RDM MARKET UPDATE

As we enter the Fall, 2017 we wanted to provide you with a brief update on the markets and the economy. First our thoughts are with anyone that has been affected by Hurricane Harvey in Texas as well as the upcoming storm due to hit the south eastern part of the country. Are thoughts are with you and we hope you all remain safe.

Last quarter GDP (for Q2, 2017) was revised up to an increase of 3% which compares favorably with the prior reading of 2.6% and the first quarter's 1.2%. Looking at the current quarter, the Atlanta Federal Reserve Tracker currently forecasts a rise of 3.2%. For reference, this compares with an average growth rate of just over 2% during the current 9-year economic expansion.

Overall, the U.S. economy continues to grow at a healthy rate. Looking beneath the surface, employment continues to expand (despite last month's employment report that came in somewhat below expectations), earnings are once again rising at a healthy rate (after several weak quarters during 2014 into 2015), consumer and business sentiment remains solid and credit spreads remain healthy. The ISM Manufacturing Index rose to a multi-year high last month which indicates that manufacturing activity appears to be on healthier footing than it has been in several years. Auto sales have been weak in recent months which is one area that we are keeping an eye on.

Over the past few weeks, events in Washington and geopolitical risks overseas have created temporary storm clouds that have led to a modest pickup in volatility. Among the issues on our radar, Congress has had to deal with the upcoming debt ceiling and 2018 budget (which have now both been extended until December, 2017), the Federal Reserve Bank is likely to start reducing its previous quantitative easing program (dubbed QE) later this year and events in Asia have investors nervous about what the unpredictable leader in North Korea may do next.

The well-known Sir. John Templeton (from Franklin Templeton Funds) once said that "Bull markets are born on pessimism, grow on skepticism, mature on optimism and die on euphoria." The current bull market is now one of the longest in the post WWII period so it's only natural for investors to question how long it may last. Importantly, looking out over the next few quarters, we still do not see signs of a recession. Although some economic reports (like this week's weekly jobless claims which rose to a one year high) may come in below expectations over the next month or two due to Hurricane Harvey (and potentially Hurricane Irma), rebuilding activity over the next several months will likely add to economic growth over the next few quarters. At present, we believe the current economic expansion is likely to continue for some time.

Securities offered through HighTower Securities, LLC | Member FINRA / SIPC / MSRB HighTower Advisors, LLC is a SEC registered investment advisor.

Entering the Month of September

The month of September has historically been the weakest month of the year. Looking back over the past 50 years, the S & P 500 has generated an average decline of 0.85% in September and has produced positive returns just 36% of the time (source: Bespoke Research). In addition, it has been more than a year now since the market has experienced a pullback of 5% or more (which is something that typically occurs about every 7 months). However, other research is less worrisome. For example, according to research from Oppenheimer and Co., when we are in a bull market (like we are now) and the S & P 500 is above the 200-day moving average (which it is today), the S & P 500 has historically posted a modest increase during the month of September. Also, according to S & P Global, in years (like the current one) when the market advances 10% or more during the first six months of the year, equity markets typically go on and post additional gains during the second half of the year. The past is the past and looking forward is certainly more important.

Corporate Profits

We have said for some time that stock prices historically tend to follow the direction of corporate profits. Some have said that corporate profits are the mother's milk of stock prices. On that front, recent data has been encouraging. According to the latest data, profits for the S & P 500 increased double digits on a year over year basis during each of the past two quarters. For reference, this is the first time the index has generated two consecutive quarters of double digit year over year growth since the second half of 2011. Last quarter sales (i.e. revenues) for S & P 500 companies increased 5.1% year over year and 69% of companies beat revenue estimates. This marks the most leading companies beating revenue estimates in six years and came in above the 15 year average of 59% (source: Strategas Research).

Corporate profits are currently forecast to increase 9.4% for all of 2017 followed by an increase of 10.9% in 2018. For all of 2017, four out of 11 S & P 500 sectors are currently forecast to post double digit earnings growth with just one sector posting a year over year decline. For 2018, six out of 11 S & P 500 sectors are currently forecast to post double digit earnings growth with all 11 sectors currently forecast to generate positive earnings growth. Sales growth estimates for companies in the S & P 500 for 2017 and 2018 currently stand at 5.5% and 5% respectively (Data provider: Factset)

The Economy

On September 1, 2017, the economy added 156,000 jobs which was somewhat less than expected. There were also 41,000 in downward revisions to the prior two months. While several of the details came in a bit below expectations (for example leisure and hospitality and education and healthcare job growth both came in below trend), the economy generated 36,000 manufacturing jobs last month equaling the highest level in four years. Looking back, the economy has generated an average of 185,000 jobs per month over the past 3 months and an average of 175,000 per month over the past 12 months. Average hourly earnings (i.e. wages) continue to grow (as they have for much of the past several years) at a steady but somewhat disappointing rate of 2.5% on a year over year basis. As the job market continues to tighten, wages should start to rise but we have not seen that happen just yet.

As noted, on September, 1, the widely followed ISM manufacturing Index posted an upside surprise and rose to 58.8 versus 56.3 in July. This was the highest reading for the index since April, 2011. Improvement was driven by the production, employment and inventories sub-components within the report.

Securities offered through HighTower Securities, LLC | Member FINRA / SIPC / MSRB HighTower Advisors, LLC is a SEC registered investment advisor.

Production rose to 61.0 (+0.4 points) and the employment sub-index increased to 59.9 (+4.7 points), the highest reading since June, 2011. This is consistent with the solid manufacturing payrolls data reported by The Bureau of Labor Statistics (BLS) in the latest employment report. New orders were little changed at 60.3 but remain consistent with a solid pace of growth in manufacturing orders. One small negative is that inventory levels rose 5.5 points on a month over month basis to 55.5 representing the highest level since September, 2010 (when the index was 56.0). Higher inventory numbers indicate that inventory levels may be too high which is something to monitor in the months ahead. As a reminder, an ISM Manufacturing index reading above 50 indicates expansion while a reading below 50 indicates contraction.

Housing activity, which represents about 15% of the economy, has generally been in an uptrend over the past several years. While recent data has been somewhat uneven, housing starts, existing home sales, the Case-Shiller Home Price Index and the Wells Fargo - National Association of Home Builders Index (which measures the outlook for housing from the perspective of home builders) generally appear to be on healthy footing. The biggest concern we have is that a lack of available homes for sale has led to an above trend rise in home prices over the past several years. While good for home owners, if this trend were to continue, it might price new entrants out of the home market and lead to an eventual decline in demand.

Turning to the consumer, which represents about 69% of the economy, retail sales increased 4.3% last month on a year over year basis. For reference, this compares with a 3-year average growth rate of 3.0% and a 5-year average growth rate of 3.3%. While these numbers look pretty healthy, a lot of the credit goes to non-store retail sales (i.e. Internet sales) which increased 11% over the past 12 months. Total U.S. consumer spending (which is almost three times the size of retail sales) and includes spending on things like durable goods (which last an average of three years or more) and other items has increased at a rate of 4.2% over the past year compared with a 3-year average growth rate of 4.2% and a 5-year average growth rate of 3.8%. Overall, consumer spending appears fairly healthy. However, one caveat is that the consumer savings rate has recently declined from a 2015 high of 6.3% (of disposable income) to a recent low of 3.5%. Thus, without further wage gains, it appears unlikely that consumer spending is likely to improve from current levels.

We are aware of growing risks around the world and would not be surprised to see the markets tread water or experience a brief pull back in the weeks ahead. Since mid- summer there has been some weakness in small capitalization stocks, transportation stocks and various sectors within the market. However, we believe this weakness remains within the context of a bull market that likely has more room to run. It wouldn't surprise us to see the market advance in a stair step fashion over the next few quarters, meaning two steps forward and one step back.

One important economic index that we have highlighted in the past is the Conference Board's Leading Economic Index (LEI) – see chart below. As a reminder, the index is made of up of 10 sub-components and typically does a decent job forecasting the direction of the economy looking out over the next few quarters. Looking at the LEI today, there are no signs of a coming recession.

Securities offered through HighTower Securities, LLC | Member FINRA / SIPC / MSRB HighTower Advisors, LLC is a SEC registered investment advisor.

some time that interest rates are likely in a multi-year bottoming process that will ultimately start to reverse the more than 30-year decline in interest rates that has been in place since 1980. With the unemployment rate at multi-decade lows, the ISM manufacturing Index at multi-year highs, the global economy on stronger footing and central banks like the Federal Reserve Bank starting to reduce the size of its balance sheet, the level of interest rates seems inappropriately low to us. Once we get past the next several weeks (i.e. North Korea, Hurricane Harvey and Irma and events in Washington etc…) we believe that interest rates should start to move higher again reflecting a relatively healthy underlying U.S. and global economy.

SUMMARY

In summary, while this has been one of the longest economic expansions in the post WWII period, there are currently no signs that the expansion is about to end. Consumer and business confidence levels are currently at multi-year highs, consumer spending levels look fairly steady, corporate profits are rising at a healthy rate and credit spreads remain positive. Last month the widely watched ISM Manufacturing Index rose to a six-year high which appears to be a positive sign for the country's manufacturing sector.

We remain constructive in our outlook but aware that there may be bumps along the way. While GDP grew at a rate of 3% last quarter (above the average rate of 2.1% during the current economic expansion), we expect the economy to continue to grow at a more moderate rate in the quarters ahead. A big wild card over the next 6-12 months is the potential for new tax legislation out of Washington. If the Trump administration can pass a tax reform package, this could generate a boost for the economy and corporate profits, likely starting in 2018. Right now the odds of this happening appear mixed but are still a real possibility and something that most investors are not currently expecting at this moment.

In terms of near term risks, the month of September has historically been one of the weaker months for the markets but at least for now the S & P 500 remains above its 200-day moving average which is a positive technical sign for the market. Recent events in North Korea are a clear reminder that the world can be an uncertain place at times. Valuation levels also remain above their historical levels which means that corporate profits will have to continue rising to help support equity prices. Lastly, events in Washington are also on our mind near term with Congress needing to pass a budget for 2018 and deal with the debt ceiling fairly soon.

Respectfully,

Michael Sheldon, CFA
Executive Director & CIO

Ronald D. Weiner, CFP®
Managing Director & Partner

Description

S&P 500 - The S&P 500 is a stock market index that tracks the 500 most widely held stocks on the New York Stock Exchange or NASDAQ.

Securities offered through HighTower Securities, LLC | Member FINRA / SIPC / MSRB HighTower Advisors, LLC is a SEC registered investment advisor.