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Economic & Market Summary
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The US economy is on track to grow at the fastest pace in the last decade. Consumer confidence is near an 18 year high, taxes are lower, and business investment has increased. A key to sustaining this velocity is whether or not labor productivity growth improves, as growth has been weak throughout this cycle. For growth to improve, businesses need to make productivity-enhancing investments such as new facilities and equipment. With tax decreases, deregulation, and increasing business confidence, the environment for these kinds of investments seems favorable. While business investment has ticked up this year, it's too early to tell if the uptick is sustainable. In our view, companies need greater visibility on global trade before investment growth can seriously accelerate.

In Washington, tariff talk has increasingly focused on China ahead of the midterm elections. The Trump administration appears to be balancing pressuring China enough with avoiding higher consumer prices before the elections. History shows that the party controlling the White House rarely fares well in the midterms. If the Republicans keep or enhance their majority, little will change. Should the Democrats gain control of one or both legislative chambers, resisting Trump at every turn will be a priority. Trade may be an exception. Over the summer, Senate minority leader Chuck Schumer supported the early tariffs against China. Regardless of how the midterms shake out, trade negotiations are likely to stick around for the time being.

Inflation has perked up modestly. The Federal Reserve's preferred inflation measure has reached its 2% target for the first time since 2012. We anticipate that inflation will stabilize around 2% or possibly drift a little higher. A tight labor market is finally leading to a modest acceleration in wage growth. Companies seem more comfortable raising prices than at any other time in this cycle. In our view, yields on long-term bonds will move higher (and prices move lower). Accordingly, we remain cautious on bonds but fixated on credit quality when owing bonds is appropriate. While inflation may move up, runaway inflation seems unlikely. The Fed's preemptive rate increases and structural factors like an aging population and price-lowering technology (i.e. ecommerce and automation) could keep inflation manageable.

Propelled by tax cuts and a strong economy, earnings growth this year has been robust. Earnings for S&P 500 companies grew 27% year-over-year through the second quarter. Growth will certainly slow in 2019 as companies lap the one-time benefit from lower taxes. Estimates for next year's earnings look a little aspirational to us, especially considering the strengthening dollar. However, the economic environment for equities remains benign. Inflation is moderate, monetary policy is still accommodative, and consumers are healthy. In our view, the good news is fully reflected in the market's valuation. The PE ratio on 12 month forward earnings is 16.9x - above the 5 year and 10 year averages of 16.3x and 14.5x respectively according to Factset. Many of the high-quality companies we favor trade in-line with or at a premium to our estimates of their intrinsic value. In this environment, being disciplined about valuation is critical.

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