Investment Tally & Perspective

Second Quarter 2017 Review

Market Activity

Equities – Stocks did well domestically and globally in the second quarter with the S&P 500 index total return exceeding 3%, while stocks outside the U.S. did even better. For U.S. equities, small cap stocks lagged large cap, and growth continued to outperform value.

One recent development to note is growth's underperformance in June - the total return for the S&P 500 growth index was -0.4% while the value counterpart returned +1.9%. This was driven by declines in technology shares which had gained over 20% through the month of May and then declined 2.7% in June. Below illustrates the reversal of performance. We are uncertain how these issues will perform in the near-term.

Total Return In 2017

	Netflix	Apple	Alphabet	Facebook	Amazon
December - May	31.7%	33.0%	24.6%	31.6%	32.6%
May - June	-8.4%	-5.7%	-5.8%	-0.3%	-2.7%

Source: Thomson Reuters

Fixed Income - Bonds did well in the second quarter, with all major investment grade classes posting gains aside from TIPs, which were subject to falling inflation expectations.

Other Assets - Returns for this asset class were a mixed bag. REITs had a positive quarter after declining in the first quarter, benefiting from declining interest rates. Oil was again a laggard, as U.S. production and rig counts increased, stoking fears of oversupply.

Economic Developments

Global GDP - All major economies are expected to expand in 2017 (IMF), including those that had recently been mired in country specific predicaments like Brazil and Russia. Global GDP growth is expected to hit 3.5% this year, up from 3.1% last year (all figures in real terms).

U.S. Inflation - The latest reading of inflation, adjusted for food and energy (core CPI) showed year on year growth of 1.7%. In general, while inflation continues to underwhelm, the Federal Open Market Committee expects the recent softness to be temporary (many market participants disagree).

Business Spending - U.S. business spending was a strong contributor to Q1 GDP with non-residential equipment fixed investment growing 7.8%, estimates for Q2 suggest a 4.9% increase. Non-defense capital goods orders excluding aircraft (a proxy for capital expenditures) is continuing to strengthen, up 5.5% in May from a year earlier.

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MAJOR ASSET CLASS RETURNS	2nd Qtr. 2017	1 Year	3 Year	5 Year
Equities				
S&P 500	3.09%	17.90%	9.61%	14.63%
MSCI EAFE	6.12%	20.27%	1.15%	8.69%
MSCI Emerging Markets	6.27%	23.75%	1.07%	3.96%
Fixed Income				
Bloomberg Barclays US Aggregate Index	1.45%	-0.31%	2.48%	2.21%
Bloomberg Barclays US Credit	2.35%	1.84%	3.40%	3.68%
Bloomberg Barclays Global Aggregate Bond Ex-US	3.55%	-3.80%	-2.42%	-0.36%
Bloomberg Barclays Municipal Bond	1.96%	-0.49%	3.33%	3.26%
Other Assets				
Dow Jones Select REIT Index	1.64%	-2.43%	8.04%	9.00%
Thomson Reuters Commodity Index	-2.92%	7.27%	-7.88%	-2.83%
Oil	-9.01%	-4.74%	-24.12%	-11.53%
Gold	-0.53%	-5.89%	-2.09%	-5.00%

Source: Thomson Reuters — All returns greater than one year are annualized

Economic Summary- The world economy continues to strengthen in a broad fashion. In the U.S., the labor market, consumer spending, and business investment are signaling strength; the odd man out is inflation which raises our suspicion that price pressures may once again surprise on the upside though timing is uncertain.

Monetary Policy

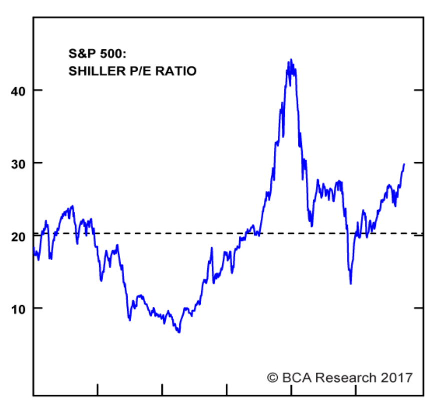
Changes at central banks were the largest "new news" this quarter. At the Fed's June meeting, the Federal Open Market Committee voted to boost the federal funds target rate to 1.00% to 1.25%, its fourth increase of this economic expansion. The Fed also guided to another increase this year and laid out plans to gradually let its balance sheet wind down. Statements and rumblings of pulling back on stimulative policies emanated from all corners of the globe, including Europe, Canada, and the U.K. This drove a rally in bond yields, witnessed primarily at the end of June.

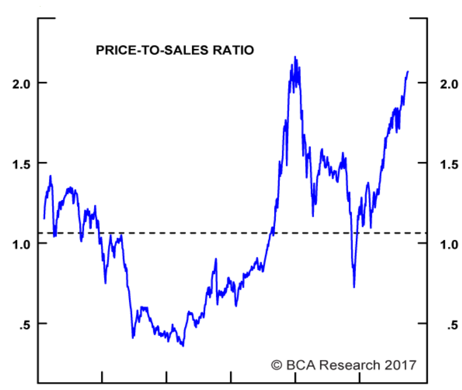
Monetary Policy Summary- We expect the Fed to continue to tighten, even in the face of lackluster inflation readings. Globally, there appears to be a simultaneous shift to a tightening stance. We will be watching this trend closely, as it could have real consequences to global economies and markets.

Asset Valuation

There is no significant change in asset valuations from the first quarter. Stocks continue to be modestly expensive on most metrics. An overview of popular valuation metrics can be seen below (Source: BCA Research). Credit spreads continue to test the lows made during this economic expansion, creating easy financial conditions and a poor risk/reward to take on credit risk.

Valuation Summary- On a historical basis, equities are rich in the U.S. From the fixed income side, real and nominal interest rates are low, credit spreads are tight, and term premium (compensation for owning longer-term bonds) is negligible.





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Investor Sentiment

Survey based measures of sentiment are not showing exuberant bullishness, nor are cash levels at mutual funds. However, the ease with which we have overcome recent events is remarkable. This quarter we saw:

- *Tensions in Syria Continue* - The U.S. dropped bombs in Syria for the first time and, more recently, has been shooting down regime planes and drones, complicating relations with Russia and Iran.
- *French Elections* - Emmanuel Macron ended up winning the Presidential election and a majority of Parliament. Prior to going to the polls, surveys suggested Jean-Luc Melenchon was gaining ground, potentially creating a run-off with Marine Le Pen (both were considered bad for markets).
- *Brexit Woes* - In Britain, Theresa May called snap elections to garner a ***larger*** majority in Parliament, only to ultimately lose her majority. This event raised serious questions about her standing as Prime Minister and her negotiating power in Brexit talks.

Under normal circumstances, we would call these developments significant and likely to impact markets. Despite this, the median daily price move (either up or down) of the S&P 500 has been 0.20% this year, compared with 0.54% in the decade ending December 2016, and 0.38% last year.

Investor Sentiment Summary - Although survey based measures depict a cautious and moderately bearish attitude, we believe investors are more complacent than the headlines suggest.

Lincoln Capital Investment Outlook & Strategy

Over ten years have passed since the first signs of the 2008-2009 financial crisis surfaced and the general stock market has more than tripled since the crisis end in 2009. During this lengthy period, the Fed and other central banks provided enormous sums of capital that served as fuel for the upward re-pricing of assets (stocks, bonds and real estate).

While central bank policies today are far from being tight, the Fed has raised interest rates four times in the past 1.5 years (tightening). They have set expectations for further rate increases and the start of the wind-down of its bond holdings.

The ramifications of these changes are quite significant. While the investment landscape continues to offer ample opportunities, it can be difficult for price-sensitive investors that seek good value to put cash to work in a world where many markets look expensive. History and experience with these types of environments lead us to conclude that having more cash than normal might be a good idea. Does this make us bearish? Not really. We see an awful lot of good things happening that are expected to support growth in global economic activity with technological developments and regulatory relief being significant and primary contributing factors. Simply stated, changes are underway that will likely create more turbulence in financial markets during the next year than during the prior year. If these ripples occur as expected, then having cash available when opportunities arise will prove worthwhile.

LINCOLN CAPITAL'S FINANCIAL PLANNING TOPICS AND TIDBITS

July 2017 - Focus On:

Retirement Income Needs

If you know how much money you need to retire comfortably, you're in the minority. According to a survey of retirement readiness from Bank of America Merrill Lynch, 81% of Americans said they don't know how much money they'll need in retirement. One of the most complicated steps in planning for retirement is estimating how much income will be needed. However, this complex calculation is based on assumptions, like how long you think you'll live, to get an answer.

It's common practice to begin estimating your retirement need by assuming a percentage of current income, which can range from 60%-100% of one's preretirement income. The problem with this approach is it doesn't address a person's specific situation. Someone who plans on traveling in retirement or purchasing a vacation home may easily need 100% or more of their current income. Other challenges exist too, such as health care expenses and living needs. Health care costs historically have increased each year for all, and significantly so for retirees as they age, which comes with the increased risk of illness. Many people's largest expense, a mortgage, is typically paid off in or near retirement and others choose to downsize, which can significantly reduce housing expenses.

Annual income need during retirement should be at least enough to cover essential living expenses plus a cushion for one time discretionary spending, such as home improvements or vacations. Some additional points one should consider:

- According to data published by the Department of Labor in 2015, inflation averaged 2.3% annually over the previous 20 years, which can significantly impact purchasing power if not planned for.
- Deciding when to retire will also help in determining how much income is needed. Having the flexibility to retire at age 50 will cost a lot more than retiring at 65, especially with increases in life expectancy.
- Government and insurance industry mortality tables come from experts and are based on age, gender, race, occupation and family history, but these are just estimates and it's best to assume you'll live longer than expected.

Income replacement rates are a great starting point for estimating income need in retirement. But as one gets closer to retirement, it's best to refine these calculations taking into consideration your unique objectives and circumstances. Please view Lincoln Capital and our retirement planning tools as resources for related information and assistance. And, as always, please contact us if we can be of assistance.

Sources: Ameriprise Financial. *Estimating your retirement income needs*. www.ameriprise.com/research-market-insights

CBS. *How much retirement income do you really need?* www.cbsnews.com/news/how-much-retirement-income-do-you-really-need/

CNBC. *81% of Americans don't know how much they need to retire*. www.cnbc.com/2017/02/15
