ROUND TABLE
WEALTH MANAGEMENT

QUARTERLY REVIEW – SECOND QUARTER 2017

Is Goldilocks back in town? During the previous economic cycle (2003-2007), Wall Street referred to the U.S. economy as the "Goldilocks Economy" …not too hot, not too cold, just right. It was also during this time that market risk metrics, such as volatility, were low. Presently, investors find themselves in an analogous situation, as today's economy continues to demonstrate modest growth and risk metrics are reaching historical lows. On the positive side, capital markets continue to grind higher in both equities and fixed income asset classes; on the negative side, many are asking when the bears are expected to be home.

No one knows when or how the next market downturn will occur, but we feel confident that the ebbs and flows of the business cycle remain intact. Whether the market pauses for an extended period of time or if a downturn occurs, investors can prepare through diversification, by holding high quality assets and making modest tactical allocation shifts to preserve capital. We are not advocating wholesale changes to portfolios at this time, however, we are evaluating allocation shifts should a sense of a drawn-out market downturn solidify. As always, we welcome an active dialogue with you to discuss our firm's view.

Annualized Benchmark Returns through June 2017*

	1 Quarter	1 Year	2 Years	3 Years	5 Years	10 Years
S&P 500	3.1%	17.9%	10.7%	9.6%	14.6%	7.2%
Russell 2000	2.5%	24.6%	7.8%	7.4%	13.7%	6.9%
MSCI World Ex. US Index	5.9%	20.1%	4.3%	1.2%	8.7%	1.5%
MSCI Emerging Markets	6.4%	24.2%	4.7%	1.4%	4.3%	2.2%
Bloomberg Barclays U.S. Aggregate	1.4%	-0.3%	2.8%	2.5%	2.2%	4.5%
Bloomberg Barclays Municipal Bond	2.0%	-0.5%	3.5%	3.3%	3.3%	4.6%
Bloomberg Barclays U.S. High Yield	2.2%	12.7%	7.0%	4.5%	6.9%	7.7%
FTSE Nareit All REITs	2.4%	1.4%	11.5%	8.9%	10.0%	6.0%
Alerian MLP	-6.4%	0.4%	-6.6%	-11.2%	1.8%	5.7%

*Source: Bloomberg   *Quarter return is not annualized.*

The Big Picture

The U.S. economy grew at 1.4% in the first quarter and inflation remains relatively tame. In prior economic cycles, most economists would consider the economy's rate of growth "stall speed", meaning economic recession is looming. Today's GDP growth rate is seemingly acceptable as the number of calls for a U.S. recession over the next twelve months is low. As economists reflect on second quarter GDP, expectations are for U.S. growth to increase at a 2.7% rate or more. Somewhat consistent with this view is the fact that the Federal Reserve raised its Fed Funds Target rate by 25 basis points (bps) to a range of 1% to 1.25%, suggesting a relatively positive outlook on the U.S. economy. The Federal Reserve has also begun discussing its thoughts on reducing its $4.5 trillion balance sheet of fixed income instruments built up through its Quantitative Easing program. It seems reasonable the Fed would not be reducing its balance sheet if it believed the U.S. economy was weak.

The benign economic outlook leaves most investors having a love/hate relationship with today's market: They love the generous returns earned year-to-date, but hate the valuations they must endure. On a positive note, U.S. corporate earnings appear to be stable and are expected to increase 9.8% in 2017. Over the course of most years, S&P earnings expectations usually decline as actual results fail to keep up, but this has not been the case in 2017 and is likely a key reason investors continue allocating to equities.

European economies continue to grow. The European Central Bank is projecting economic growth of 1.9% for the Euro region in 2017. Underpinning this growth is an accommodative ECB and stronger global demand for European products. The Euro currency has rebounded since the election of Macron in France, who defeated nationalist Le Pen. The latter was considered a key risk to the survival of the Euro common currency. Favorable economic and corporate fundamentals combined with a reduction in European political risk has drawn in investors to the region. More recently the ECB has hinted at curbing its quantitative easing program, which has led to increased bond yields and volatility in European markets.

Summary of Allocation Recommendations

Asset Class	**Recommendation**	**Comment**	**Asset Class Summary Link**
U.S. Large Cap	Neutral/Underweight	Earnings remain strong but indices reaching target levels, remain vigilant of valuations	*U.S. Large Cap Review*
U.S. Small & Mid Cap	Neutral/Underweight	Premium valuation with high prospective growth, domestic focus, M&A activity looks promising	*U.S. Small Cap Review*
Non-U.S. Developed	Overweight	Attractive relative valuations and improving macro and corporate fundamentals	*International Equity Review*
Emerging Markets	Neutral	EM currency concerns and commodity risks, attractive valuations	*International Equity Review*
Fixed Income	Neutral	Maintain safe haven assets for volatility and floating rate loans to alleviate interest rate risk, shorter duration given flat yield curve	*Fixed Income Market Review*
Tactical	Neutral	Master limited partnerships, financials, pharmaceuticals,	*Tactical Investments Review*
Alternative	Hedge Funds & Private Equity	For appropriate allocations	Contact your Wealth Advisor

The Outlook

We continue to recommend a neutral/underweight allocation to U.S. Large Cap Equites as upside is likely modest in the near-term. The S&P is currently trading around 22x trailing twelve-month (TTM) earnings, which remains a significant premium over historical valuations. In addition, the S&P is trading at price levels near or equal to year-end targets projected by leading market strategists, suggesting limited upside through yearend. This dynamic might encourage investors to sell and reallocate to other investments, however, we remind ourselves that long-term capital gains taxes (or worse, short-term capital gain taxes) produce a permanent loss of capital. A modest return through year end is much better than a tax bill reducing profits by 20%.

We reduced our allocation to small and midcap equities from overweight to neutral/underweight. Valuations remain elevated on the promise of higher earnings growth. Small cap companies have increased their level of net debt on balance sheets, increasing fundamental risk in a potentially lower earnings growth environment combined with higher interest rates.

We raised our recommended allocation to non-US developed markets to overweight. This builds on the increase in exposure we advocated for at the end of the first quarter. Valuations in developed markets remain at large discounts to U.S. equities against a backdrop of improving European corporate earnings. We suspect a higher level of volatility in European shares as the European Central Bank has alluded to tempering its asset purchase program. Recent news on this development sent German Bund yields higher and equity shares modestly lower.

We are recommending a neutral allocation to emerging markets. The asset class had mixed performance across regions in the second quarter as commodity producers sold off in the wake of an oil price decline. Year-to-date the broad emerging market index has performed well but we remain wary of lurking risks. We note that realized volatility in the emerging market asset class is historically low, which raises concerns around a potential repricing of risk in the asset class vis-a-vis declining share prices. Foreign currency translation contributed less to returns this quarter as compared to the first quarter and may prove less beneficial moving forward.

We continue to recommend a neutral allocation to fixed income. The Federal Reserve increased its Fed Funds Rate to 1.0% in June, an increase of 0.25%. Corporate bond yields of varying credit quality provide modest incremental income over comparable U.S. Treasuries. A key risk is a widening of credit spreads should investor appetites increase for risk free U.S. government bonds as the Federal Reserve raises its Target Rate. Currently the U.S. Treasury yield curve, a plot of interest rates at increasing maturities, is relatively flat and suggests extending bond portfolio duration provides diminishing yield enhancement. As such, we recommend that marginal allocations to fixed income include shorter duration exposure.

Our recommendation toward tactical exposure includes master limited partnerships (MLPs) and specific sector ETFs. MLPs underperformed in the first half of 2017 and were highly correlated to the price of oil. Within the Alerian MLP Index, on average, MLPs are anticipated to increase distributions by 5.1% in 2017. The Index's current yield is approximately 7.0%, making it a reasonable source of income. Our financial sector tactical investment gained this quarter, supported by two developments. The first being the passage of the CHOICE Act by the House of Representatives (which sought to undo parts of Dodd-Frank) and the second by the release of favorable bank stress tests that are expected to lead to higher dividend payouts and share repurchases. In the case of the former, while the U.S. Senate is not likely to approve the CHOICE Act, its passage by the lower house suggests financial reform remains a top-of-mind issue for the Trump administration.

Tax and Financial Planning News

As we approach the slower-paced days of summer, it is an ideal time to review your current beneficiary designations. Given the fast-paced lifestyle we have become accustomed to, it may have been some time since you've revisited your beneficiary designations and how they fit into your current overall estate plan. There may have been a recent marriage, divorce, death, or a new addition to the family that may require an update to these beneficiary designations.

Upon death, assets are passed to survivors in three ways; 1) beneficiary designation (i.e., IRA's or insurance policies), 2) by operation of law (i.e., joint ownership), and 3) at the direction of your estate documents—wills and/or Revocable Trusts. Be sure to consider your estate plan currently in place and whether it still meets your testamentary wishes.

For additional information on this please see our recent blog post here or contact your Wealth Advisor.

Firm News

Bruce Hyde, a Partner and Chief Compliance Officer at Round Table, celebrated his fifth anniversary with the Firm.

Please join us in congratulating Eric Thompson for passing the Certified Financial Planning examination!

Respectfully submitted,
Round Table Wealth Management