UNION

MONTHLY UPDATE AND COMMENTARY
APRIL 2017

Recap: The U.S. economy has been on solid footing for some time. Stable economic growth has materialized with consistent employment gains, equating to 16 million private sector jobs added since 2010. The unemployment rate has hovered at estimates consistent with the US economy's natural rate of unemployment. Tighter labor markets have resulted in wage increases meaningfully outstripping the current inflation rate. Inflation appears likely to reach upward to the Fed's 2% target by the end of this year.

While consumer spending got off to a slow start this year, measures of consumer confidence have continued to signal optimism. Consumer assessments of both current and future economic conditions have remained high. The Conference Board's measure of consumer confidence climbed to the highest level since December 2000. More important for real consumer spending, the consumer's outlook for income growth and job growth both posted rather dramatic improvements over the past two months. This should translate into stronger real consumer spending growth beyond the first quarter of 2017.

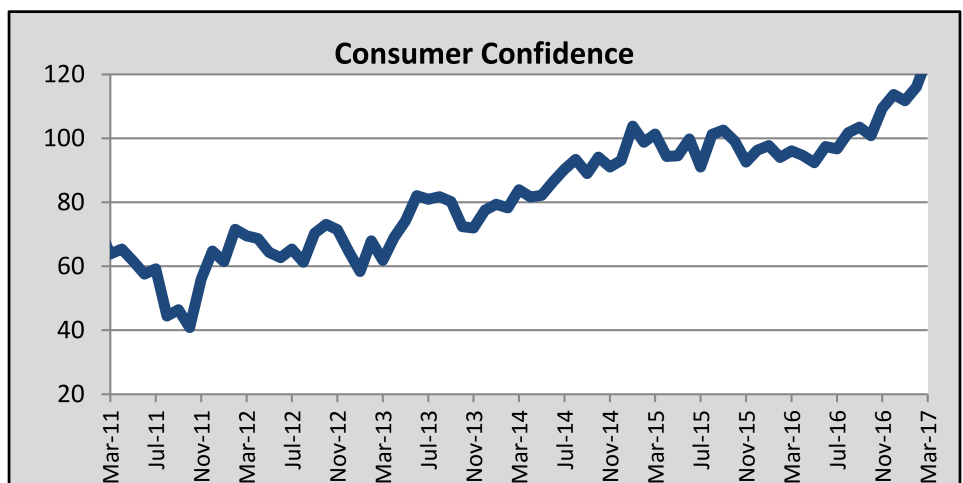
GDP: The final estimate of GDP growth for the fourth quarter of 2016 showed that the economy expanded at a 2.1% pace to close out 2016. The slight upward revision from previous estimates was attributed to somewhat higher real consumer spending and business investment.

This year's first quarter also looks like it could be the weakest of the year. Real GDP growth is expected to be a 1.0%-1.5% annual rate. While the weather played a role in suppressing growth this early year, it was not so much from the late winter blizzard as it was from the milder weather earlier, which cut utility use. The widening trade deficit also looked to have subtracted 0.5 percentage points off growth in the quarter. The early timing of the Chinese New Year led to a surge in imports in January that all but assured trade would be a huge drag on growth for the quarter. With final demand growing solidly, trade will also likely subtract from growth in subsequent quarters. Moreover, government spending will also decline.

Personal Income: Personal income rose 0.4% month-over-month in February. Real disposable personal income was up just 0.2%. Personal spending was up a modest 0.1% in nominal terms, and actually fell 0.1% in real terms. This poor showing followed a 0.2% decline in real spending in January. Consumer prices rose 0.2%, pushing year-over-year headline inflation up to 2.1% from 1.9% in January. The personal saving rate rose to 5.6% from a downwardly revised 5.4% in January.

Although the first quarter of 2017 would seem likely to start with a drag in terms of real GDP growth, this is likely to be only a temporary setback. With strong consumer confidence and strengthening income growth, spending should bounce back in the second quarter. This should help restore economic growth to an above trend rate.

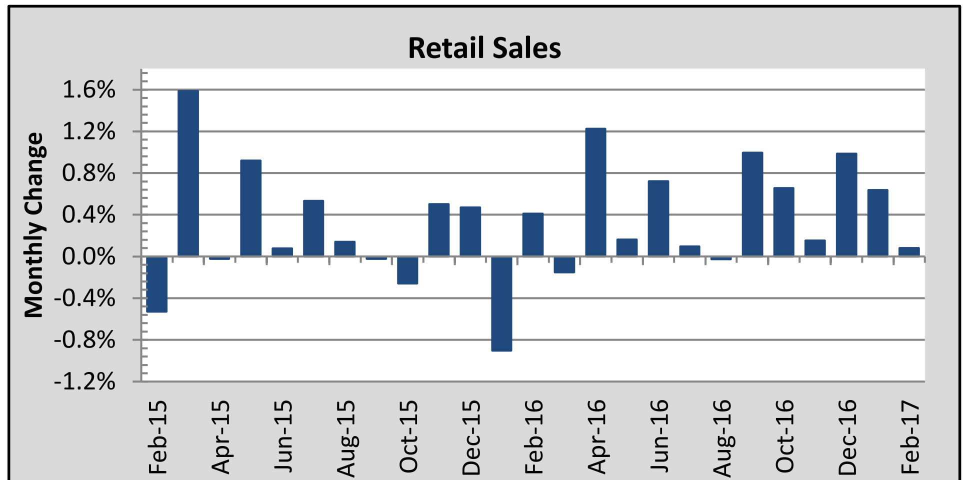
Consumer Confidence: Consumer confidence jumped 9.5 points in March to 125.6 while data for February were also revised 1.3 points higher. This marked the highest level since December 2000. The largest improvement came in the proportion of consumers expecting more jobs to be created over the next six months. A growing proportion of consumers also expected their income to rise over the six months while fewer expected a decrease.



This surge in consumer confidence likely reflected a legitimate improvement in business conditions. This level of

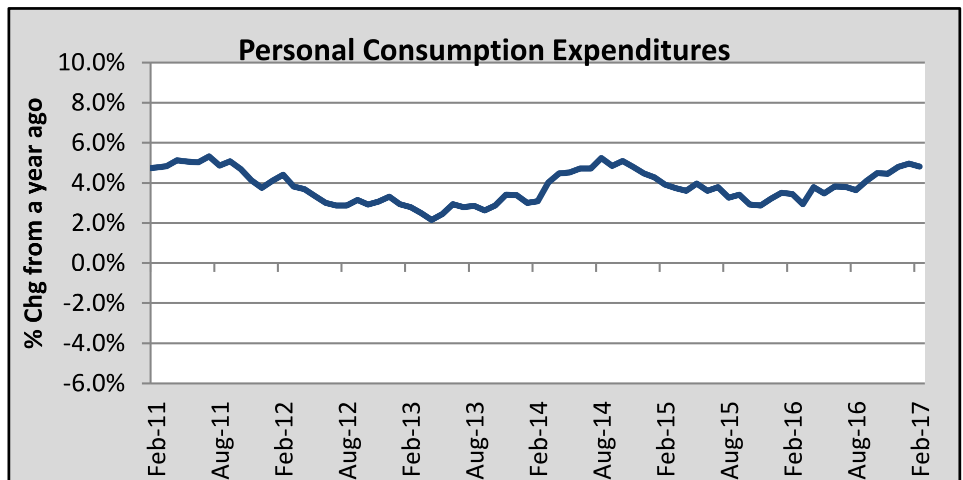
improvement since the election would be hard to dismiss as merely a post-election bounce. Overall consumer confidence has risen about 25 points since October and coincides with improvement in other consumer surveys, as well as surveys of manufacturers, small businesses and homebuilders. This should bode well for strengthened economic activity in the coming months.

Retail Sales: Retail sales rose by 0.1% in February while January spending was revised up by 0.6%. The upward revisions to January data have pointed to a much healthier consumption profile than previously anticipated, and would suggest that the enthusiasm to shop carried into 2017. Overall, consumption was expected to exceed 2% during the first quarter of 2017 despite the warmer weather that pulled down spending on winter clothing and utilities.



Recent retail sales figures have indicated changing patterns in consumer behavior, with Americans increasingly opting for online purchases and shying away from department stores. Having said that, consumers are expected to continue driving growth this year, as strong job gains and income gains enable American consumers to spend more.

Inflation: The personal-consumption expenditures price index, which is the Fed's preferred inflation gauge, edged up in February and climbed 2.1% from a year earlier, the largest annual gain for the price measure since March 2012. The core inflation, which excluded volatile food and energy prices, rose 1.8% from a year earlier, matching the highest levels touched since 2012, though still a bit below the 2% mark.

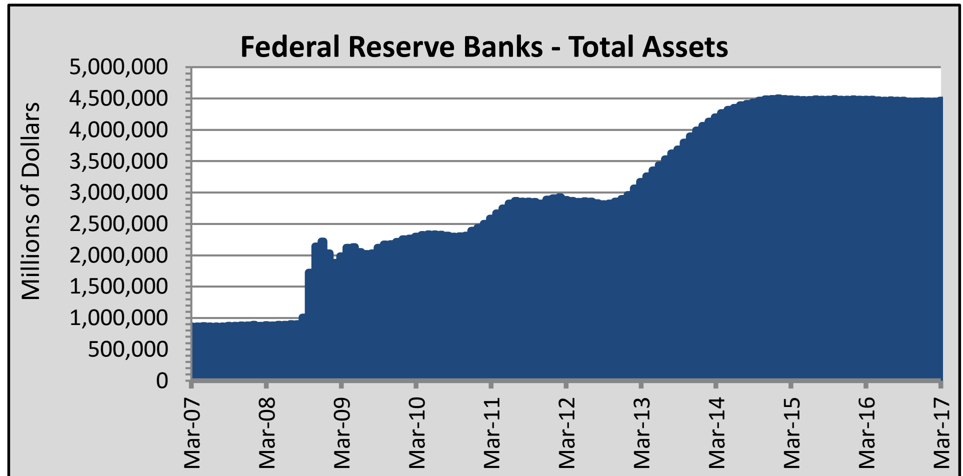


Inflation's rise, driven in part by firming wage growth, serves as a signal that slack in the economy in the form of excess industrial capacity, high unemployment and empty buildings have diminished, removing the forces that have weighed on consumer prices for several years. Firmer inflation will give Fed officials leeway to follow through with plans to raise interest rates and reduce their bond holdings.

Housing: While current quarter consumer spending will likely be soft, housing market data has begun to surprise to the upside. Pending home sales climbed 5.5% in February after falling 2.8% in January. In addition, new home construction bounced back in February more than offsetting January's decline. New home sales were up solidly in February. Expectations of rising mortgage rates may have played a role in the unseasonably strong showing in February. Still, underlying strength in the domestic economy supported housing demand. Job and income growth should continue to bring more potential homebuyers into the market, even as mortgage rates rise. Rising home prices and the lean inventory of existing homes for sale should encourage more home construction going forward. Real residential investment may well expand at a 10% pace in Q1, making residential investment in Q1 one of the few bright spots in the outlook for Q1 GDP growth.

Federal Reserve: The Federal Reserve raised interest rates by a quarter percentage point at its December and March meetings - but has been noncommittal on how it will handle its bond portfolio, which grew from less than $1 trillion before the financial crisis to $4.5 trillion through asset-purchase programs aimed at lowering long-term interest rates and boosting economic growth.

The Fed should raise short-term interest rates at least two more times in 2017 and then potentially pause rate increases, perhaps late in the year. That would allow the Fed to start winding down its portfolio of securities in a gradual and measured way, as part of their broader effort to drain reservoirs of stimulus out of the financial system, before resuming additional rate increases in 2018.



Shrinking the balance sheet could cause long-term rates to rise as the Fed sells its bond portfolio into the market. Another way to reduce the balance sheet is to allow securities to mature without using the proceeds from maturing securities to buy new ones, as it does now. The Fed also must decide whether to slow reinvestment in treasuries and mortgage bonds simultaneously or to reduce the holdings of one before the other. How it proceeds is of great importance to market participants.

Trade Deficit: The U.S. posted its biggest monthly trade deficit in nearly five years in January, a potential short-term drag on growth that highlighted broader economic forces working against the current administration's plans to reshape the country's international economic agenda. The foreign-trade gap for goods and services increased 9.6% from December to a seasonally adjusted $48.5 billion in January. That was the highest monthly level since March 2012. Falling exports and rising imports weighed on overall economic output in the final three months of 2016. That pattern shifted slightly in January, with exports growing, but not as fast as imports.

A strong dollar along with domestic demand showing signs of strengthening, especially business investment, led to the increase in deficit. Both were good signs for US economic growth but would also tend to widen the trade deficit, rather than shrink it. Erasing the U.S. trade deficit is a daunting task in any economic environment and last year's gap reached just over $500 billion, led by a $309.76 billion imbalance with China.

United Kingdom: United Kingdom has invoked Article 50 of the Lisbon Treaty, officially beginning the two-year negotiation of the terms of separation from the European Union. Negotiations on the terms of the breakup between the UK and EU can now officially proceed over the next two years, with the hope that an agreement will be reached by the deadline of April 2019.

The UK economy has performed well following the Brexit referendum, with household consumption remaining resilient despite increasing uncertainty about the future of the UK. Nevertheless, rising inflation should take a bite out of the purchasing power of UK households this year and next, which should result in a gradual deterioration in consumer spending. Although the total economic costs of this breakup are still unknown and will ultimately depend on the new relationship between the UK and the EU, the long-run growth of the UK economy is likely to slow by about 0.5 percentage points because of Brexit beginning in 2019. This is due mainly to a slower migration of workers to the UK, and a slower pace of business investment that could dampen productivity growth. Perhaps the most important unknown is what the new trade arrangement between the UK and the EU will ultimately look like.

Global Economy: The global economy ended 2016 with a strong performance, building on the momentum that took hold in the middle of the year. Global growth will be expected to rebound from last year's sub-par 2.9% rate to about average

of 3.5% in 2017-18.

Economic conditions have been better than anticipated, owing largely to outperformance in advanced economies. The relative stability in global financial markets, combined with a more optimistic economic outlook, has given the U.S. Federal Reserve confidence to tighten monetary policy. Elsewhere, central banks are not expected to follow the Fed's lead. Headline inflation rates have been rising globally, but underlying inflation in Europe and Japan has remained weak, a consequence of economic slack and other structural headwinds. This theme of policy divergence – U.S. tightening as other AEs maintain a highly accommodative monetary policy stance – should provide support for the dollar over the next couple of years.

Outlook: U.S. real GDP is expected to grow around 2.5% this year, following a 1.6% gain in 2016. This is largely due to greater domestic demand, and business investment. Measures of business sentiment have largely held on to their post-election jumps, and that optimism will likely translate into increased spending this year, particularly now that the prolonged weakness in corporate profits appears to have turned around, and the worst is over in the oil patch.

Consumer spending is being supported by strong job and income growth. Consumer confidence has also held on too much of the gain posted following the presidential election. In addition, the earlier firming in oil prices has led to a rebound in oil exploration and production. Homebuilding also appears to be gaining momentum, particularly in the South and West. The unemployment rate is expected to inch lower and inflation will continue to firm. Economic growth should remain strong enough for the Federal Reserve to hike the federal funds rate two more times, with the next hike likely coming in June.

Potential fiscal policy shifts in Washington present the main upside and downside risk to the outlook and market performance. On the upside is the potential for tax cuts and infrastructure spending. However, this is far from a certainty. Congressional Republicans would like to pass a comprehensive tax reform package. And, President Trump campaigned on more investment in infrastructure. However, Republicans have a slim majority in the Senate, and any package would need essentially universal support among GOP Senators. It is clear Republicans will need to strike significant compromise amongst themselves if this is to be achieved, as evidenced by the failure of the early proposal put forth on healthcare reform. While the equity markets appear to discount success on these policy reforms it is uncertain that these measures will pass and what form they will ultimately take if they do pass. And, it will take time for Republican members of Congress and the White House to reach a mutually acceptable compromise on these key policy priorities. Therefore, any fiscal boost would likely be a factor in the 2018 outlook and beyond, not this year. The equity market's enthusiasm over the impact of these potential changes to profits and behavior may be ahead of their actually being enacted and achieved.

On the downside is the potential for more restrictive immigration policy and protectionist trade measures. These positions may have less of an impact in the near-term, but present downside risk to U.S. medium-term economic growth. Moreover, uncertainty in these areas would cast a shadow over globally integrated companies and sectors that are reliant on international trade and the free flow of labor.

Concerns stemming from political uncertainty in Europe did clear one hurdle in March with the Dutch election result. But, France's Presidential elections loom ahead, and the UK has triggered two years of Brexit negotiations with the EU. The potential for euro-driven market volatility to disturb markets' current placid optimism will remain a threat.

1st Quarter 2017 Capital Markets in Review

Recap: The S&P 500 Index produced an impressive 6.1% total return in the first quarter setting a strong start to 2017. Meanwhile, the Barclays U.S. Aggregate Bond Index climbed 0.8% in the first quarter as interest rates trended downward over the quarter despite the Federal Reserve raising interest rates in December 2016 and once again during the quarter at its March meeting. The stock market has been propelled by investor optimism around the new administration producing some real changes in Washington and fostering improvements to economic growth and corporate earnings. Expectations may be a bit ahead of actual results so far, but in all fairness, it has only been a couple of months since President Trump took the reins and his cabinet has not even been fully established to date.

Primary concerns for the markets include above average equity valuations, the impacts of rising interest rates off of historically low levels, periodic conflicting signals from officials at the Federal Reserve regarding the timing and number of rate hikes in 2017, and the potential for political surprises overseas that could influence market clarity. But so far, the bull has been in the driver's seat in 2017, pushing the U.S. stock market indexes to new record levels alongside a growing list of skeptics within the strategist ranks.

Domestic Stocks: A wide variety of domestic stock market benchmark indexes returned to new record highs during the quarter. This was supported by a domestic economy that continued to show signs of gradual improvement, or at least few signs of broad slippage.

Additionally, foreign economies appeared to be gaining some traction and investors saw promise in gradual improvements in corporate earnings. Research analysts began the year expecting overall 2017 S&P 500 operating earnings to come in near $131, a 20% increase over the 2016 tally. As of this writing, the final actual Q4 2016 earnings results (98% reported) look like they will come in a couple dollars light of the forecast at the start of the year. However, the quarter's results still mark a turning point back to positive earnings growth, and with a more favorable outlook for Energy sector earnings fueled by more stable oil prices, hopes run high for continued earnings strength throughout the year.

Mid and small-cap stocks lagged their larger brethren in the quarter, slowing down a bit from the relative strength seen at the end of 2016. Nonetheless, the Russell Mid-Cap Index still rose a respectable 5.2% in the quarter and the Russell 2000 Index representing small stocks rose 2.5%. There is hope that these areas of the market would continue to see broader investor interest during the year, after seeing several recent years of underperformance prior to 2016.

Interestingly, Growth stocks regained the momentum over Value stocks to start off 2017. The Russell 1000 Growth Index climbed over 8.9% based on total return, while the Russell 100 Value Index came in under 3.3% for the quarter. Similar margins were seen within the Russell Mid Cap and Russell 2000 Growth and Value universes. Sector performance was a primary driver of this divergence as Growth stocks were aided by strong results in Technology, Health Care and Consumer Discretionary stocks. Financials make up a larger share of the Value universes and this sector was unable to sustain the advances seen at the end of last year.

Sector performance for the S&P 500 Index was predominantly positive for the quarter with 9 of 11 sectors in positive territory. Technology was the top performing sector coming in near 12.6%, followed by Consumer Discretionary (8.5%) and Health Care (8.4%). Energy shares declined 6.7% during the quarter as oil prices weakened a bit from where they started the year. The telecom sector was also negative during the quarter, coming in at -4.0%. The Financials sector (+2.5%) was the laggard among positive sectors.

Foreign Stocks: Developed equity and Emerging Markets outside the U.S. also posted some admirable results to kick off 2017, which was nice to see following several years of lagging performance. The MSCI EAFE rose 7.3% for the quarter and the MSCI ACWI ex USA Index (that has greater emerging markets exposure) was up 7.9%. Foreign stock markets started 2017 with some uncertainty due to a fair number of upcoming elections, particularly in Europe. Concerns have been centered on whether any additional populist victories could ultimately lead to the demise of the European Union. We do not share this view and put low odds on such an extreme outcome. Recent economic traction from stimulus measures has also shown some results and should bode well for earnings improvements overseas. These factors could dampen voter enthusiasm for sweeping political upheaval.

Emerging Markets stocks also performed quite well in the quarter as commodity markets provided a favorable backdrop. These markets also seemed to shrug off prior fears that the new U.S President Trump would pursue a detrimental shakeup in globe trading agreements. The MSCI EM Index rose 11.5% for the quarter, surpassing the return seen in all of 2016.

Bonds: The US 10-Year Treasury closed the quarter with a 2.39% yield (down slightly from 2.45% at year-end 2016). Similar 10-Year notes for Germany and Japan posted yields near 0.33% and 0.07%, respectively. The Barclays U.S. Aggregate Index rose 0.8%, despite the Federal Reserve raising interest rates by 25 basis points in March, while the Barclays Global Aggregate ex U.S. rose 2.5% - with Emerging Market debt performing even better.

The high yield bond market continued to see strong investor demand. For the quarter the Barclays High Yield Corporate Index was up 2.7%. The asset class certainly benefited from improving stability in energy markets and decreased likelihood of a sharp rise in default rates of those borrowers. Income-oriented investors continued to flock to the segment believing that gradual economic improvements would support the underlying debt.

Non-Traditional Investments: Commodity-related investments saw mixed results during the quarter. MLP investors saw decent results despite declines in the S&P 500 Energy sector and lower oil prices. West Texas Intermediate crude oil slipped from near $56 at the start of the year to $51 at the end of the quarter. Meanwhile the Alerian MLP Index managed to climb about 4%.

Real estate investments fared a bit better this quarter relative to past periods when higher interest rates weighed on the market segment. The FTSE NAREIT Equity REIT Index rose 1.2% in the quarter. Rising interest rate environments can stoke investor concerns of negative impacts to property values. However, these fears often prove short-lived, particularly in markets with positive fundamentals and rental rates adjusting higher.

Outlook: It is appropriate to reiterate that strategic investors should keep their focus on maintaining a disciplined long-term positive perspective on capital markets. Attempts to make substantial portfolio adjustments as markets ebb and flow for all kinds of reasons are not likely to prove fruitful. Preference should be placed on meaningful and purposeful strategic allocations to client portfolios and adjusting them modestly from time to time as needs arise or conditions change. With relatively reasonable market expectations, diversified portfolios should continue to provide investors an appropriate balance of risk and return.

Index Performance as of 3/31/17

	1 Week	1 Month	QTD	3 Month	YTD	1 Year	3 Year	5 Year
Russell								
3000 Value	1.02	-1.01	2.99	2.99	2.99	19.98	8.58	13.08
3000	1.01	0.07	5.74	5.74	5.74	18.08	9.75	13.18
3000 Growth	1.00	1.16	8.63	8.63	8.63	16.29	10.90	13.22
1000 Value	0.87	-1.02	3.27	3.27	3.27	19.24	8.67	13.13
1000	0.90	0.06	6.03	6.03	6.03	17.44	9.98	13.26
1000 Growth	0.92	1.16	8.91	8.91	8.91	15.77	11.27	13.32
Mid Cap Value	1.52	-0.73	3.76	3.76	3.76	19.83	8.94	14.07
Mid Cap	1.25	-0.16	5.15	5.15	5.15	17.04	8.48	13.09
Mid Cap Growth	0.93	0.55	6.89	6.89	6.89	14.08	7.88	11.96
2000 Value	2.71	-0.85	-0.13	-0.13	-0.13	29.39	7.62	12.55
2000	2.37	0.13	2.47	2.47	2.47	26.24	7.21	12.36
2000 Growth	2.01	1.18	5.35	5.35	5.35	23.05	6.72	12.10
Standard & Poors								
S&P 500	0.82	0.12	6.07	6.07	6.07	17.18	10.37	13.30
Consumer Disc	1.66	2.05	8.45	8.45	8.45	13.18	12.63	16.25
Consumer Staples	-0.11	-0.30	6.36	6.36	6.36	6.17	11.29	12.90
Energy	2.21	-1.03	-6.68	-6.68	-6.68	14.27	-4.98	1.72
Financials	0.86	-2.77	2.53	2.53	2.53	32.63	11.65	15.38
Health Care	0.15	-0.42	8.37	8.37	8.37	11.60	10.11	16.66
Industrials	0.93	-0.69	4.56	4.56	4.56	18.39	9.93	14.17
Information Technology	1.08	2.55	12.57	12.57	12.57	24.93	16.82	14.64
Materials	1.49	0.48	5.86	5.86	5.86	19.23	5.56	9.46
Real Estate	0.92	-1.03	3.54	3.54	3.54	2.50	10.63	10.06
Telecom Services	-0.78	-1.15	-3.97	-3.97	-3.97	1.69	7.92	10.29
Utilities	-1.18	-0.19	6.39	6.39	6.39	7.07	11.31	12.10
Other U.S. Equity								
Dow Jones Industrial Avg.	0.32	-0.60	5.19	5.19	5.19	19.92	10.61	12.16
MSCI USA	0.85	0.14	6.23	6.23	6.23	17.46	10.17	13.20
Wilshire 5000 (Full Cap)	1.08	0.13	5.72	5.72	5.72	18.53	9.43	13.02
International Equity - Broad Market								
MSCI EAFE	0.00	2.75	7.25	7.25	7.25	11.68	0.50	5.83
MSCI EM	-1.06	2.52	11.45	11.45	11.45	17.23	1.17	0.81
MSCI Frontier Markets	-0.97	2.47	8.89	8.89	8.89	12.87	-1.65	5.83
MSCI ACWI	0.36	1.22	6.91	6.91	6.91	15.05	5.08	8.37
MSCI ACWI Ex USA	-0.19	2.54	7.86	7.86	7.86	13.14	0.56	4.36
MSCI AC Asia Ex Japan	-0.35	3.27	13.39	13.39	13.39	17.48	4.66	4.77
International Equity - Country Region								
MSCI Brazil	-0.18	-4.50	10.37	10.37	10.37	42.83	-3.47	-7.35
MSCI BRIC	-0.56	1.69	11.58	11.58	11.58	23.46	2.70	0.42
MSCI China	-1.29	2.13	12.93	12.93	12.93	19.70	6.40	5.59
MSCI Europe	0.32	4.02	7.44	7.44	7.44	9.77	-1.51	5.63
MSCI India	1.57	5.98	17.12	17.12	17.12	18.41	7.46	6.26
MSCI Japan	-1.50	-0.37	4.49	4.49	4.49	14.45	6.02	6.82
MSCI EM Latin America	-0.38	0.55	12.06	12.06	12.06	23.27	-3.98	-6.11
MSCI Russia	-1.01	2.13	-4.61	-4.61	-4.61	27.62	-1.13	-4.40

Index Performance as of 3/31/17

	1 Week	1 Month	QTD	3 Month	YTD	1 Year	3 Year	5 Year
Fixed Income								
Barclays U.S. Aggregate	0.07	-0.05	0.82	0.82	0.82	0.44	2.68	2.34
BofAML 3-Month T-Bill	0.01	0.02	0.10	0.10	0.10	0.36	0.17	0.14
Barclays U.S. Gov't	0.03	-0.04	0.68	0.68	0.68	-1.34	2.04	1.59
Barclays U.S. Credit	0.06	-0.15	1.30	1.30	1.30	2.97	3.52	3.70
Barclays High Yield Corp.	0.89	-0.22	2.70	2.70	2.70	16.40	4.56	6.82
Barclays Municipal	0.19	0.22	1.58	1.58	1.58	0.15	3.55	3.25
Barclays TIPS	-0.05	-0.05	1.26	1.26	1.26	1.48	2.03	0.97
Barclays Gbl Agg Ex USD	-0.37	0.30	2.48	2.48	2.48	-3.93	-2.68	-1.13
Barclays Global Aggregate	-0.17	0.15	1.76	1.76	1.76	-1.90	-0.39	0.38
BofAML Emerg. Mkt. Cred	0.25	-0.07	4.22	4.22	4.22	18.95	8.32	8.37
Alternative Investments								
Alerian MLP	2.14	-1.30	3.95	3.95	3.95	28.34	-5.17	2.64
Bloomberg Commodity	0.99	-2.66	-2.33	-2.33	-2.33	8.72	-13.91	-9.54
FTSE NAREIT Equity REIT	0.87	-2.29	1.16	1.16	1.16	3.57	10.26	9.99
S&P Global Natural Res.	0.50	-0.11	2.92	2.92	2.92	24.62	-2.22	-1.03
S&P N. Amer Natural Res.	2.56	-0.57	-4.25	-4.25	-4.25	17.94	-5.88	-0.45

Sources: Department of Labor, Department of Commerce, The Conference Board, National Association of Realtors, Standard & Poors.

Securities are not insured by FDIC or any other government agency, are not bank guaranteed, are not deposits or a condition to any banking service or activity, are subject to risk and may lose value, including the possible loss of principal.