Yr	-0.22	4.49	4.49	2.40	2.44	4.31
Barclays HY Muni	1.83	9.69	9.69	4.77	4.35	5.25
Alternative Investments						
Alerian MLP	-0.95	-6.52	-6.52	-9.32	-0.06	6.05
Bloomberg Commodity	4.71	1.70	1.70	-5.03	-8.45	-6.83
FTSENAREIT Equity REIT	1.51	5.23	5.23	5.62	9.46	7.44
S&P Global Natural Res.	8.59	22.66	22.66	7.23	2.50	-0.38
S&P N. Amer Natural Res.	5.94	1.23	1.23	0.11	1.07	-0.23

Source: Morningstar

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Recap: The U.S. economy will be heading into 2018 powered by one of the sturdiest periods of growth in its nine-year expansion, a vigor that will help the economy's vital signs to be stronger than they have been in years. Consumer spending, home sales, consumer confidence and business investment have been among a number of recent indicators exhibiting economic strength.

Companies have been posting jobs faster than they have been able to find workers to fill them. The stock market has been setting records, seemingly every month. For the first time, employers have added jobs each month for the past seven years. Workers have benefited from an economy that has delivered broad-based gains in income and employment for the first time in at least a decade. Groups that were left behind in the early stages of the economic recovery, such as African-Americans and people without a college degree, have seen unemployment rates drop sharply in recent years. And although wage growth has remained disappointing, household income has shown strong gains, particularly for poorer households.

Companies in nearly every sector have reveled in the best opportunity they have seen in years. Improving global growth has given a lift to U.S. manufacturers. Rising incomes and strong consumer confidence have helped retailers, whose payrolls grew at the fastest pace since January, despite the shadow of rising online sales.

Why has the economy improved? Faster growth abroad has helped, as has the continued accommodation by the Federal Reserve. That strength could also pose challenges, particularly in light of the \$1.5 trillion tax cut that Congress recently passed. The tax bill could provide at least a modest lift to the economy. There are some concerns however: with unemployment so low and the economy fundamentally healthy, a tax cut could lead the economy to grow too quickly while adding to the national debt, pushing up inflation and forcing the Federal Reserve to raise interest rates faster than planned.

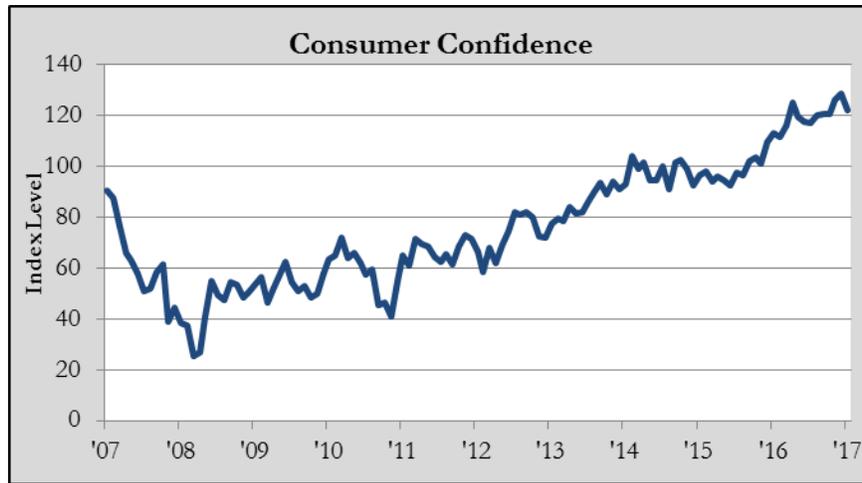
Consumer spending: Americans spent more and saved less in November, a sign that low unemployment, robust consumer confidence, the prospect of tax cuts and buoyant financial markets are underpinning a strong holiday shopping season. Americans have been saving at the slowest pace in a decade, likely in anticipation of continued job and wealth gains as stock indexes barreled to new records in November and the unemployment rate stood at a 17-year low.

Meanwhile spending was strong in a key month of the holiday season, outpacing income gains. Very elevated consumer confidence has made people more comfortable saving less. But the saving rate will not fall forever, so income growth will need to pick up if consumers are to continue spending at their recent pace.

Inflationary pressures picked up somewhat in November. The price index for personal-consumption expenditures, the Federal Reserve's preferred inflation measure, rose 0.2% from October and was up 1.8% from a year earlier. After touching the Fed's 2% annual target earlier this year, inflation has been below-target for nine consecutive months. Below-target inflation for much of 2017 has been puzzling since the unemployment rate has been very low and the economy has been growing.

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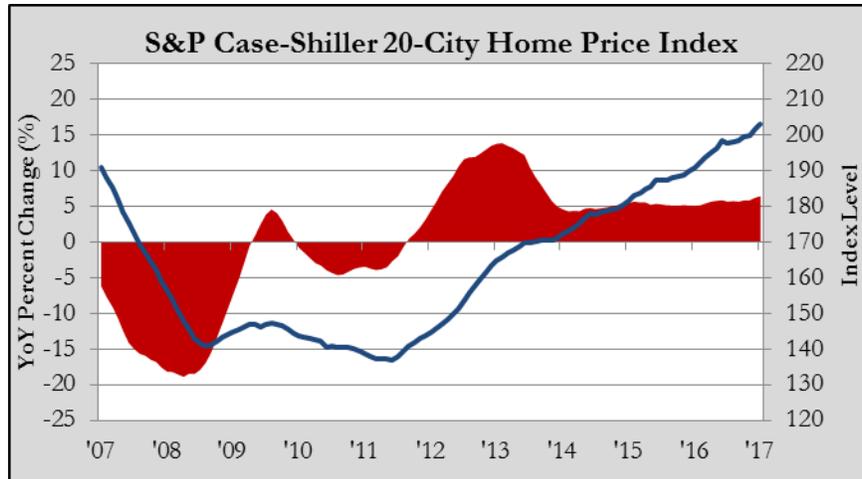
Consumer Confidence: Consumer confidence has remained high, with its headline index registering a 17-year high in October. Confidence has stemmed from a combination of the strong labor market and financial gains improving consumers' assessment of the present situation, as well as rising expectations about the future. There has been a marked uptick in the expectations index in recent months. Apparently, partisan political bickering has not deterred consumers' optimism for the impact of tax cuts. The rising stock market and home values have also boosted their outlook.



Source: The Conference Board

Housing: The hurricanes introduced a little bit of volatility into the monthly housing numbers, but the underlying story essentially has remained the same. Home sales and new home construction continued to be constrained by supply, likely to ease only modestly in 2018. As a result, modest gains are expected in new and existing home sales and single-family construction should rise. Multifamily construction will likely fall slightly in 2018, reflecting a sharp increase in apartment completions and rising vacancy rates in many of the more active, large apartment markets. Housing will make a positive contribution to real GDP growth in 2018, but the persistence of unusually lean inventories of homes for sale should keep prices rising well ahead of incomes and inflation, exacerbating affordability challenges. Median sales prices of an existing home should rise about 5% in 2018.

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Source: S&P / Case-Shiller

While tax reform may have some slightly negative intermediate impacts on the housing market it should remain a modest positive for the broader economy. Stronger job and income growth and lower unemployment should continue to boost homeownership. Demographics will also become more positive.

Labor market and wages: The U.S. economy has been hitting milestones not seen in more than a decade, marked by robust hiring that has led to low unemployment and a sustained pickup in output. Nonfarm payrolls saw a record 87th straight month of expansion in December. Steady hiring has in turn driven the unemployment rate down to a 17-year low.

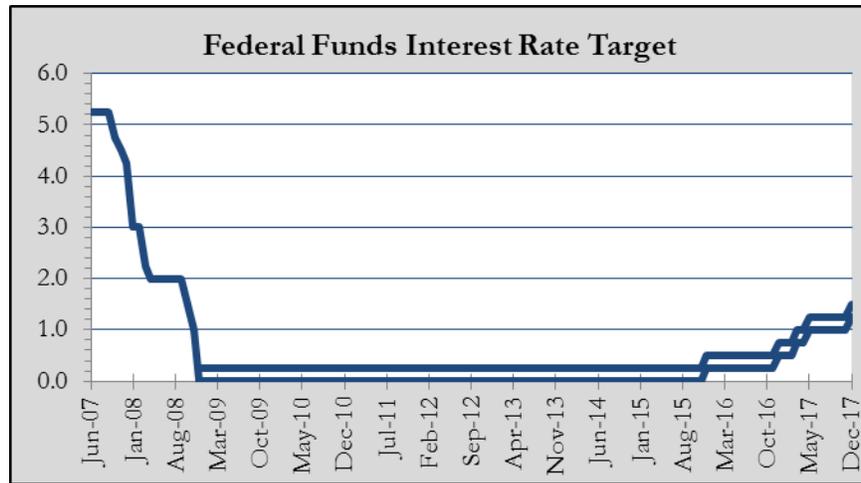
One gray mark has been wage growth. Wages were up about 2.5% in 2017, near the same lackluster pace maintained since late 2015. Wages should pick up when workers gain the confidence in the economy to demand raises — and to change jobs if they do not get them. There have been signs that could already be happening. Nearly 9.5 million workers quit their jobs voluntarily in the third quarter, the most since 2001. The low unemployment rate could mean workers are finally getting the bargaining power to start demanding and winning higher wages, though longer-run forces have helped to hold wages in check. Well-paid baby boomers have been replaced by lower-earning millennials and the development of a global labor market means factory workers in the U.S. compete with those in China. Still, soft inflation has made it harder for companies to pass along wage increases to customers.

Rising pay would be good news for workers. However, it could cause concern at the Federal Reserve, where policymakers have been gradually raising rates and paring the Fed's bond holdings in a bid to keep inflation in check. The Fed has signaled plans to raise interest rates three times in 2018, but if inflation started to pick up, the Fed could be forced to act more quickly than it wants, with unpredictable effects on financial markets and the economy.

Federal Reserve: In the near-term, a combination of low unemployment and modest wage growth and inflation will likely keep the Federal Reserve on a path of gradually pushing up short-term interest rates. The Fed could become more inclined to push rates up at a slightly faster pace in 2018 if the job market keeps cranking out strong monthly gains. The Fed has to be

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cognizant of the fact that if they let unemployment get too low, they may have to raise rates more aggressively, and that would risk causing a recession. Another risk would be that financial markets could overheat even as the real economy seems to be on strong and sustainable footing.



Source: Federal Reserve Bank of New York

U.S. Dollar: The Fed’s “Major Currency” index, measuring the trade-weighted value of the dollar vis-à-vis the other major currencies of the world, rose more than 40% between 2011 and the 2016. However, the index has declined more than 5% on balance in 2017, and is expected to further dollar depreciate against many foreign currencies in coming quarters.

The U.S. dollar was boosted over the past few years by monetary policy “divergence.” That is, market participants looked for the Federal Reserve to dial back its policy accommodation, and these expectations were subsequently realized. Conversely, most foreign central banks were ramping up their policy accommodation during this period. Consequently, interest rates moved in favor of the U.S. dollar.

The U.S. has entered a period of monetary policy “convergence.” Foreign central banks have started to remove policy accommodation. Although the Fed will likely continue to hike rates, history has shown that the dollar tends to do best at the beginning of the Fed’s tightening cycle. Once the tightening cycle has become more mature, the dollar will tend to get “less bang for the buck” in terms of additional rate hikes. If most foreign central banks began a process of hiking rates or, in some cases, tighten further, then the U.S. dollar likely would continue to follow a downward trend against many foreign currencies. The extent of foreign currency strength should depend on the degree of monetary policy adjustment by foreign central banks.

On the other hand, a provision of the recent tax reform bill will be expected to release a tide of U.S. corporate cash from abroad, a development likely to jolt the dollar higher and reverberate throughout financial markets early next year. Companies could bring back as much as \$400 billion as they take advantage of a one-time cut for repatriation of earnings and cash held overseas written into the tax reform bill. That would typically require them to sell foreign holdings and buy assets denominated in dollars, which could boost the U.S. currency.

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It is uncertain how much of the more than \$1 trillion U.S. companies estimated to have stashed abroad will be converted into dollars under the new tax law and what part of that amount is already in the U.S. dollar. That makes it difficult to gauge how the tax bill will affect the dollar, or what impact the repatriations will have on the economy.

The most immediate threat to a dollar rally, however, could come from outside the U.S., where a burgeoning Eurozone economy has been paving the way for the European Central Bank to unwind its monetary-easing policies and eventually raise rates. That would be a boon for investors who have wanted to diversify their dollar holdings but have stayed out of euros because interest rates in the region have been near historical lows.

Global: After a sub-par start to 2017, global economic growth has accelerated to an above-trend 4% (annualized) pace in both the second and third quarters of the year. Moreover, a similar brisk pace has been estimated for the October-December period. Expansionary macroeconomic policies that were put in place in 2016 in many major foreign economies, have helped to stimulate global economic activity. Growth in global trade has also strengthened in 2017 in line with the acceleration in global industrial production. Recent momentum in advanced economies and notably G7 outperformance, combined with a resilient Chinese economy, has led to an expectation of 3.5% global growth in both 2018 and 2019.

On the surface, this synchronized expansion in economic activity would seem to be the real deal, with the seeds planted by highly accommodative monetary policy, and recently, supportive fiscal policies bearing fruit. Moreover, business and consumers have been the most confident they have been during this cycle, reinforcing the notion that the economy no longer requires life support. Nevertheless, concerns about the sustainability of the current expansion have lingered among policymakers, particularly in a world of aging labor forces, low productivity growth, high income inequality, elevated policy uncertainty, and slow uptake of structural reforms. These structural impediments will not go away anytime soon.

Accordingly, the focus for policymakers has remained on what above-trend economic growth would mean for capacity pressures, interest rates, and asset prices. Shrinking unemployment rates and output gaps would all suggest that it's only a matter of time before wage and price pressures build. Indeed, recent labor market and inflation data have been supportive of this narrative.

The Euro area should likely see an above 2.0% pace heading into 2018, aided by accommodative financial conditions, healthy business and household spending, and ongoing absorption of excess labor market slack. In Japan, a combination of robust private consumption and infrastructure investment related to the 2020 Tokyo summer Olympics should help to offset the speed bump posed by the October 2019 value-added tax increase to 10%, from 8%.

Not surprisingly, the UK has been the odd one out, as Brexit looms in fifteen months. Economic activity in the UK should unlikely hold much above trend over the forecast horizon, as slow productivity growth and higher prices combine with Brexit-related uncertainty to keep consumer and business spending relatively subdued.

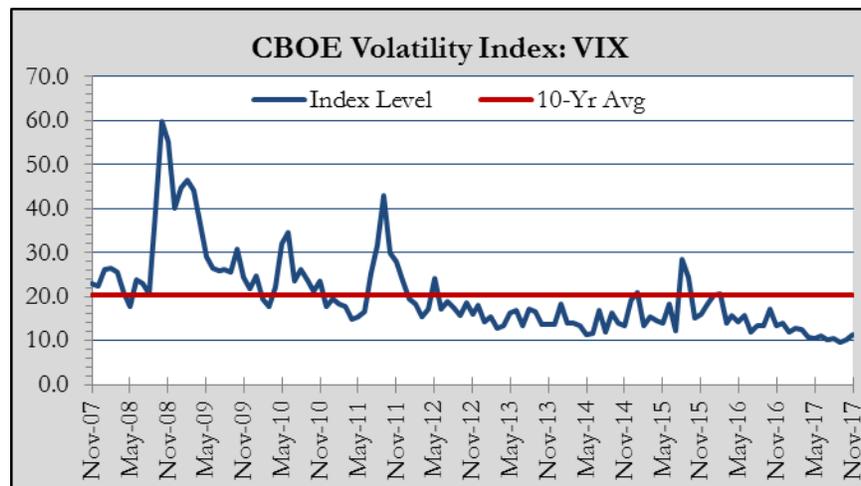
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Emerging market (EM) economies have also been experiencing an upswing in economic activity, with a modest and deliberate slowdown in China offering a counterweight. As the primary engine, EMs generated more than 58% of global annual income. However, persistent, above-trend economic growth has only begun to take hold. China has managed to maintain an above-trend pace in 2017 despite measures undertaken by authorities to rein in excessive credit growth. In contrast, commodity exporting economies such as Brazil and Russia have continued to struggle to build momentum, while economic experiments in India have led to a choppy performance.

Rebounding commodity prices and stronger foreign demand should help drive EM economies to an above-trend 5.0% pace through 2019. As with advanced economies, risks to the EM outlook seem somewhat better balanced than in the past, with downside risks largely unchanged from past quarters.

Outlook: After a bumpy start to 2017, growth in the U.S. held at a 3.0% pace for the remainder of 2017. Moreover, stronger-than-expected growth became a global theme, as G7 economies broadly surprised to the upside. Strong growth spurred central bank action, with the Fed raising rates three times, but no longer alone in removing stimulus. Other major central banks also raised rates or reduced their monetary accommodation.

Not only is the U.S. economy in good shape today, the economic expansion is likely to continue for some time. The last two economic expansions were derailed when asset prices overheated—tech stocks in the late 1990s and real estate in the mid-2000s. An index of market volatility, dubbed the “fear gauge,” has been hovering near its lowest levels on record.



Source: Chicago Board Options Exchange

If the economy performs in 2018 as it did in 2017, unemployment will likely fall from the already low level of 4.1% in October to 3.5% at the end of 2018, a rate not seen since the late 1960s. This could entice the Fed to raise interest rates more quickly than planned to prevent an unwanted pickup in inflation. For now, broad measures of inflation have been restrained, a sign the economy isn't overheating.

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Downside risks: What Could Possibly Go Wrong? First, the debt-to-GDP ratio in the Chinese economy has shot up over the past decade, with leverage in the non-financial corporate sector rising markedly. A debt implosion in China probably would not have large financial effects on the rest of the world, at least not directly. Foreign exposure to the \$30 trillion of outstanding Chinese debt totals only \$1.6 trillion. However, China is the second-largest economy in the world and a sharp economic slowdown in the Chinese economy, caused by an inability to service excessive leverage, would clearly have economic repercussions on China's major trading partners.

Second a sharper-than-expected rebound in global inflation could pose another potential downside risk to the global economic outlook. At present, inflation has generally remained benign on a global basis. If inflation should creep up only slowly, then central banks would be likely to tighten policy at a restrained pace. However, if inflation was to shoot up sharply, then central banks could tighten at a much faster pace, posing a threat to the global economic expansion.

Third, there is the risk of global trade tensions. The United States, Mexico and Canada are currently negotiating revisions to the NAFTA agreement. An abrupt end of the agreement would impart adjustment costs on many businesses in the three countries. In addition, the Trump Administration came into office talking a hard line about American trade relations with China. So far, the administration's actions have not matched its rhetoric, but an increase in trade tensions between the two largest economies in the world could lead to financial market volatility and slower global economic growth.

Finally, there are a whole host of geopolitical risks to ponder, which are truly difficult to forecast. Concerns about North Korea's military ambitions will remain, as will tensions between the major powers in the Middle East. Political events in Europe will also remain on the radar as Phase two of Brexit negotiations are set to begin soon. Moreover, results from Catalonian election in December, has shown strong support for independence-minded parties, suggesting the potential for economic uncertainty to linger in Spain. Add elections in Italy, Sweden and Eastern Europe in 2018, and European politics would dominate headlines for another year. Hopefully strong economic growth will manage to trump uncertainty in 2018.

Capital Markets in Review

Recap: The S&P 500 Index returned 6.6% in the fourth quarter and finished 2017 with a total return over 21.8%. The full year 2017 was unique in that the S&P 500 witnessed positive returns in each month of the year. In fact, it has now seen positive monthly returns for 14 straight months (October 2016 was the last month with a negative return). Meanwhile, the Bloomberg Barclays U.S. Aggregate Bond Index returned 0.4% in the final quarter and saw its total return come in near 3.5% for the year overall. All things considered, these results are extraordinary and investors should be extremely pleased overall. The results came in much better than most market strategists had envisioned at the start of the year, with the average forecast return on the S&P 500 Index expected to come in near only 6%.

As discussed in the economic commentary above, 2017 saw some of the lowest volatility on record, with stagnant low levels across the year in the VIX Index. There were only a few short

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bursts higher that were quickly stomped down quickly by market participants. The year began with concerns including above average equity valuations and the likelihood of interest rates moving higher as the Federal Reserve had set its intentions and seemed committed to following through. In the end stocks pushed higher supported by steadily improving corporate earnings and global economic growth, and the Fed did in fact raise rates three times across 2017.

Despite the surprisingly strong returns for many asset classes, 2017 once again proved a challenge to “get the right mix” and was another year where some diversification strategies failed to add significant incremental value to investment portfolio results.

Domestic Stocks: The S&P 500 Index returned almost 22% this past year and handily exceeded the expectations of most Wall Street strategists by a large margin. Earnings improved relative to the previous year and provided sufficient tailwinds for stocks to move higher without stretching valuations materially higher. Research analysts began the year expecting overall 2017 S&P 500 operating earnings to climb 20% and come in near \$131. While the final Q4 2017 earnings results will not be available for several more weeks, the current full year expectations were adjusted downward and now stand near \$125. Adjusting for changes to the Q4 2016 final numbers this still marks overall growth of 18% for the year if the estimates pan out.

Mid and small-cap stocks trailed their larger brethren for much of this past year, but still posted strong absolute returns for investors. The Russell Mid-Cap Index rose 6% in the fourth quarter to finish the year up 18.5% for the year overall. The Russell 2000 Index representing small stocks rose 3.3% in the final quarter to mark a yearly total return of over 14.6%.

Growth stocks were in vogue in 2017 after trailing Value stocks the previous year. Investors fixated on those companies that could deliver high levels of earnings growth and they showed a willingness to pay handsomely for them. Momentum was a very strong factor trend that led Growth stocks to outperform Value stocks across the market cap spectrum. The Russell 1000 Growth Index returned +30.2% for the year, while the Russell 1000 Value Index returned +13.7%.

Sector performance for the S&P 500 Index was overwhelmingly positive for the year, with nine of eleven sectors landing in positive territory. In fact, all of the sectors with positive results for the year returned over 10%! Growth sectors dominated overall, with Technology (+38.8%), Materials (+23.8%), and Consumer Discretionary (+23.0%) taking top performance honors. Telecom Services and Energy were the only negative performing sectors, *falling* 1.3% and 1.0%, respectively.

Foreign Stocks: Developed equity markets outside the U.S. also posted strong results in the final quarter of 2017 and the year overall. The MSCI EAFE returned 4.2% for the quarter but climbed over 25% for the year. The MSCI ACWI ex USA Index (that has greater emerging markets exposure) was up 5% for the quarter and up 27.2% for the year. Despite some fears of economic and political uncertainty as the year began, foreign stocks started 2017 on a strong note and never really looked back. A weaker U.S. dollar enhanced returns for domestic investors in overseas markets.

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Emerging Markets stocks performed very well over the course of the year as economies improved and many commodity markets continued to show signs of stabilizing. Performance results were bolstered further by strong investor flows. Debt investors shook off any fears of political instability and flocked to the higher interest rates that were available from these countries. The equity markets benefited too, but it was mostly the larger market capitalization companies that prospered from a surge in passive investment flows. The MSCI EM Index posted a return of 7.4% for the quarter, and saw an impressive total return almost 37.3% for U.S. investors for the year.

Bonds: The U.S. 10-Year Treasury closed the quarter and year with a 2.40% yield, essentially unchanged from the 2.45% yield at the end of 2016. Similar 10-Year notes for Germany and Japan posted yields near 0.4% and 0.05%, respectively. The Bloomberg Barclays U.S. Aggregate Index returned 0.4% during the quarter, while the Bloomberg Barclays Global Aggregate ex U.S. rose 1.1%. For the year, these bond indexes returned +3.5% and +10.5%, respectively. The larger return from international bonds was primarily driven by a weaker U.S. dollar for most of the year.

Domestically, the high yield bond market stole the show again this year as investors continued to search the space for higher incremental income. Improving economic signals, stronger corporate balance sheets, and low default rates provided ample support for these investor decisions. For the quarter the Bloomberg Barclays High Yield Corporate Index was up 0.5%, to finish out the year up 7.5%. This annual result was not quite as strong as the 17.5% in 2016, but respectable nonetheless.

Non-Traditional Investments: Commodity-related investments demonstrated additional efforts to recover from weakness in previous years, but in general did not move materially higher. Oil prices were under pressure for the first half of the year as global production remained high. OPEC's efforts to curtail further increases were applauded and oil prices stabilized and moved higher over the second half of the year. WTI ended 2017 near \$60 per barrel – up approximately 11% for the year. MLP investors bore the brunt of energy commodity price volatility over the year, and the Alerian MLP Index *declined* 6.5% for the year.

Real estate investments also saw periods of volatility over the year as investors wrestled with moves in interest rates and the perception that rates would continue to move higher over time. Rising interest rate environments are generally viewed negatively by real estate investors that fear negative impacts to property values. However, often times these fears prove short-lived, particularly in markets with positive fundamentals and rental rates adjusting higher. However real estate markets largely saw returns in line with fixed income investments. In the final quarter of 2017 the FTSE NAREIT Equity REIT Index returned 1.5%, and provided a positive 5.2% total return for the year overall.

Outlook: Wall Street strategists are sticking to a mid-single digits prediction for 2018 S&P 500 returns, an average 7% price return expectation on the Index (slightly higher than the 6% 2017 prediction, but below the 10% “normal” return expectation). Making these predictions is no easy task, but the year-end targets are part of the job for these strategists. Historically the consensus expectation for any given year has proven to hold a poor track record. This year the forecasts are

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again skewed to the low end, with the largest group looking for a price return of less than 5% on the S&P 500.

The recent changes to corporate tax policies could provide some additional benefits to corporate earnings growth in the coming year. Currently stock research analysts are looking for corporate earnings growth of 16% over the course of 2018 with operating earnings on the S&P 500 Index targeted at \$145. Wall Street strategists are right in line with their research peers and see earnings coming in at \$146 on average.

The S&P 500 Index now trades at 22 times forward earnings according to the Wall Street Journal (above the 19 times level at the start of 2017). Market valuations increased slightly over the course of 2017 as investors applauded the corporate earnings growth recovery that coincided with stronger global economic growth. Domestic stock markets are not cheap, but Wall Street is implying a marginal decline in valuations for this year based on lower market return expectations alongside earnings growth near 16%.

In other areas, developed foreign equities continue to appear relatively attractive based upon more favorable valuations, earnings potential, dividends, and stimulative government activities that remain in place despite signs of economic recovery. As interest rates move higher fixed income investments could face sizable headwinds, although there certainly will be periods of stability. Based on recent economic and market trends and forgoing a significant change to current inflation trends, the Federal Reserve appears to be targeting 3 interest rate hikes in 2018.

As strategic investors we prefer to focus on maintaining a disciplined long-term positive perspective on capital markets. While short-term market disruptions and turbulence are inevitable, no attempts are made to make substantial portfolio adjustments as markets ebb and flow over the short term. Our preference is to make meaningful and purposeful allocations to portfolio strategies, and adjust them occasionally, once again for the long term, as needs arise.

At the same time, we are mindful of the many potential risks that could impact markets over shorter periods. While coming up with an exhaustive list of potential culprits that could upset markets in 2018 is inherently faulty, we do make an attempt to be mindful of these based on our reviews of the markets and economic environment. The list of potential risks to 2018 results could include (in no particular order): changes in leadership at the Federal Reserve that materially change current outlooks and communications to market participants, relatively high domestic stock market valuations, continued polarization in Washington and the unwillingness to “cross the aisle” in order to effect meaningful beneficial policy reforms, the second year of a presidency struggling to exert influence and any associated upheavals in both domestic and foreign policies, potential impacts from the removal of global economic stimulus and rising interest rates from perceived accelerating inflation, and inevitably the persistent threats from geopolitics, terrorism, and other “black swan” events.

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Disclosures

This report is not intended to be a client-specific suitability analysis or recommendation, an offer to participate in any investment, or a recommendation to buy, hold or sell securities. Do not use this report as the sole basis for investment decisions. Do not select an asset class or investment product based on performance alone. Consider all relevant information, including your existing portfolio, investment objectives, risk tolerance, liquidity needs and investment time horizon.

The Capital Markets Review was prepared in close collaboration with Capital Market Consultants, Inc. (“CMARKC”). CMARKC has been retained by GYL. CMARKC is an independent third party research firm that develops capital market assumptions and other value added investment insight for GYL and other investment advisors nationally. This report is for general informational purposes only and is not intended to predict or guarantee the future performance of any individual security, market sector or the markets generally.

Sources

Bureau of Economic Analysis, Department of Labor, Department of Commerce, Institute for Supply Management, S&P Dow Jones Indices, The Conference Board, National Association of Realtors, The Federal Reserve, Chinese National Bureau of Statistics, Eurostat, Morningstar.

Economic Indices

The Conference Board **Consumer Confidence Index**[®] (CCI) is a barometer of the health of the U.S. economy from the perspective of the consumer. The index is based on consumers’ perceptions of current business and employment conditions, as well as their expectations for six months hence regarding business conditions, employment, and income.

The Conference Board **U.S. Leading Economic Index**[®] is a composite economic index designed to signal peaks and troughs in the business cycle. The leading economic index is essentially a composite averages of several individual leading indicators. They are constructed to summarize and reveal common turning point patterns in economic data in a clearer and more convincing manner than any individual component – primarily because they smooth out some of the volatility of individual components.

The Institute of Supply Management (ISM) **Manufacturing Index**[®] is a composite index based on the diffusion indexes of five of the indexes with equal weights: New Orders (seasonally adjusted), Production (seasonally adjusted), Employment (seasonally adjusted), Supplier Deliveries (seasonally adjusted), and Inventories. An Index values over 50 indicate expansion; below 50 indicates contraction. The values for the index can be between 0 and 100.

The Institute of Supply Management (ISM) **Non-Manufacturing Index**[®] is a composite index based on the diffusion indexes for four of the indicators with equal weights: Business Activity (seasonally adjusted), New Orders (seasonally adjusted), Employment (seasonally adjusted) and Supplier Deliveries. An Index values over 50 indicate expansion; below 50 indicates contraction. The values for the index can be between 0 and 100.

The **Consumer Price Index (CPI)** measures the price of a fixed basket of goods and services purchased by an average consumer.

Asset Indexes

An index is unmanaged and not available for direct investment.

Alerian MLP Index is a composite of the 50 most prominent energy master limited partnerships calculated by Standard & Poor's using a float-adjusted market capitalization methodology.

Barclays Global Aggregate Index is a measure of global investment grade debt from 24 local currency markets. It includes treasury, government-related, corporate and securitized fixed-rate bonds from both developed and emerging markets issuers. The three major components of this index are the US Aggregate, the Pan-European Aggregate, and the Asian-Pacific Aggregate indices. The index also includes Eurodollar and Euro-Yen corporate bonds, Canadian government, agency and corporate securities, and USD investment grade 144A securities.

Barclays Global Aggregate Ex-US Index provides a broad-based measure of the global investment-grade fixed income markets excluding U.S. dollar-denominated securities. The three major components of this index are the US Aggregate, the Pan-European Aggregate, and the Asian-Pacific Aggregate indices. The index also includes Eurodollar and Euro-Yen corporate bonds, Canadian government, agency and corporate securities, and USD investment grade 144A securities.

Barclays Treasury Inflation Protected Securities (TIPS) Index includes all publically issued, investment-grade U.S. TIPS with an outstanding face value of more than \$250 million and that have at least one year to maturity.

Barclays U.S. Aggregate Bond Index is composed of the Barclays Capital U.S. Government/Credit Index and the Barclays Capital U.S. Mortgage-Backed Securities Index, and includes Treasury issues, agency issues, corporate bond issues, and mortgage-backed securities.

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Barclays U.S. Credit Bond Index is an unmanaged, market-weighted index generally representative of intermediate and long-term investment grade corporate debt securities having maturities of greater than one year.

Barclays U.S. Government Bond Index is an unmanaged, market-weighted index generally representative of intermediate and long-term government debt securities having maturities of greater than one year.

Barclays U.S. High Yield Corporate Index measures the USD-denominated, high yield, fixed-rate 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.

Barclays U.S. Municipal Bond Index represents municipal bonds with a minimum credit rating of at least Baa, an outstanding par value of at least \$3 million, and a remaining maturity of at least one year. The Index excludes taxable municipal bonds, bonds with floating rates, derivatives, and certificates of participation.

Bloomberg Commodity Index is designed to be a highly liquid and diversified benchmark for commodities as an asset class. The index is composed of futures contracts on 22 physical commodities. No related group of commodities (e.g., energy, precious metals, livestock and grains) may constitute more than 33% of the index as of the annual re-weightings of the components. No single commodity may constitute less than 2% of the index.

BofA Merrill Lynch Emerging Markets Corporate Index is designed to measure the performance of U.S. dollar-denominated emerging markets corporate senior and secured debt publicly issued in the U.S. domestic and Eurobond markets.

BofA Merrill Lynch US 3-Month Treasury Bill Index is comprised of a single issue purchased at the beginning of the month and held for a full month. At the end of the month that issue is sold and rolled into a newly selected issue. The issue selected at each month-end rebalancing is the outstanding Treasury Bill that matures closest to, but not beyond, three months from the rebalancing date. To qualify for selection, an issue must have settled on or before the month-end rebalancing date.

Dow Jones Industrial Average is a price-weighted average of 30 U.S. stocks traded on the New York Stock Exchange and NASDAQ.

FTSE NAREIT US All Equity REITs Index is designed to track the performance of REITs representing equity interests in (as opposed to mortgages on properties.) It represents all tax-qualified REITs with more than 50 percent of total assets in qualifying real estate assets, other than mortgages secured by real property that also meet minimum size and liquidity criteria.

MSCI AC Asia Ex-Japan (net) is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of developed and emerging markets in Asia, excluding Japan. The Index consists of 10 country indices comprising 2 developed and 8 emerging market country indices. Developed Markets countries in the index include: Hong Kong and Singapore. Emerging Markets countries include: China, India, Indonesia, Korea, Malaysia, the Philippines, Taiwan and Thailand.

MSCI AC World Index (net) is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of developed and emerging markets. The Index consists of 45 country indices comprising 22 developed and 23 emerging market country indices. The developed market country indices included are: Australia, Austria, Belgium, Canada, Denmark, Finland, France, Germany, Greece, Hong Kong, Ireland, Italy, Japan, Netherlands, New Zealand, Norway, Portugal, Singapore, Spain, Sweden, Switzerland, and the United Kingdom. The emerging market country indices included are: Argentina, Brazil, Chile, China, Colombia, Czech Republic, Egypt, Hungary, India, Indonesia, Israel, Korea, Malaysia, Mexico, Morocco, Peru, Philippines, Poland, Russia, South Africa, Taiwan, Thailand, Turkey and United States.

MSCI AC World Ex-USA Index (net) is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of developed and emerging markets, excluding the USA. The Index consists of 45 country indices comprising 22 developed and 23 emerging market country indices. The developed market country indices included are: Australia, Austria, Belgium, Canada, Denmark, Finland, France, Germany, Greece, Hong Kong, Ireland, Italy, Japan, Netherlands, New Zealand, Norway, Portugal, Singapore, Spain, Sweden, Switzerland, and the United Kingdom. The emerging market country indices included are: Argentina, Brazil, Chile, China, Colombia, Czech Republic, Egypt, Hungary, India, Indonesia, Israel, Korea, Malaysia, Mexico, Morocco, Peru, Philippines, Poland, Russia, South Africa, Taiwan, Thailand, and Turkey.

MSCI EAFE Index (net) (Europe, Australasia, Far East) is a free float-adjusted market capitalization index that is designed to measure the equity market performance of developed markets, excluding the US & Canada. The Index consists of the following 21 developed market country indexes: Australia, Austria, Belgium, Denmark, Finland, France, Germany, Hong Kong, Ireland, Israel, Italy, Japan, the Netherlands, New Zealand, Norway, Portugal, Singapore, Spain, Sweden, Switzerland, and the United Kingdom.

MSCI Emerging Markets Index (net) is a free float-adjusted market capitalization index that is designed to measure equity market performance of emerging markets. The MSCI Emerging Markets Index consists of the following 23 emerging market country indexes: 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.

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MSCI Emerging Markets Latin America Index (net) is a free float-adjusted market capitalization index that is designed to measure equity market performance of emerging markets in Latin America. The MSCI Emerging Markets Latin America Index consists of the following 5 emerging market country indexes: Brazil, Chile, Colombia, Mexico, and Peru.

MSCI Frontier Markets Index (net) is a free float-adjusted market capitalization index that is designed to measure equity market performance of frontier markets. The MSCI Frontier Markets Index consists of the following 24 frontier market country indexes: Argentina, Bahrain, Bangladesh, Bulgaria, Croatia, Estonia, Jordan, Kenya, Kuwait, Lebanon, Lithuania, Morocco, Kazakhstan, Mauritius, Nigeria, Oman, Pakistan, Romania, Serbia, Slovenia, Sri Lanka, Tunisia, Ukraine, and Vietnam. The MSCI Saudi Arabia Index is currently not included in the MSCI Frontier Markets Index but is part of the MSCI Gulf Cooperation Council (GCC) Countries Index. The MSCI Bosnia Herzegovina Index, the MSCI Botswana Index, the MSCI Ghana Index, the MSCI Jamaica Index, the MSCI Palestine IMI, the MSCI Trinidad & Tobago Index and the MSCI Zimbabwe Index are currently stand-alone country indexes and are not included in the MSCI Frontier Markets Index. The addition of these country indexes to the MSCI Frontier Markets Index is under consideration.

MSCI Brazil Index is designed to measure the performance of the large and midcap segments of the Brazilian market.

MSCI BRIC Index is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance across the following 4 Emerging Markets country indexes: Brazil, Russia, India and China.

MSCI China Index captures large and midcap representation across China H shares, B shares, Red chips and P chips.

MSCI Europe Index captures large and midcap representation across 15 Developed Markets countries in Europe. Developed Markets countries in Europe include: Austria, Belgium, Denmark, Finland, France, Germany, Ireland, Italy, the Netherlands, Norway, Portugal, Spain, Sweden, Switzerland and the UK.

MSCI India Index is designed to measure the performance of the large and midcap segments of the Indian market.

MSCI Japan Index is designed to measure the performance of the large and midcap segments of the Japanese market.

MSCI Russia Index is designed to measure the performance of the large and midcap segments of the Russian market.

MSCI USA Index is designed to measure the performance of the large and midcap segments of the US market.

Russell 1000[®] Index measures the performance of the largest 1000 companies in the Russell 3000 Index.

Russell 1000[®] Growth Index measures the performance of those Russell 1000 companies with higher price-to-book ratios and higher forecasted growth values.

Russell 1000[®] Value Index measures the performance of those Russell 1000 companies with lower price-to-book ratios and lower forecasted growth values.

Russell Midcap[®] Index measures the performance of the 800 smallest companies in the Russell 1000 Index, which represent approximately 25% of the total market capitalization of the Russell 1000[®] Index.

Russell Midcap[®] Growth Index measures the performance of the growth segment of the Russell Mid Cap Index.

Russell Midcap[®] Value Index measures the performance of the value segment of the Russell Mid Cap Index.

Russell 2000[®] Index measures the performance of the 2,000 smallest companies in the Russell 3000[®] Index, which represents approximately 8% of the total market capitalization of the Russell 3000 Index.

Russell 2000[®] Growth Index measures the performance of the growth segment of the Russell 2000 Index.

Russell 2000[®] Value Index measures the performance of the value segment of the Russell 2000 Index.

Russell 3000[®] Index measures the performance of the 3,000 largest U.S. companies, representing approximately 98% of the investable U.S. equity market.

Russell 3000[®] Growth Index measures the performance of the growth segment of the Russell 3000 Index.

Russell 3000[®] Value Index measures the performance of the value segment of the Russell 3000 Index.

S&P 500 Index is a capitalization-weighted index calculated on a total-return basis with dividends reinvested. The index includes 500 widely held U.S. market industrial, utility, transportation and financial companies.

S&P Global Natural Resources Index is comprised of 90 of the largest publicly traded companies, based on market capitalization, in global natural resources and commodities businesses that meet certain investibility requirements. The Index component securities represent a combination of the component securities included in each of the following three sub-indices: the S&P Global Natural Resources - Agriculture Index, the S&P Global Natural Resources - Energy Index and the S&P Global Natural Resources - Metals and Mining Index. The maximum weight of each sub-index is capped at one-third of the total weight of the Index.

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S&P North American Natural Resources Index comprises publicly traded large- and mid-capitalization U.S. and Canadian companies in the natural resources and commodities businesses that meet certain investability requirements and are classified within the sub-industries of one of three natural resources categories: energy, materials or agriculture.

Wilshire 5000 Total Market Index is a market-capitalization-weighted index of the market value of all stocks actively traded in the United States.