INVESTMENT COMMITTEE MARKET COMMENTARY

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U.S. EQUITIES

U.S. equity markets saw the Dow and the S&P 500 register their sixth straight weekly gain, while the Nasdaq finished higher for a fourth week in a row. Markets rallied as the Senate passed a budget plan that cleared the way for the start of negotiations regarding tax legislation.

a) **Dow Jones +2.04%, MTD +4.22%, YTD +20.33%** b) **S&P 500 +0.88%, MTD +2.31%, YTD +16.88%**
c) **Russell 2000 +0.45%, MTD +1.27%, YTD +12.36%**

Drivers: I) The **Senate passed a budget resolution** last Thursday night, but still needs to agree with the House on a single budget document. The House passed its own budget plan earlier this year, but the chamber may take up the version that passed the Senate. A Republican spokesperson said it is likely the House will do that. Such a move would eliminate the need to go to a conference, where differences between bills are resolved.

II) Once a **budget agreement is passed by Congress**, they can **move along to tax reform**. Republicans have released a tax reform framework that calls for cutting the top corporate rate to 20% from 35%; reducing the existing seven individual tax rates into three; and repealing the estate tax. Many issues remain to be resolved, including the amount of an increased child tax credit and how state and local tax deductions are addressed.

III) **Factory orders** reported by the Commerce Department over the last 12 months has been favorable but uneven which is due to monthly swings for aircraft orders. Yet the trend, despite weakness in August and July, is above the zero and climbing. The dollar total was a seasonally adjusted **$472 billion for an annual gain of 5.7%**, which is a very respectable mid-single-digit pace.

IV) **Housing starts ran at a 1.13 million** seasonally adjusted annual rate, down 4.7% for the month, the Commerce Department reported. Street consensus was for a 1.17 million pace. Starts were 6.1% higher compared to a year ago. A positive in the government's report was the **resurgence of single-family homes.** Starts for those houses were also down during the month, but stood 9.1% higher for the year to date compared to last year.

V) **Equity prices in October are higher with Large-Cap, Growth, Information Technology and Utilities leading equity price performance. The laggards for the month are Small-Cap, Value, Energy and Con. Staples.**

Capitalization: **Large Caps +2.29%** (YTD +16.78%), Mid-Caps +2.21% (YTD +14.20%) and **Small Caps +1.27%** (YTD +12.36). **Style: Value** +**1.37%** (YTD +8.27%) and **Growth +2.33%** (YTD +14.14%). **Industry Groups (Leaders): Info. Tech +3.87% (**YTD +31.30%), Tech +3.28% (YTD +27.87%), Healthcare +2.58% (YTD +23.10%), Materials +3.41% (YTD +19.81%), Industrials +2.76% (YTD +18.90%), Financials +3.10% (YTD +15.87%), **Utilities +3.45%** (YTD +15.61%), Con. Discretionary +1.39% **(**YTD +13.35%), REITs +1.50% (YTD +8.87%) and **Con. Staples -0.13%** (YTD +6.27%). **(Laggards):** Telecom -0.74% (YTD -6.09%) and **Energy -0.97%** (YTD -7.59%).

EUROPEAN EQUITIES

The MSCI Europe index was lower by -0.65% last week as investors watched the unfolding of Spain's Catalonia situation along with the latest moves in the UK/EU Brexit negotiations.

Drivers: I) **British Prime Minister Theresa May** won a modest reprieve in **stalled talks with the European Union** as EU leaders said they would begin preparations to move into the second phase of Brexit talks in December. EU Council President Tusk indicated that EU leaders have agreed on a joint Brexit position and given the go-ahead to begin preparations for the second phase of talks.

II) Last Thursday, the **Madrid government indicated that it would suspend Catalan autonomy** and begin the process of imposing direct rule. The announcement came after Catalan leader Carles Puigdemont failed to meet a deadline to withdraw a declaration of independence. The national government will seek to approve measures to impose article 155 in the Spanish constitution, thus the Catalan region will be **ruled directly from Spain's capital.**

III) **Performance of European Indexes for the week, month-to-date and year-to-date. The MSCI Europe Index was down by -0.65% for the week (MTD +0.36% YTD +23.23%).**

ASIAN EQUITIES

Asian markets were higher last week, but muted, as investors waited for the outcome of Sunday's Japanese general election. Also, the People's Bank of China's Governor Zhou Xiaochuan warned that asset prices could fall in China after a period of growth, due to currency and debt issues. The Dow Jones Asia Index rose by +0.60% for the week, (MTD +3.34% YTD +21.06%).

Drivers: I) **Prime Minister Abe** is seeking to **consolidate power in Japan's parliament**, which his conservative Liberal Democratic Party currently leads in a coalition with the center-right Komeito party. According to the Mainichi newspaper survey, **Abe's LDP is set to win 281 to 303 seats out of 465 seats** on Sunday.
The prime minister's approval ratings improved in the wake of escalating tensions with North Korea.

II) According to **PBoC governor Zhou Xiaochuan**, China will fend off risks from **excessive optimism** that could lead to a **Minsky Moment (an asset bubble).** China will control risks from sudden adjustments to asset bubbles and will seriously deal with disguised debt of local government financing vehicles, Zhou said. But China's overall debt levels could decline if authorities keep a tight control on credit. Worries about a rapid build-up in China's debt prompted S&P to cut China's sovereign credit rating last month, following a cut by Moody's in May.

III) **Performance of Asian Indexes for the week, month-to-date and year-to-date. The Nikkei was up by +1.43% (MTD +5.41%, YTD +14.15%), the Hang Seng Index advanced by +0.09% (MTD +3.48%, YTD +28.68%) and the Shanghai Composite was lower by -0.35% (MTD +0.89%, YTD +8.86%).**

FIXED INCOME

Treasury yields rose last week as prospects of the tax cut "brightened" when the Senate approved a budget resolution and in anticipation of another Fed rate hike coming in December.

Performance: I) **The 10-year Treasury yield was higher last week ending at 2.383% up from 2.275%. The 30-year yield rose last week advancing from 2.805% to 2.898%.**

II) **Performance for the week, month-to-date and year-to-date. The Bloomberg Barclays US Aggregate Bond Index fell -0.45% last week, MTD -0.13% and YTD +3.01%. The Bloomberg Barclays US MBS TR was down -0.43% last week, MTD -0.21% and YTD +2.10%. The Bloomberg Barclay's US Corporate HY Index rose +0.31%, MTD +0.50% and YTD +7.53%.**

COMMODITIES

The DJ Commodity Index was down -0.74 last week but is higher month to date +0.92% (YTD +0.14%) as the dollar climbed higher after the U.S. Senate approved a budget plan for the 2018 fiscal year that will ease passage for Republicans to pursue a tax-cut package.

Performance: I) **Oil prices rose** last week by +1.26% up to $52.07 and is higher month to date for October +0.83% (YTD -3.38%). Oil jumped higher, boosted by bullish Chinese data and geopolitical risks in the Middle East, particularly in the wake of President Donald Trump's refusal to certify Iran's compliance with the nuclear deal.

II) The **ICE USD Index**, a gauge of the U.S dollar's movement against six other major currencies, **rose +0.65%** from 93.05 to 93.66 for the week (MTD +0.63% YTD -8.51%). The U.S. dollar rallied after the U.S. Senate passed a budget plan, which could clear the way for tax cuts which is positive for the dollar, and extended after September home-sales report.

III) **Gold hit a two-week low on Friday**, suffering the biggest weekly loss in a month as the dollar strengthened following the Republican-controlled Senate's passage of a budget plan. Gold was **lower by -1.86**% last week, falling from $1306.1 to $1281.8 (MTD -0.05% YTD +11.27%).

HEDGE FUNDS

Hedge fund returns in October are primarily higher, as the core strategies Equity Hedge, Macro and Relative Value are in positive territory. Event Driven and Distressed are down for the month.

Performance:

I) The HFRX Global Hedge Fund Index is higher at +0.37% MTD and +4.81% YTD.
II) Equity Hedge has risen +0.57% MTD and is up +7.68% YTD.
III) Event Driven has declined MTD -0.29% and is higher YTD +6.27%.
IV) Distressed Debt is lower by -0.72% MTD and is positive YTD +1.69%
V) Macro/CTA has advanced by +1.02% MTD and is up +0.92% YTD.
VI) Relative Value Arbitrage has risen +0.32% and is higher by +3.18% YTD.

ECONOMIC DATA WATCH AND MARKET OUTLOOK

In a look towards **next week's market action**, investors will once again ponder over the reasons as to **why global equity markets** should **experience a significant corrected**. Markets have gone through 350 trading days without a 3% drop, rising on a weekly and monthly basis gaining just under 17.0% for the S&P 500. The market has been fueled by positive global economic growth. This was confirmed by the **OECD last week**, who reported that the **45 major economies** they follow are **all in a growth mode** for the first time in a decade. But this coordinated growth, also on the plus side, has yet to induce a worrisome level of inflation.

From an **equity market perspective**, we **have yet to see the levels of euphoria** and high volumes of speculative trading we **tend to see at market tops**. Stock-market bubbles tend to form when euphoric investors bid up prices to unsustainable levels, as happened in late 1990s during the tech boom. To the contrary, despite records and elevated valuations, investor surveys show that high enthusiasm levels came down over the past few months. **Danger signs** would flash **should corporate earnings begin to slide** and disappoint.

As to **earnings season**, thus **far 87 companies in the S&P 500 have reported** results; of these, **70% have beaten analysts' sales estimates while 75% have exceeded analysts' earnings estimates**. The quarter's blended sales growth rate (which includes actual and estimated results) stands at 4.9%, while the EPS forecast, which reflects the impact of hurricanes during the period, is just 1.7%. It is possible to see **earnings come in at a better than expected mid-single digit level.**

In turning to **next week's economic calendar**, the week ends on **Friday** with the first **estimate for third-quarter GDP**. Third-quarter GDP is expected to slow to a still respectable **2.5% annualized rate** from the second quarter's very solid 3.1%. Consumer spending, seen at 2.2% versus 3.3% in the prior quarter, was mixed in the third quarter, but will get a lift from vehicle replacement demand following Hurricanes Harvey and Irma. The GDP price index is seen rising to a 1.6% rate vs 1.0% in the second quarter.

Durable goods orders are out on Wednesday which is a report where strength may be building internally. Durable goods growth has been steady and moderate with one special highlight and that's **improvement for capital goods**. **Vehicles** were another a high point of the August report with **replacement demand** a possible key plus for September. Street consensus for durable goods orders is a **1.0% gain** on top of August's 2.0% rise.

Housing will be the week's sector theme including new home sales also on Wednesday, a report that has been soft. **New home sales have been the leading strength of the nation's housing sector** despite slowing steadily through the year. Hurricane effects were evident in the South during August though other regions also declined. The consensus for September new home sales is for **an annualized rate of 555,000 vs 560,000 in August.**

Pending sales of existing homes come out on Thursday, a report that has been very soft. Pending sales, which track initial contract signings for resales, have been accurately forecasting this year's steady weakness in the existing home sales report where final sales are tracked. Weakness in August pending sales included the hurricane-hit South but other regions were soft as well. After August's surprisingly sharp 2.6% drop, the consensus for the **September** pending sales index is a **gain of 0.5%.**