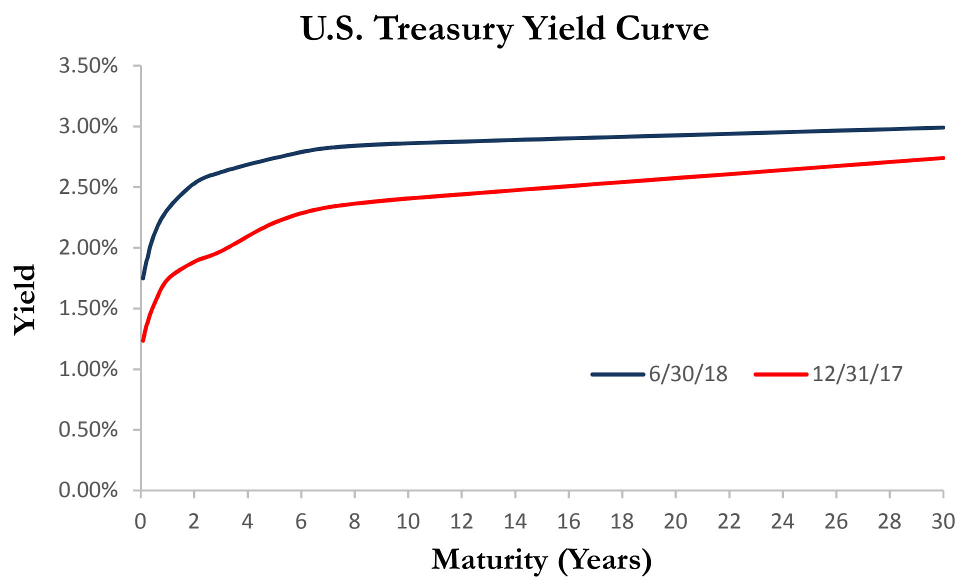
Economic and Capital Markets Commentary

The Flattening Yield Curve…

The yield curve is a graph showing the interest earned on short-, intermediate-, and long-term U.S. Government debt. Historically, the farther one moves out on the curve (the maturity date) the higher the yield (the interest earned). Beginning in the 1970s, each time the yield curve 'inverted' (short-term yields exceeded longer-term yields) the economy went into recession within one to two years. As a result, investors have monitored the yield curve closely.



While not currently inverted, the curve is flattening, putting some Wall Street analysts on alert. At the short-end of the curve, the two-year yield is rising, in-line with Federal Reserve policy. In June, the Fed raised the Federal Funds rate another 0.25%, to 2.0%, and the Fed has indicated two more such moves in 2018 and three potential increases in 2019.

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While the Fed has expressed confidence in the nine-year U.S. economic expansion, it does not want inflation to significantly overshoot its 2% target, hence a slightly accelerated schedule of rate hikes compared to prior Fed guidance.

While the two-year yield has increased, the yield on the ten-year Treasury has declined after hitting a nearly seven-year high in May, reducing the yield spread between these two bonds and flattening the curve. The current administration in Washington is using tariffs and the threat of tariffs to try to negotiate more favorable terms with many of our trading partners. This approach, however, has raised the threat of an all-out trade war and created the general perception that there is a real risk to the current worldwide economic expansion. During times of heightened risk, global investors often seek the safety of U.S. Treasuries, which may explain the recent decline in the ten-year yield (bond prices and yields are inverse; demand pushes prices up and yields down).

Despite the flattening curve, U.S. economic growth is solid – unemployment is low, consumer confidence is high, corporate earnings are strong – and expectations are for continued GDP growth driven by tax cuts and consumer spending. Few economists anticipate a slowdown in the near-term and some believe that years of central bank intervention in global bond markets have reduced the usefulness of the yield curve as a predictive tool.

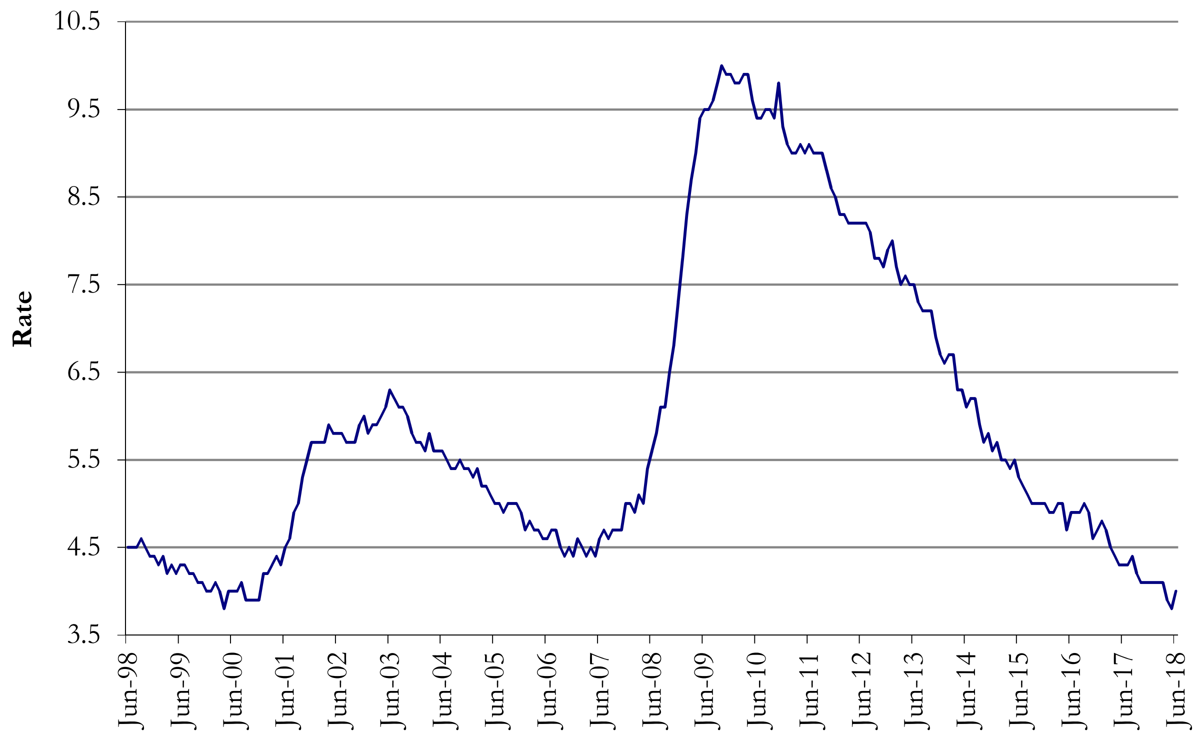
Whether the stock market rally, now ten years old, can continue is a separate question. Expectations of continued strong growth are largely built into stocks prices and we expect the increased volatility seen in the first half of 2018 to continue. Therefore, we believe it is useful to review account goals and objectives and begin to plan for a time when the economy and the stock market are less robust.

Economic and Capital Markets Data

	June 30, 2018	June 30, 2017	June 30, 2013
S&P 500 Index	2718	2423	1606
Price/Earnings Ratio	20.7x	20.9x	15.8x
Yield	1.93%	1.97%	2.14%
Federal Funds Rate	2.00%	1.25%	0.25%
10 Year U.S. Treasury Yield	2.86%	2.31%	2.49%
Gold	1253	1242	1235
Oil (Brent)	79	48	102
GDP (Annualized)	4.1%	3.1%	0.8%
Unemployment	4.0%	4.3%	7.5%
Inflation (Annualized)	2.9%	1.6%	1.8%

U.S. Unemployment Rate

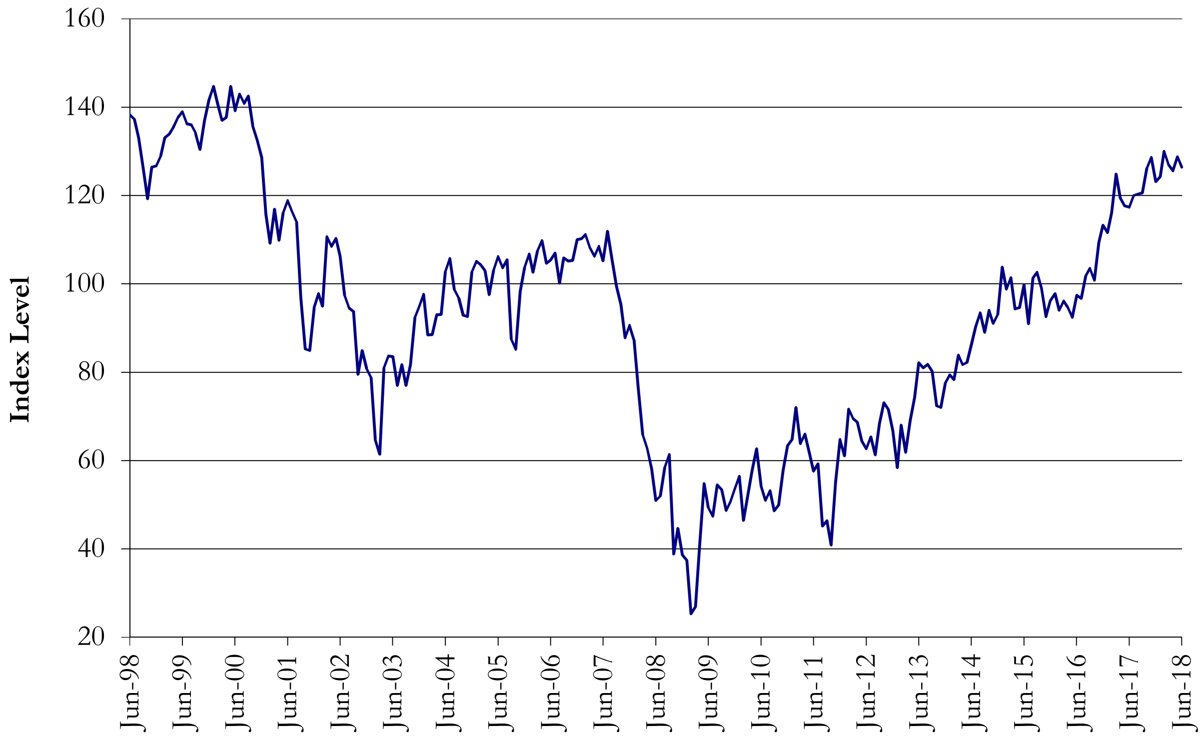
Twenty Years



Courtesy of Bloomberg

Consumer Confidence Index

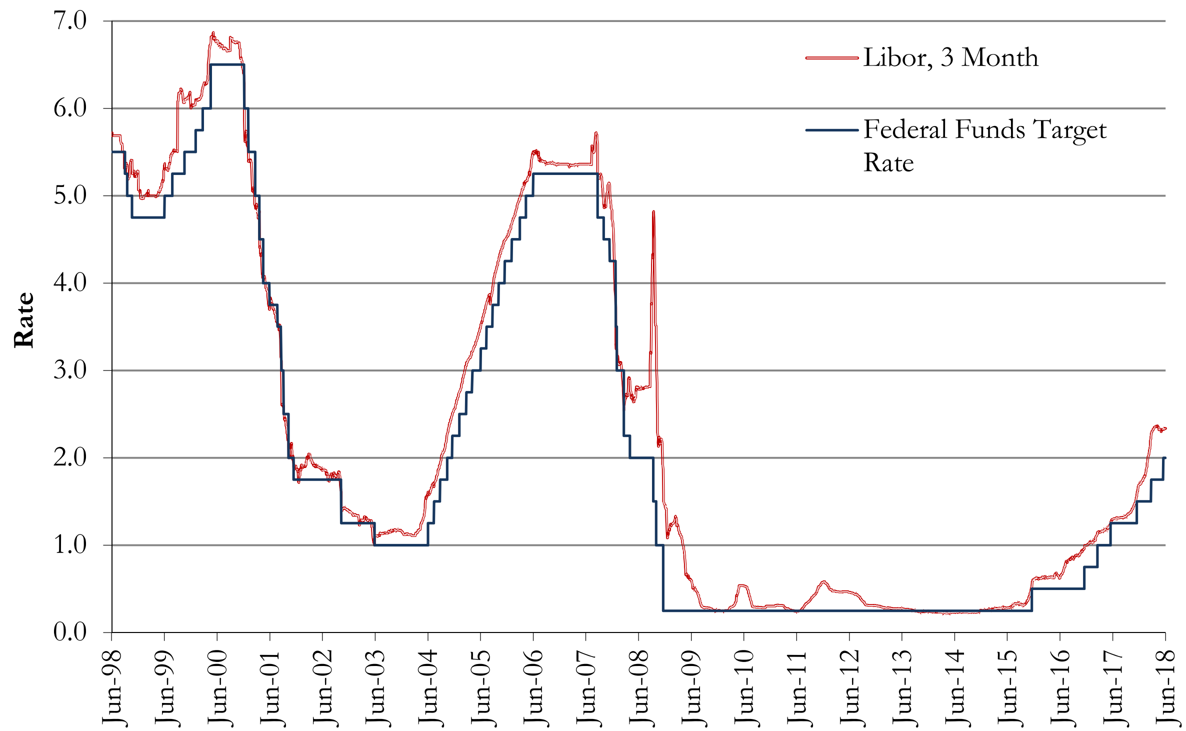
Twenty Years



Courtesy of Bloomberg

Federal Funds Target Rate & Libor USD Index

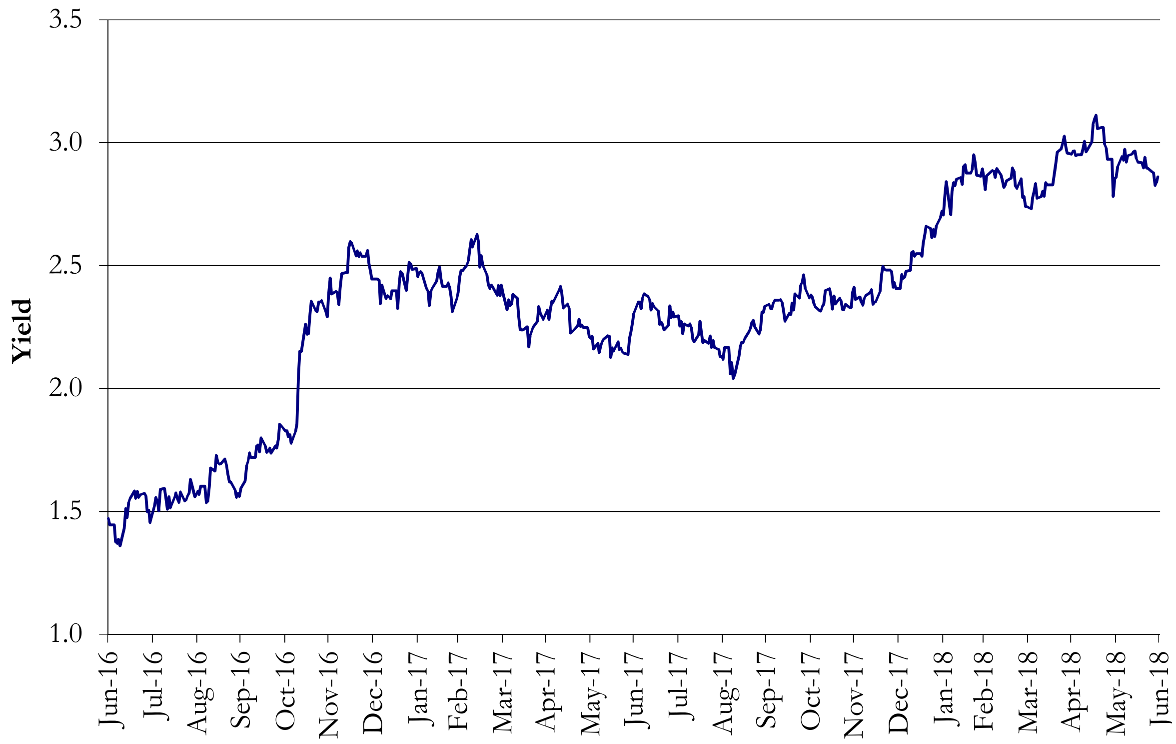
Twenty Years



Courtesy of Bloomberg

U.S. Treasury Ten Year Bond Yield

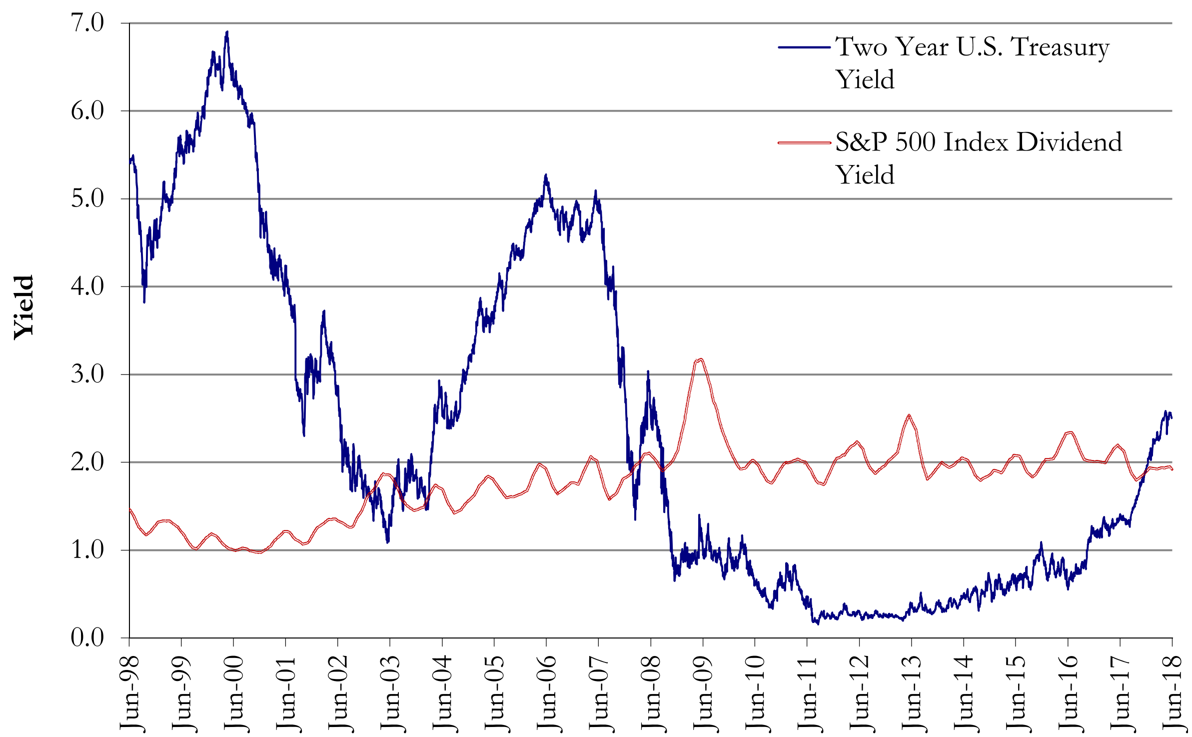
Two Years



Courtesy of Bloomberg

S&P 500 Index Dividend Yield & U.S. Treasury Two Year Bond Yield

Twenty Years



Courtesy of Bloomberg

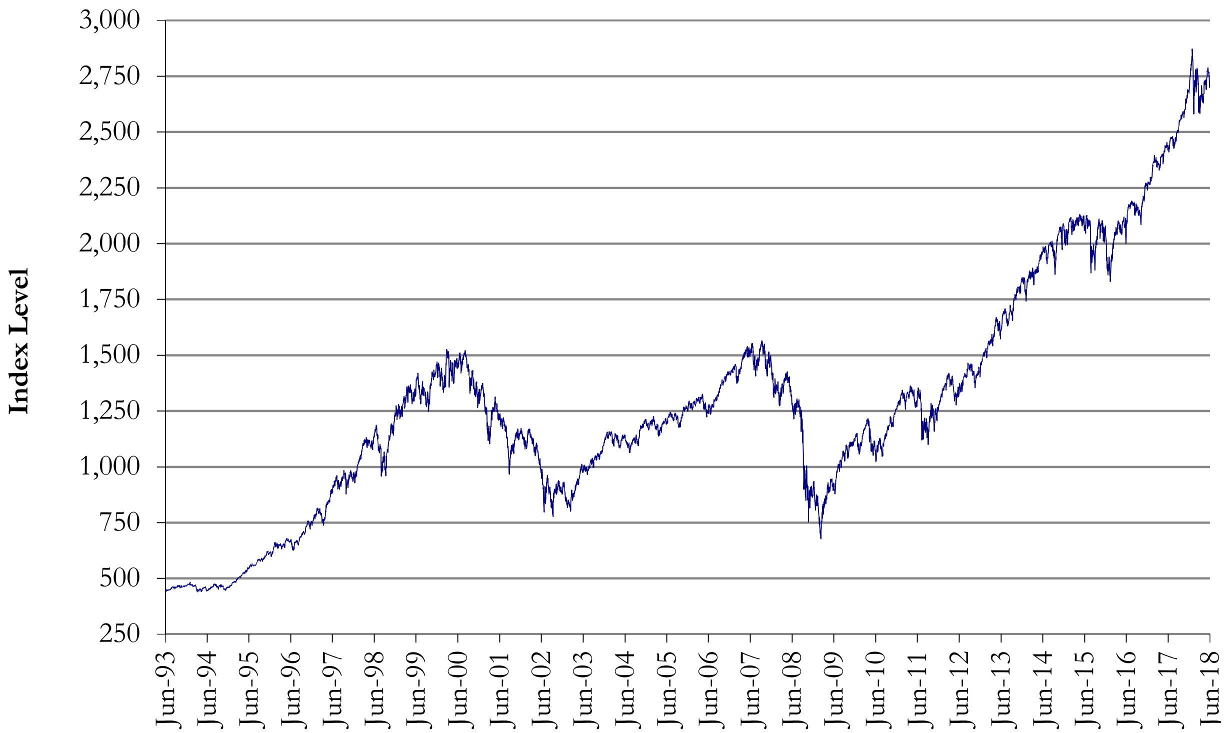
Standard & Poor's 500 Index

Five Years

Courtesy of Bloomberg

Standard & Poor's 500 Index

Twenty Five Years



Courtesy of Bloomberg