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Economic & Market Summary
July 2017

We remain generally positive on the US economy. First quarter US GDP growth was 2.1% over the prior year, consistent with the post-recession trend. Business investment, a weak component of growth throughout the recovery, was notably stronger. The consumer appears to be in good shape. Household debt-to-GDP and debt service payments as a percentage of income are both well below their pre-recession peaks. The labor market looks sound. Real wage growth is perking up, job openings remain abundant, and the labor force participation rate for workers 25-54 years old is starting to rise after nearly 16 years of decline. One caveat to monitor is the fact that job openings remain above total hires, suggesting a skills mismatch. Near-term catalysts for economic growth acceleration include deregulation and tax reform. However, the prospects for timely reform seem lower than earlier this year due to persistent distractions in Washington.

Despite weak recent inflation data, US economic stability and a strengthening labor market allowed the Federal Reserve to feel comfortable increasing rates again. The Fed views inflation weakness as transitory and expects core inflation to stabilize around 2% in the coming years. Plans for reducing the size of the balance sheet were also introduced. While the Fed has steadily increased rates over the previous 18 months, its overall posture under Janet Yellen has been accommodative. Speculation that Yellen will be replaced at the end of her term in February of 2018 appears to have subsided. Long-term government bond yields remain above last year's levels but have retreated somewhat due to declining inflation expectations. While the recent inflation softness warrants continued observation, we believe the Fed's actions are appropriate, as we have long argued that the economy is strong enough to return to a normalized interest rate environment.

With a P/E of 19x on the S&P 500 vs 18x last year, the equity market's valuation continues to drift higher. While this appears moderately elevated, it's important to note that strong first quarter earnings have buttressed the market in the face of declining expectations for fiscal policy reform. If recent commentary is a guide, the investment management community is beginning to acknowledge equities' higher price tag. With valuations creeping up and the recovery extending into its 8th year, healthy corrections could occur at any time, even with a positive economic backdrop. Sustained downturns (bear markets) are often preceded by a set of conditions that are largely absent. The economy appears healthy, inflation is moderate, and monetary policy is still generally accommodative. An elevated market valuation makes finding high-quality companies at reasonable prices more challenging. Nevertheless, we are still discovering pockets of value, even in a market where good bargains seem elusive.

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To request our SEC Form ADV Part II, please contact Michael L. Wise, Chief Compliance Officer, at the address above.