PATHSTONE
FEDERAL STREET

# MARKET FLASH REPORT

*October 2017*

## KEY TAKEAWAYS

- Historically speaking, September has often not been a good month for stocks. Investors did not seem to get that message, however, as U.S. equity markets last month continued to break through to all-time highs. Up to this point, investors have largely disregarded North Korea and political tensions, while still holding out hope that lawmakers will be able to push through tax cuts at some point.
- The Federal Reserve left short-term rates unchanged at their September meeting, but kept the door open for one more rate hike later this year (likely in December). The Fed also confirmed that its balance sheet "normalization" plan will kick off in October, at which time it will roll-off rather than reinvest proceeds of its massive bond portfolio. Markets have thus far taken the Fed's plans in stride. However, with Chair Yellen's term expiring early next year, uncertainty over who will next lead the Fed could cause some consternation.
- Republicans unveiled broad strokes of their long-awaited tax reform plan. The key aspects of the proposed framework would be to dramatically lower rates for businesses (from 35% to 20%) and reduce the number of individual tax brackets from seven to three (or perhaps four). Still missing are the details of the new code and the plan for how to pay for it. As investors react to the ongoing debate in Congress, increased market volatility may ensue.
- The U.S. dollar snapped a six-month losing streak, gaining ground in September. Investors seem to expect tax reform to drive growth which will lead to rising interest rates and in turn support for a stronger dollar.


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## INDEX PERFORMANCE (as of 09/30/17)

| Equity | Quarter | Year-to-Date | One-Year |
|---|---|---|---|
| U.S. Large Cap | 4.5% | 14.2% | 18.6% |
| U.S. Small Cap | 5.7% | 10.9% | 20.7% |
| Developed Non-U.S. | 5.5% | 20.5% | 19.7% |
| Emerging Market | 8.0% | 28.1% | 22.9% |
| **Real Assets** | | | |
| Real Estate | 3.6% | 11.9% | 5.8% |
| Commodities | 2.5% | -2.9% | -0.3% |
| Natural Resource Equities | 7.4% | -4.4% | 0.4% |
| **Fixed Income** | | | |
| Core Plus | | | |
| U.S. High Yield Debt | 2.0% | 7.0% | 8.9% |
| Emerging Market Debt | 3.6% | 14.3% | 7.3% |
| Core Bonds | | | |
| U.S. Aggregate Bonds | 0.8% | 3.1% | 0.1% |
| U.S. Treasuries | 0.4% | 2.3% | -1.7% |
| U.S. Municipal Bonds | 0.7% | 3.7% | 1.0% |

| Month-End Values/Yields | Current | Prior Month | One-Year Ago |
|---|---|---|---|
| CBOE Volatility Index | 9.5 | 10.6 | 13.3 |
| 10-Year Treasury Yield | 2.3% | 2.1% | 1.6% |

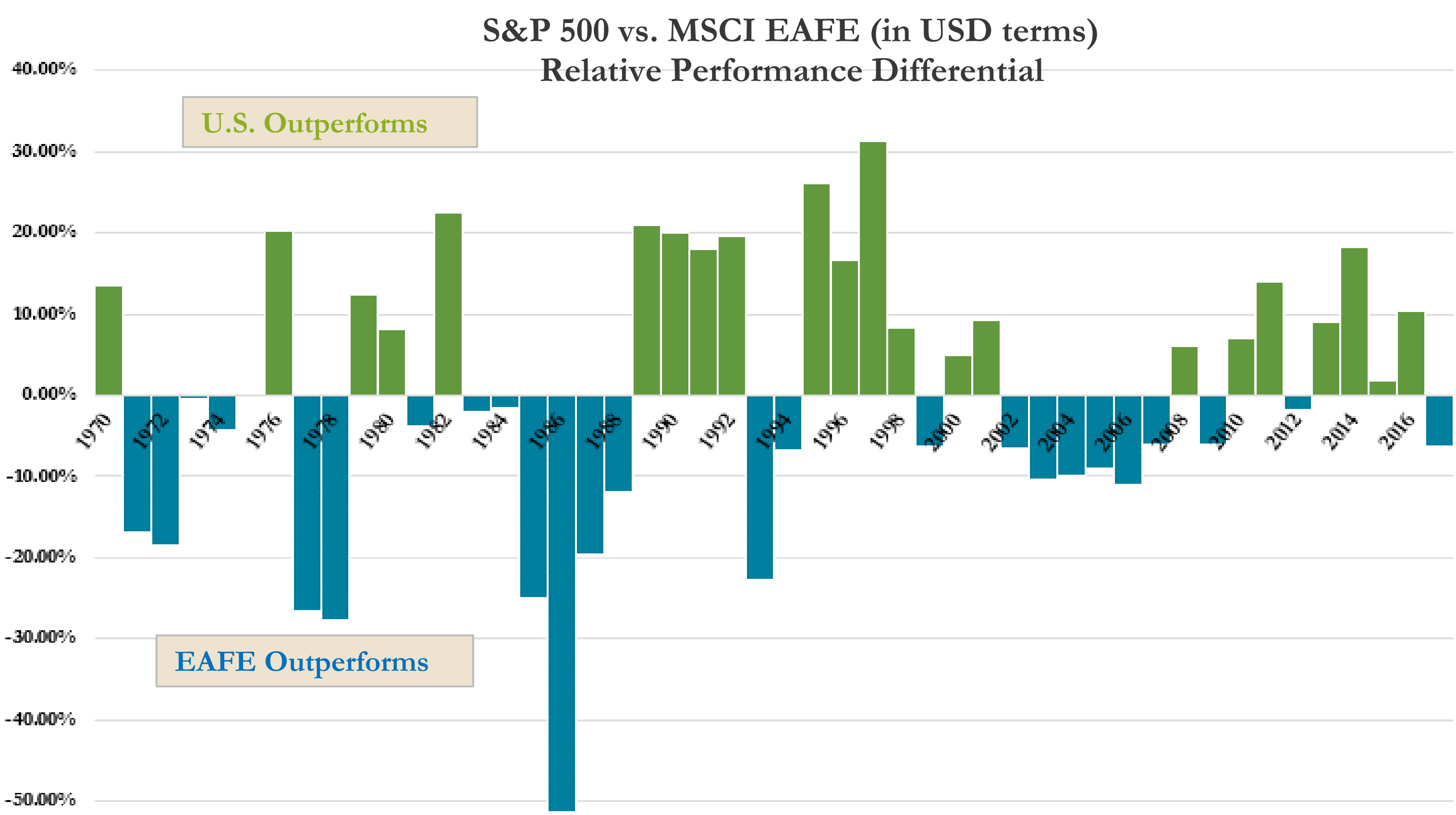
*Sources: Bloomberg, Morningstar*

*You cannot invest directly in an index; therefore, performance returns do not reflect any management fees. Returns of the indices include the reinvestment of all dividends and income, as reported by the commercial databases involved.*

## REGIONAL COMMENTARY

- Entering October, the S&P500 Index is at all-time highs. The Fed has announced its plans for starting to slowly reduce its $4.5 trillion balance sheet in October and all eyes are now focused on the potential for tax reform. Markets enjoyed somewhat of a rotation in September as value stocks outperformed growth for just the second month this calendar year, and big tech growth stocks took a little breather.
- Global markets have continued to shrug off geopolitical events (for the most part), as global growth and more optimism abounds. With the re-election of Angela Merkel in Germany, the French President Emmanuel Macron's labor policy reforms (reduction of regulatory burdens on companies), and overall efforts to bring the European Union closer together, there is renewed optimism in investors' spirits. Nonetheless, much of the returns experienced by U.S. based investors have been driven by the strength of the Euro vs. the USD. It is also worth noting that the recent Catalan secession movement has had only a local effect on Spanish markets.
- Despite subtle tensions between the U.S. and China, in particular over North Korea, the Chinese market continues to show signs of growth. Further optimism driven by policy change has helped the Chinese markets perform well. Emerging Market equities suffered their first monthly loss of the year in September with a 40bps pull-back, but are still up nearly 28% year-to-date. Investors will pay close attention to any potential ripple effects in the Emerging Markets caused by U.S. Fed rate policy. Otherwise, EM still remains the most attractively valued of the equity spectrum.

**"International Stocks are the Latest Fashion"**
**Helped by USD weakness, International Stocks outperforming for only 3rd time in 10 years.**




*Sources: Pertrac, S&P, MSCI*

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U.S. Large Cap Equity is represented by the S&P 500 Index, with dividends reinvested. U.S. Small Cap Equity is represented by the Russell 2000 Index. Developed Non-U.S. Equity is represented by the MSCI EAFE Index. Emerging Market Equity is represented by the MSCI EM Index. Real Estate is represented by the S&P Global Property Index. Commodities are represented by the DJ UBS Commodity Index. Natural Resource Equities are represented by the S&P North American Natural Resources Index. U.S. High Yield Debt is represented by the Bloomberg Barclays U.S. Corporate High Yield Index. Emerging Market Debt is represented by the JPM GMI-EM Global Diversified Index. U.S. Aggregate Bonds is represented by the Bloomberg Barclays U.S. Aggregate Bond Index. U.S. Treasuries is represented by the Bloomberg Barclays U.S. Treasury Index. U.S. Municipal Bonds is represented by the Bloomberg Barclays Municipal 1-10yr Index.