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INVESTMENT COMMITTEE MARKET COMMENTARY

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U.S. EQUITIES

U.S. equity market indexes finished the week hitting fresh all-time highs, capping off their best start since 2003, propelled by a solid start to the earning's season and solid economic data.

a) **Dow Jones +2.02%, MTD +4.44%, YTD +4.44%** b) **S&P 500 +1.61%, MTD +4.28%, YTD +4.28%**
c) **Russell 2000 +2.06%, MTD +3.70%, YTD +3.70%**

Drivers: I) The **consumer price index rose 0.1% in December**, with four-fifths of the increase tied to the highest cost of housing. The increase matched the Street forecast. The **12-month rate** of inflation as measured by the CPI dropped to **2.1%** from 2.2%. The more closely followed core rate edged up to 1.8% from 1.7%, and it has been trapped in this range for eight months in a row.

II) **Sales at U.S. retailers rose 0.4%** in December, a fourth straight monthly gain. Excluding automobiles and gasoline, retail sales also rose 0.4% last month. **Retail sales rose a healthy 4.2% in 2017**, the **largest increase in three years**, to reflect the strongest U.S. economy since the early 2000s. And strong sales in the fourth quarter could push GDP above 3.0% for the third quarter in a row.

III) U.S. **wholesale prices rose in 2017** at the **fastest pace in six years**, a buildup in inflation that could push the Federal Reserve to raise interest rates more aggressively unless it slows down. The **producer price index increased 2.6% last year**, even after a small decline of 0.1% in December. The core PPI rose 0.1% in December, however.

IV) The **S&P 500 Index has gone 387 sessions without a 5% drawdown**, the second-longest stretch in the history of the index, according to Goldman Sachs data. The **longest run** occurred between 1994 and 1996, and lasted for **394 sessions**. If the current trend continues, it will match the longest streak ever at the end of trading on Jan. 18, a Thursday.

V) **Equities in January are higher with Large-Cap, Growth, Energy and Industrials leading equity price performance. The laggards for the month are Mid-Cap, Value, Real Estate and Utilities.**

Capitalization: **Large Caps +4.18%** (YTD +4.18%), **Mid-Caps +3.57%** (YTD +3.57%) and Small Caps +3.70% (YTD +3.70). **Style: Value +3.06%** (YTD +3.06%) and **Growth +3.91%** (YTD +3.91%). **Industry Groups (Leaders):** Energy +7.31% (YTD +7.31%), Consumer Discretionary +6.51% (YTD +6.51%), Industrials +6.06% (YTD +6.06%), Information Tech +5.23% (YTD +5.23%), Healthcare +5.12% (YTD +5.12%), Materials +4.83% (YTD +4.83%), Financials +4.70% (YTD +4.70%), Tech +4.63% (YTD +4.63%) and Telecom +0.20% (YTD +0.20%). **(Laggards): REITs -5.27%** (YTD -5.27%), **Utilities -4.51%** (YTD -4.51%) and Consumer Staples -0.37% (YTD -0.37%).

EUROPEAN EQUITIES

The MSCI Europe index was higher last week rising by +1.26%, as German politicians reached a breakthrough in talks to form new coalition government. Minutes from the recent meeting of the ECB revealed they may change the tone of its monetary policy communication early this year to reflect improving growth prospects.

Drivers: I) The **German economy expanded at the fastest pace in six years** in 2017 driven by domestic demand. **Gross domestic product was up 2.2%** on the year in 2017 after growing 1.9% in 2016. Germany has now expanded eight consecutive years with 2017 being the fastest growth since 2011. The growth rate exceeded the average of the last 10 years by almost 1.0%.

II) At the December meeting, **ECB staff upgraded its forecasts for growth to 2.4% in 2017** and 2.3% in 2018. Households and businesses in the region were expected to keep spending and investment activity was also forecast to pick up. And the "output gap", which refers to the gap between where growth now is and where it would be were the economy operating at its full capacity, would close earlier than previously projected.

III) **Performance of European Indexes for the week, month-to-date and year-to-date. The MSCI Europe Index was higher by +1.26% for the week (MTD +3.60%, YTD +3.60%).**

ASIAN EQUITIES

Asian markets were mixed as the Japanese currency rallied for a third straight day after the Bank of Japan cut the size of ongoing purchases of government bonds for one bucket of longer-term debt. The Dow Jones Asia Index rose by +1.21% for the week, (MTD +3.76%, YTD +3.76%).

Drivers: I) Last Tuesday, markets were surprised by the **Bank of Japan's decision to reduce its purchases of 10 to 25-year JGBs and 25 to 40 JGBs paper by ¥10 billion each**, from its previous operations, to ¥190 billion and ¥80 billion respectively. But the BoJ maintained the amount of its bond purchases on Thursday, helping to soothe a market upset earlier this week by a cut in its buying of longer-dated debt that engendered worries that the Bank may be moving to turn off its stimulus.

II) **China's December consumer price index increased 1.8%** on the year, up from 1.7% in November. The increase in headline inflation was driven by a smaller decline in food prices, which declined by 0.4% on the year after dropping by 1.1% in November. On the year increases in non-food prices moderated from 2.5% to 2.4%.

III) **Performance of Asian Indexes for the week, month-to-date and year-to-date. The Nikkei was lower by -0.26% (MTD +3.90%, YTD +3.90%), the Hang Seng Index rose by +1.89% (MTD +4.88%, YTD +4.88%) and the Shanghai Composite was up by +1.10% (MTD +3.68%, YTD +3.68%).**

FIXED INCOME

Treasury yields rose last week as the 10-Year hit a nine-month high. Benchmark US rates have risen steadily so this year as inflation expectations climbed and investors prepared for the eventual reduction in stimulus from both the Bank of Japan and European Central Bank, as well as tighter policy from the Federal Reserve.

Performance: I) **The 10-year Treasury yield was higher last week ending at 2.549 up from 2.477%. The 30-year yield rose last week advancing from 2.808% to 2.849%.**

II) **Performance for the week, month-to-date and year-to-date. The Bloomberg Barclays US Aggregate Bond Index dropped by -0.18% last week, MTD -0.50% and YTD -0.50%. The Bloomberg Barclays US MBS TR was down -0.21% last week, MTD -0.38% and YTD -0.38%. The Bloomberg Barclay's US Corporate HY Index fell by -0.04%, MTD +0.69% and YTD +0.69%.**

COMMODITIES

The DJ Commodity Index was higher by +1.40 last week and is higher MTD +1.22% (YTD +1.22%), after energy rose on declining supplies and precious metals advanced on rising inflation expectations.

Performance: I) The price of **oil rose last week by +4.56%** up to $64.40 and is higher month to date for January +7.15% (YTD +7.15%). Oil prices were higher last week, as a spate of weekly declines in U.S. crude stockpiles helped prices attain a fifth consecutive session of gains.

II) The **ICE USD Index**, a gauge of the U.S dollar's movement against six other major currencies, **fell -1.20%** from 92.01 to 90.90 for the week (MTD -1.51%, YTD -1.51%). The U.S. dollar fell against its major counterparts as the ECB and BOJ indicated they were ready to reduce stimulus due to stable and improving economic conditions.

III) **Gold scored a fifth week of gains in a row**, finding support as the dollar extended its earlier decline despite a slightly higher-than-expected climb in core U.S. inflation. Gold was up by +1.36% last week, rising from $1320.3 to $1338.3 (MTD +2.54%, YTD +2.54%).

HEDGE FUNDS

Hedge fund returns for January are in positive territory, with all core strategies Equity Hedge, Event Driven, Distressed, Macro and Relative Value higher for the month.

Performance:

I) The HFRX Global Hedge Fund Index is higher at +1.67% MTD and +1.67% YTD.
II) Equity Hedge is up +2.30% MTD and is up +2.30% YTD.
III) Event Driven has advanced MTD +1.72% and is higher YTD +1.72%.
IV) Distressed Debt is higher by +1.17% MTD and is positive YTD +1.17%
V) Macro/CTA has risen by +2.19% MTD and is up +2.19% YTD.
VI) Relative Value Arbitrage has advanced by +0.57% and is higher by +0.57% YTD.

ECONOMIC DATA WATCH AND MARKET OUTLOOK

As we look ahead to **next week's trading session**, investors will be anxious to see if the **best start for equity market returns in decades will be supported by strong corporate earnings**. As important, will **forward earnings guidance from corporations** provide a solid base for equities to continue their momentous climb? Thus, a healthy global economy and higher oil prices support a pickup in growth, and record U.S. data surprises along with record results from early earnings reports **suggest many corporations will beat their estimates**.

FactSet, projected S&P 500 companies will report fourth-quarter earnings **rise of 10.2%,** the second-strongest since 2011, based on the consensus forecasts of analysts. However, the **actual pace of earnings increase** may be **closer to 14%**, given the large number that are **turning in results above estimates**. FactSet also predicted that **all 11 S&P 500 sectors** will post both **earnings and revenue growth in the fourth quarter**, something that has **not happened** since the **third quarter of 2011.**

In turning to next week's economic calendar, a week shortened by Monday's Martin Luther King holiday will bring **definitive data on December's factory sector**. On **Wednesday** morning, we will receive data on industrial production where the outlook is surprisingly soft. The Street's consensus gain for **December industrial production is 0.4% which would follow November's 0.2% rise**. Based on factory hours in December's employment report, forecasters see the manufacturing component rising a moderate 0.3% to extend what has been a stubbornly soft trend for this series. Total capacity utilization in December is seen rising 0.2% to 77.3%.

Housing was the big strength of the year-end economy and **solid performances are expected for December housing starts and permits on Thursday**. A small drop is the call for December's housing starts and permits data which posted significant gains in November and October. Single-family homes, the dominant component in this report, have been the center of recent strength and have more than offset extending weakness for multi-family units. The **consensus for December housing starts is a 1.280 million annualized** rate versus 1.297 million in November with **housing permits seen at a 1.300 million rate** versus November's revised 1.303 million (1.298 million initially reported).

Consumer sentiment ends the week on Friday and a bounce higher is the call. Though the consensus is up for January, consumer sentiment did slow noticeably in December especially toward the end of the month. Expectations were December's weakness offset only in part by a positive assessment of current conditions and much welcome improvement in inflation expectations. Street consensus for the preliminary **January consumer sentiment index is 97.0** which would **compare with 95.9 in December and 98.5 in November.**