Beacon Trust
INNOVATING WEALTH STRATEGY

Market Outlook 2Q 2017 Review July 11, 2017

Second Quarter Summary

The bull market in equities, which began in March of 2009, continues to roll along with stocks turning in yet another positive quarter. The S&P 500 tacked on a 3.09% gain in the second quarter, bringing its first half advance to a solid 9.34%. Technology stocks were again among the leaders, both in performance and news. Amazon.com shocked the retail industry with its proposed takeover of Whole Foods, moving it into the grocery business in a big way. Apple, the most valuable company in the world by market capitalization, celebrated the 10th anniversary of its groundbreaking iPhone. Bonds, as represented by the Barclays Aggregate Index, continued to move up, rising 1.45% in the second quarter as political gridlock in Washington D.C. raised fears among investors about the likelihood of near term economic stimulus. The Federal Reserve raised short-term interest rates again, its second 0.25% increase in 2017, at its June Federal Open Market Committee (FOMC) Meeting. The Fed also provided some guidance on how it plans to shrink its enormous $4.5 trillion balance sheet. “Slow but steady” is probably the best characterization of its plans, and the market shrugged off the news, keeping the bull market intact.

Market Outlook

Our market outlook for equities for the remainder of 2017 is positive, but we expect more muted returns in the second half as well as increased volatility, relative to the exceptionally smooth sailing experienced thus far. The economy appears to be in relatively good shape, with unemployment (4.3%) at its lowest levels in more than a decade. GDP is moving along at an unspectacular pace of roughly 2% per year, before any stimulus, such as tax relief or infrastructure spending, has been implemented. Consumer confidence remains strong and real estate prices, as represented by the S&P Case-Shiller National Index, have surpassed levels achieved prior to the Great Recession.

Although Technology stocks exhibited the strongest performance during the first half of the year, some changes may be afoot. As the second quarter came to a close there seemed to be a rotation away from Technology stocks and towards Financials and Healthcare stocks. The latter two sectors are in positive territory year to date, but have lagged their higher profile peers, especially the FANG stocks (Facebook, Amazon, Netflix, and Google), as well as other market darlings, Apple and Tesla. Financial stocks appear to be getting a boost from Fed policy, since their profit margins generally increase as short-term rates increase. Investors in Healthcare stocks seem to be seeing some light at the end of the tunnel as the new administration’s healthcare policy takes shape. But one month does not make a trend so we will closely be watching sector rotation developments as a sign for the next group of market leaders.

We believe bonds are likely to be range bound for the remainder of 2017, despite the Fed raising short-term rates again in June. In our view, the benchmark 10-Year Treasury Note, currently at 2.30%, is likely to stay within a band of 2.0% - 2.75%. We trimmed our earlier ceiling estimate for the 10-Year Treasury from 3.0% to 2.75% since it seems like meaningful economic stimulus will not be enacted this year.

As always, there are macroeconomic risks that loom on the horizon. Perhaps the most serious threat is the continued nuclear and intercontinental ballistic missile tests being conducted by North Korea. Although North Korea poses little current danger to the United States, it may inflict significant damage on South Korea and Japan, two very important countries in the global technology chain. Furthermore, tensions in North Korea offer the potential to disrupt U.S.-China relations, which appear trending in a positive direction after some tough campaign talk by the Trump Administration.

Speaking of President Trump, we occasionally receive questions from concerned clients about the impact of a potential impeachment on the financial markets. We will sidestep the question of the merits of a potential impeachment and focus on the implications. First, only two sitting Presidents (Andrew Johnson and Bill Clinton) have been impeached by the House of Representatives, where a 50% majority vote is needed. Neither President

Johnson, nor Clinton were impeached in the Senate where a 2/3 majority vote of the Senate is required. Although the findings of Special Counsel Mueller have not been revealed, based on history, an impeachment is unlikely. In the event of an impeachment, Vice President Pence would be elevated to the Presidency. Although there may be an initial selloff due to fear of the unknown, we believe ultimately the market would recover its losses, if not trade higher. A Pence Presidency would likely have a similar economic agenda to the current one and be perceived as more stable. In short, we don't have great concern about impeachment risk. Rather, we would move to a sluggish or cautious outlook from our current somewhat optimistic outlook if much of the proposed stimulus is permanently sidetracked or shuttled.

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