U.S. EQUITIES

U.S. equity markets saw the S&P 500 and NASDAQ close on Friday at new highs, rallying for a third straight week, as optimism over corporate earnings over came worries of a government shutdown.

a) **Dow Jones +1.08%, MTD +5.56%, YTD +5.56%** b) **S&P 500 +0.88%, MTD +5.20%, YTD +5.20%**
c) **Russell 2000 +0.36%, MTD +4.08%, YTD +4.08%**

Drivers: I) The **US House on Thursday passed a one-month spending bill** that would keep the government funded through Feb. 16, but the temporary measure currently **did not have enough support to clear the Senate**. The current interim funding bill that was passed in December expired at 12:01 a.m. Eastern Time on Saturday.

II) Historical data shows that **markets have seen modest weakness during shutdowns**, with the S&P 500 falling an average of 0.6% over the period of the closure, according to LPL Financial. The benchmark index was only positive in 44.4% of the 18 shutdowns going back to 1976. A shutdown's lasting market effect also remains unclear, but **the S&P 500 rose during the past three shutdowns** regardless of its length.

III) The **S&P 500 broke a 20-year record** as the index has gone **395 sessions without a 5% drawdown**, the longest stretch in the history of the index. The previous record occurred between 1994 and 1996 and had lasted for 394 sessions. The S&P 500 has closed higher in 10 of the 13 sessions that have occurred thus far this year, ending at a record in each of its positive sessions.

IV) **Industrial production rose 0.9% in December** for the fourth straight monthly increase, the Federal Reserve reported Wednesday. The **gain was above Wall Street expectations** of a 0.6% increase. For the fourth quarter, production jumped at an 8.2% annual rate, after a 1.3% drop in the prior quarter caused by hurricane damage. For the **calendar year, production rose 3.6%,** up from a 0.8% gain in 2016 and the **fastest pace since 2010**.

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

Capitalization: **Large Caps +5.07%** (YTD +5.07%), **Mid-Caps +4.06%** (YTD +4.06%) and Small Caps +4.08% (YTD +4.08). **Style: Value +3.13%** (YTD +3.13%) and **Growth +5.23%** (YTD +5.23%). **Industry Groups (Leaders): Consumer Discretionary +7.10% (**YTD +7.10%), **Healthcare +7.08%** (YTD +7.08%), Information Tech +6.80% **(**YTD +6.80%), Tech +6.11% (YTD +6.11%), Energy +5.89% (YTD +5.89%), Financials +5.80% (YTD +5.80%), Industrials +5.44% (YTD +5.44%), Materials +4.62% (YTD +4.62%) and Consumer Staples +2.07% (YTD +2.07%). **(Laggards): Utilities -5.01%** (YTD -5.01%), **REITs -4.48%** (YTD -4.48%) and Telecom -0.23% (YTD -0.23%).

EUROPEAN EQUITIES

The MSCI Europe index was higher last week rising by +1.23%, climbing for a third straight week to end at its highest level since August 2015. Markets were driven by the continued rally in tech stocks and hopes that a coalition government will be formed this weekend in Germany.

Drivers: I) Exhaustive **talks between German Chancellor Merkel's Christian Democrats (CDU)** and their Bavarian ally, the **Christian Social Union (CSU)** with the opposition **Social Democrats (SPD)** appear to have achieved a **breakthrough**. Germany has been in political limbo since the inconclusive elections last September and efforts to maintain the existing 'grand coalition' between the two sides have been ongoing since. An apparent removal of a major source of political uncertainty should be an important **plus for the euro and Eurozone stock markets.**

II) December's final harmonized index of **consumer prices confirmed the 1.4% yearly rate** posted in the flash report. The two main core rates continued to indicate **no increase in underlying inflation pressures**. This was down from November's 1.5% and reflected a 0.4% monthly gain in prices. The narrowest measure, which excludes energy, food, alcohol and tobacco, was unrevised at a 0.9% annual rate for a second month.

III) **Performance of European Indexes for the week, month-to-date and year-to-date. The MSCI Europe Index was higher by +1.23% for the week (MTD +4.87%, YTD +4.87%).**

ASIAN EQUITIES

Asian markets rose last week following the lead of US markets which ended higher, and was further supported by positive economic data from China. The Dow Jones Asia Index rose by +1.31% for the week, (MTD +5.12%, YTD +5.12%).

Drivers: I) The pace of growth in **China's economy accelerated last year for the first time in seven years** as exports, construction and consumer spending all climbed strongly. China's National Bureau of Statistics announced on Thursday that the **economy expanded 6.9%** last year, up slightly from 6.7% in 2016 and breaking a trend of gradual slowing that began in 2011. For the fourth quarter, the bureau reported economic growth of 6.8% over a year earlier.

II) In **Japan,** November private sector **machinery orders** (excluding volatile items) **advanced 5.7%** on the month after increasing 5.0% in October. This series, which excludes orders for ships and those from electric power companies, is considered a **proxy for capital expenditures**. On the year, orders were up 6.1%. Orders strengthened in the non-manufacturing sector, but weakened in the manufacturing sector.

III) **Performance of Asian Indexes for the week, month-to-date and year-to-date. The Nikkei was higher by +0.65% (MTD +4.58%, YTD +4.58%), the Hang Seng Index rose by +2.77% (MTD +7.78%, YTD +7.78%) and the Shanghai Composite was up by +1.72% (MTD +5.46%, YTD +5.46%).**

FIXED INCOME

Treasury yields jumped last week, as the 10-year Treasury hit its highest level since September 2014. Despite the potential of a US government shutdown, improving global growth and growing inflation concerns have put U.S. government debt under pressure.

Performance: I) **The 10-year Treasury yield was higher last week ending at 2.659 up from 2.549%. The 30-year yield rose last week advancing from 2.849 to 2.935%.**

II) **Performance for the week, month-to-date and year-to-date. The Bloomberg Barclays US Aggregate Bond Index dropped by -0.44% last week, MTD -0.93% and YTD -0.93%. The Bloomberg Barclays US MBS TR was down -0.44% last week, MTD -0.81% and YTD -0.81%. The Bloomberg Barclay's US Corporate HY Index fell by -0.08%, MTD +0.61% and YTD +0.61%.**

COMMODITIES

The DJ Commodity Index was lower by -0.19 last week, but is higher month to date +1.03% (YTD +1.03%), as oil declined on rising US production levels and metals declined due to rising interest rates.

Performance: I) The price of **oil rose dropped last week by -1.29%** down to $63.57 but is higher month to date for January +5.77% (YTD +5.77%). Oil prices declined on worries over growing U.S. oil production, after a major energy watchdog predicted **shale producers would help drive output** to levels not seen since the 1970s.

II) The **ICE USD Index**, a gauge of the U.S dollar's movement against six other major currencies, **fell -0.25%** from 90.90 to 90.67 for the week (MTD -1.76%, YTD -1.76%). The U.S. dollar declined last week as the potential **shutdown of the US government** put modest **downward pressure** on the dollar, as investors look to international markets for better short-term opportunities.

III) **Gold was slightly lower last week,** balancing the negative effect of rising interest rates versus concerns over a shutdown of the US government. Gold was down by -0.53% last week, falling from $1338.3 to $1331.1 (MTD +1.99%, YTD +1.99%).

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 +1.89% MTD and +1.89% YTD**.**
II) Equity Hedge is up +2.50% MTD and is up +2.50% YTD.
III) Event Driven has advanced MTD +1.47% and is higher YTD +1.47%.
IV) Distressed Debt is higher by +1.25% MTD and is positive YTD +1.25%
V) Macro/CTA has risen by +3.08% MTD and is up +3.08% YTD.
VI) Relative Value Arbitrage has advanced by +0.78% and is higher by +0.78% YTD.

ECONOMIC DATA WATCH AND MARKET OUTLOOK

As we look ahead to **next week's trading session**, investors are seeing, during the early part of the earnings reporting season, the **reduction in corporate tax rates** will likely **boost profits and the overall economy**. With only **11% of the S&P 500 reporting**, approximately **two-thirds have been earnings expectations**. Street analysts are estimating that forth quarter earnings are slated to increased 9.5%, along with a rise in revenues of about 6.2%. But of **greater importance** will be the **forward guidance** from companies, regarding the positive effect the tax cut will have on top and bottom line growth.

With the **passage of the tax bill**, **Street** prognosticators have been **raising expectations for earnings growth** in 2018. The **consensus estimates for S&P 500 earnings growth in 2018 is 18.6%,** which would bring earnings to $151.55 per share. Meanwhile, analysts expect **6% revenue growth in 2018**. Earning growth will be needed to drive stock prices higher, as P/E multiple expansion will be hard to justify based on current stock price levels. The price-to-earnings ratio based on the next year's estimated earnings is currently at 18.4, above the 5-year average of 15.9.

In turning to **next week's economic calendar**, on Monday the national activity index is expected to offer a positive assessment of December's economy. The **economy is solid based on the national activity index** which firmed through the second half of 2017 and included a 0.15 gain in November. **Retail sales** are likely to be a **positive** in the December report with building permits neutral. The manufacturing component of the industrial production report is a likely weakness. The consensus for December's national activity index is 0.25.

Existing home sales will be released Wednesday, with **new home sales** on Thursday, and **both are expected to show solid December strength** and only limited giveback from outstanding strength in November. Existing home sales had been lagging sharp acceleration in new home sales until the November report when sales jumped 5.6% to a 5.810 million annualized rate. November's rate was by far the strongest of the expansion with 5.700 million in March last year the next closest. But the sales surge drove down supply to only 3.4 months which means a lack of selection was likely to have slowed December sales. Still, a very solid 5.750 million rate is the Street consensus for December.

The **durable goods report on Friday** where forecasters are calling for **very solid results**. Durable goods orders are often bumpy, but forecasters, despite a hard comparison with November's jump in aircraft orders, do not see a downswing in December. On the contrary, **Street consensus** for **durable goods orders is a 0.8% gain** with ex-transportation seen up a solid 0.6% and core capital goods orders also seen up 0.6%.

The week's highlight is saved for **Friday** and the **first estimate on fourth-quarter GDP**, a quarter when **consumer spending is expected to have made the difference**. The first estimate for fourth-quarter GDP is expected to come in at a **2.9%** annualized rate vs 3.2% and 3.1% in the prior two quarters. Consumer spending is expected to be the driver in the fourth quarter, seen rising at a consensus gain of 3.6% which would compare with 2.2% in the third quarter and 3.3% in the second quarter. Residential spending is also expected to show strength in the fourth quarter with inventories seen as a negative.