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In last quarter's review, we wrote that we had already met, or exceeded, return expectations for the full year and that we were surprised by the lack of volatility with which those returns were achieved. We're happy to reiterate those comments in recounting Q3, yet perhaps this time, with less surprise. The theme we saw emerging in Q2 was the transition from irrational exuberance surrounding the election and purported pro-growth fiscal policies, to solid corporate earnings and fundamentals, as the main driver of market returns. If one thing was made abundantly clear in the last quarter, it's that this theme is no longer nascent; rather it is growing on the strength of corporate fundamentals.

Globally, growth is trending at above-average levels, which has provided a positive backdrop for corporate earnings. Earnings are growing at a greater than 10% rate in all the major international regions, the fastest such pace since 2005. In both developed and emerging markets, a strengthening and widening of not only the economic recovery, but now its expansion, has infused a sense of optimism in the economy and markets. Global growth in the first half of 2017 averaged 3.5%, while the US churned out just over 2%, backed by robust consumer spending, business investment and housing strength.

Domestically, economic indicators continue to communicate growth. The core measure of durable goods orders was up 6.1%, year-over-year and the ISM's manufacturing PMI Index, a measure of the health of that sector, registered 60.8 in September, the highest reading since 2004; this represents the 13th straight month of growth for the manufacturing sector and the 100th consecutive month of overall economic expansion, per the index. Similarly, the ISM's services-industries index hit a record of 59.8, a level not seen since 2005 (readings above 50 indicate sector expansion, below 50 indicate contraction). These across-the-board gains should support further corporate earnings accretion, providing justification for current market valuation levels and reinforcing the case for equities, going forward.

Given the preponderance of positive economic indicators, the Fed has continued its campaign of tightening, not only signaling that further rate hikes are expected, but also taking steps to reduce the size of its massive balance sheet, thus reducing liquidity in the market. The US economic dynamic favors further labor market tightening and gradual upward pressure on wages, supporting the Fed's stance. We will most likely see one more rate move in 2017 and then two or three in 2018. Economic outperformance in the US and other G7 nations is eliminating excess capacity at a faster than anticipated rate, and though wages have yet to reflect any significant upward pressure, it is only a matter of time, in this current mature economic cycle. Once companies begin to vie for scarcer skilled labor, wages should rise, crimping profit margins and engendering a durable escalation in consumer prices. While core inflation in the Eurozone is expected to remain subdued for a longer period than in the US, it is clear that highly accommodative monetary policy has done its job in sowing the seeds for self-sustaining growth

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across a number of regions. Therefore, the impending rise in interest rates can be viewed as confirmation that the current expansionary cycle has more room to run.

Looking ahead, we continue to hold a domestic equity bias amid the “Steady-Eddie” growth picture in the US, in spite of the prospect for rising rates and diminishing of accommodative monetary policy. We expect persistence of loose central bank positioning and more robust growth numbers in the Eurozone and Japan, creating an attractive case to invest internationally. Similarly, emerging economies appear poised for gains, as stronger global demand should support economic activity more broadly across those markets, while valuations are still quite reasonable. As a result, we have increased our allocation to global equities to the mid-teens as a percentage of our overall portfolios.

On the fixed income side, today’s valuations and credit spread levels imply that the majority of future returns will come from coupon returns, rather than price appreciation. Therefore, on the whole we see more upside in equities with the global growth picture being bright, however, we will continue to allocate a portion of the portfolio for income purposes and their stabilizing effect on our portfolios.

Our outlook for the fourth quarter is unchanged, as we expect to remain robustly positive, through year-end. The solid economic growth and corporate earnings discussed, should allow the bull market to continue, but that isn’t to say we might not experience bouts of volatility or pullbacks. Nonetheless, staying diversified and disciplined around our long-term objectives is paramount.

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