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What to Watch in Q4

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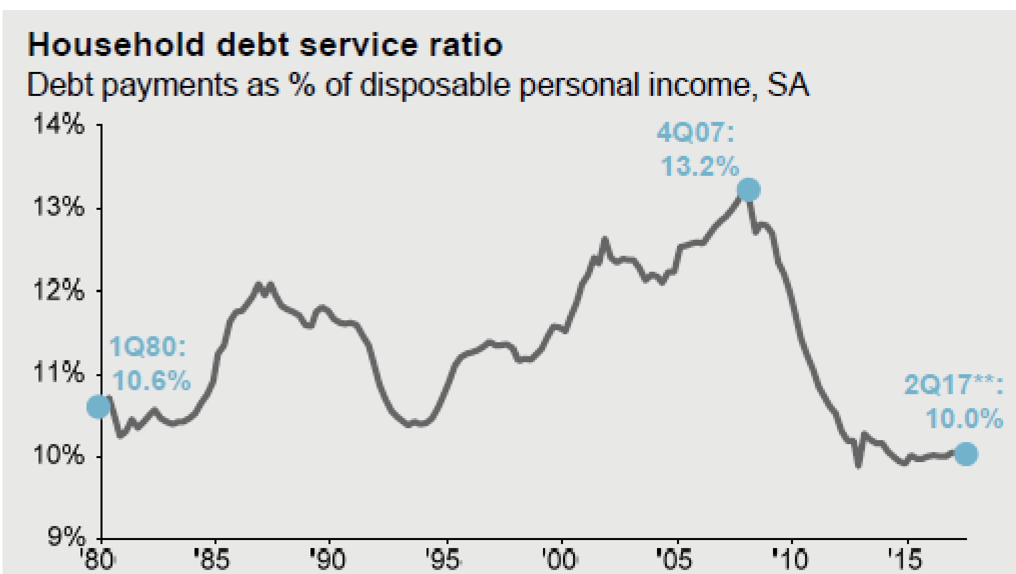
We've officially closed out the third quarter of 2017 and entered the final three months of the year. In the past few weeks, there's been no shortage of news ranging from geopolitical tensions to natural disasters.

We remain optimistic about the economy and opportunities in the fourth quarter of 2017. Here are a few things we're keeping an eye on:

1. **Market movement:** Some have called this the "most hated" bull market in history. Much of this talk has come from investors who have held on to cash for several years in anxious anticipation of the next bear market, which has not yet come to fruition.

We would note that one reason this cycle has been so long-lasting is because we have not seen an overextension on spending and investing from consumers or businesses. During many previous recoveries, businesses and households became overextended and those excesses spurred a correction. Today, we are instead reminded how much cash businesses have on hand and how consumers' debt payments are as low a percentage of their disposable income as they have been in decades (see chart below).



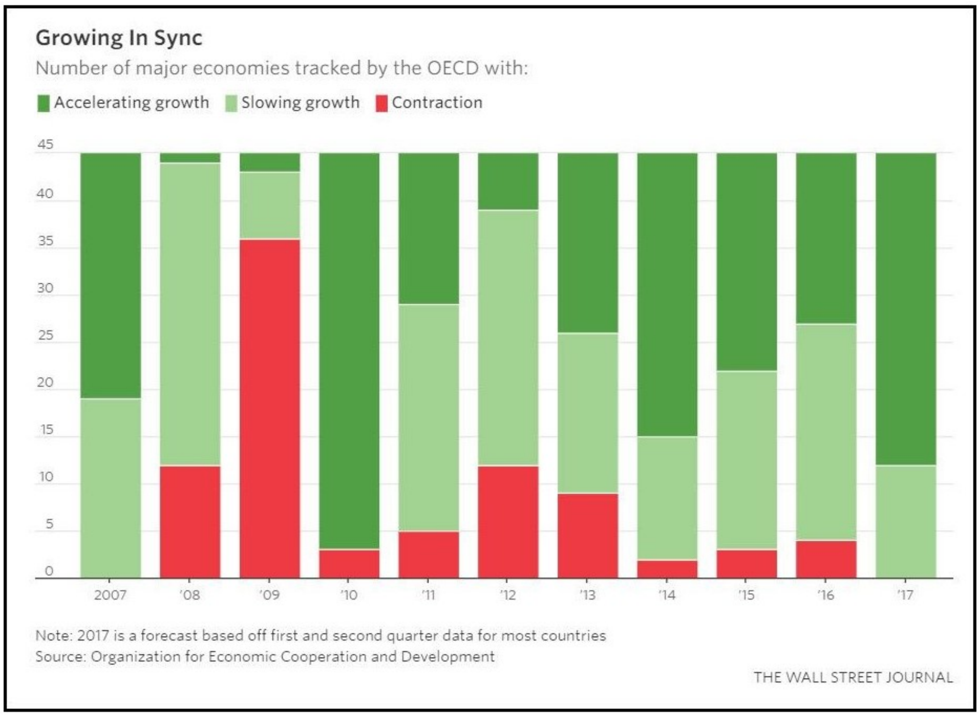
Source: "Guide to the Markets: Consumer Finances" J.P. Morgan Asset Management

Another thing we've noticed is that following two 50 percent corrections – The Dotcom Crash and the

2008 Financial Crisis – investors and commentators seem to be conditioned to expect 50 percent drops every seven or eight years. However, declines of this magnitude are rare. There have been only five of these over the last 100 years, with two occurring during The Great Depression and the other two mentioned above since 2000.

While it's certainly possible for us to have another 50 percent correction in the near future, it is much more likely that when the market does correct next it will be of the common variety in the 10 to 20 percent range.

2. **Global growth**: Recent data shows strengthening international economic numbers. As illustrated in the chart below, all 45 countries tracked by the Organization for Economic Cooperation and Development (OECD) are in a rare period of expansion. The world's largest economies are growing synchronously for the first time since 2007.



Source: The Wall Street Journal

This growth should help support markets. Over the last several years, global growth has been disjointed, where one country's economy accelerates and another falls into a recession. Now, every major economy is accelerating, with especially optimistic numbers coming from Europe and emerging markets like China. This trend, along with the recent rally in commodities, seems to confirm that the global economy and trade are strengthening. We expect a diversified portfolio with domestic and international exposure will be positioned well to take advantage of this growth.

3. **Interest rates**: At the latest Federal Open Market Committee (FOMC) meeting on September 20, the Federal Reserve announced it will leave interest rates unchanged for now and begin to unwind its $4.5 trillion balance sheet in October.

   We'll be closely watching to see if U.S. growth is strong enough to merit one more rate increase from the central bank before the end of the year. Nonetheless, we don't think rising interest rates from these lows will be a near-term issue for the equity market. We believe the market's current earnings yield of about 4.9 percent (*Morningstar*) will look relatively attractive until bonds' 2.5 percent yields move higher, closer to 4 percent, which may take some time.

We'll be closely monitoring these three key areas – market movement, global growth and rising interest rates – in the final quarter of 2017 and will report back on what we are seeing.

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