BARNES • PETTEY
FINANCIAL ADVISORS, LLC
Independent Registered Investment Advisor

Global Stocks Cap Strong First Half

According to the Wall Street Journal, all but four of the thirty major indexes representing the world's largest stock markets by value have risen this year, a first half performance unmatched since 2009. It was an impressive gain in a bull market that now stands as the second longest since World War II.

The year began on positive footing as investors cheered what they viewed as a unified government that seemed bent on passing corporate tax cuts, cutting rates sharply on the repatriation of overseas earnings, and unlocking new funds to expand and repair the nation's infrastructure. Fast forward to the end of June and early expectations of a quick passage of pro-growth measures have been severely tempered by policy disputes among key party members that control government. Still that has done little to damper enthusiasm. Instead there seems to have been what I call a passing of the baton: from policy prescriptions that would aid the economy and stocks to stronger S&P 500 profit growth, modest at best economic growth at home, a still relatively accommodating Federal Reserve, and a large acceleration in global economic growth. Yes investors hate heightened uncertainty and we have been treated to plenty of it, but respectable fundamentals have set the tone for investors. **Some are calling this a Teflon stock market, nothing negative sticks!**

The big news last week was that Federal Reserve chairman Janet Yellen resumed her "Fairy Godmother" role when she testified before Congress and made it clear that any future interest rates increases would be gradual, data dependent, and probably few and far between. Specifically Chairman Yellen acknowledged the recent softness in inflation and said that the Federal Reserve could alter its policy if inflationary weakness proves to be more stubborn than the Federal Reserve expects. As a result, the next key interest rate hike by the Fed may be postponed until late December.

The rally has also been marked by a lack of volatility, giving rise to concerns in some corners that complacency will inevitably lead to a rockier trading environment.

The big winner in the first half is the foreign markets with the MSCI EAFE up 11.8% and the MSCI emerging market index increased 18.4%. We have noted in our previous Newsletters the undervaluation of the foreign markets relative to the US markets.

We have also witnessed a very strong start for major US Large Cap averages, with growth easily taking the top spot in all three categories of large, mid cap, and small cap stocks. The value side of the market proved to be the laggard.

US economic performance has been underwhelming in the first half but investors' enthusiasm tied to tax cuts, tax reform, and a burst in infrastructure spending, all of which would boost the economy, have been tempered by the current political reality.

We enter the ninth year of this economic expansion. There is an adage that says "expansions do not die of old age". It is typically Federal Reserve interest rate hikes or speculative excesses that do them in. **I believe a silver lining in today's slow economy is that we have not seen speculative excesses brought on by euphoria buildup in the economy** and that could extend the life of this stock market rally.

The Federal Reserve's target of inflation at 2% is not going too well. Core inflation, which excludes food and has yet to reach the 2% target, suggests it will take a bit longer for the Federal Reserve to obtain what it considers to be price stability. In summary, the key points for continued equity outperformance are positive growth, low inflation, climbing earnings, and an accommodating Federal Reserve. It does appear that these trends will continue, but that does not mean we will eliminate our defensive positions.

-INTERESTING FACTS-

FEDERAL RESERVE STRESS TEST – The findings of the Federal Reserve's "**stress test**" completed on **34 large US banks** were released on Thursday 6/22/17. The tests, created in 2009, showed the **banks all passed** for the 3rd consecutive year. The banks were put through financial simulations to determine if they could survive a 2-year economic slump that included a 10% national unemployment rate, a 50% decline in stock values, a 25% drop in home process and a 35% decline in commercial real estate prices (source: Federal Reserve).

NEW HOME CONTSTRUCTION – Permits for the construction of 6.14 million single family homes were issued during the 4 years of 2003-2006. Permits for the construction of 6.06 million single family homes were issued during the 10 years of 2007-2016 (source: Joint Center for Housing Studies of Harvard University).

BETTER CARE RECONCILIATION ACT – Of the estimated **22 million** Americans that would not have health insurance coverage by the year 2026 under the "Better Care Reconciliation Act" (BRCA) when compared to the current law, **15 million** are Medicaid beneficiaries while **7 million** buy their policies in the individual insurance market (source: BRCA). The Congressional Budget Office (CBO) estimates that the BCRA would **reduce the federal deficit by $321 billion** over the next 10 years (201702026), the net of **$1.022 trillion** in reduced federal spending (including $722 billion in **lower Medicaid spending**) offset by **$701 billion** in reduced federal revenues (including **$563 billion** in repealed **"Affordable Care Act" taxes**) (source: CBO).

JOBS – In July 2009 there were **14.6 million** unemployed Americans and **2.2 million** job openings. In April 2017 there were **7.1 million** unemployed Americans and **6.0 million** job openings. (source: Department of Labor).

From Our Friends at RiverFront

GLOBAL EARNINGS IMPROVING

SYNCHRONIZED MOMENTUM GLOBALLY; A GOOD SIGN FOR MARKETS

In our view, economic improvement is mainly relevant to investors insofar as it has a positive effect on the trajectory of corporate earnings.

To this point, we are seeing global earnings momentumimprove to its strongest level since 2010, with a particular emphasis on areas like the Eurozone, Japan and emerging markets. We view this as positive for global stock markets.

According to IBES consensus earnings estimates, the world's major geographic areas are all on track to produce significantly positive earnings in fiscal year 2017, in contrast to the last eight years, where improvement tended to be clustered only in certain geographies.

Source: Thomson Reuters Datastream, Institutional Brokers' Estimate System Earnings (IBES) current forecast is designed to help portfolio managers and analysts identify, manipulate, and analyze exceptional information for over 40,000 equities worldwide.

RiverFront's momentum equals the number of earnings-per-share estimates revised up, minus number revised down divided by total number of estimates over last 3 months.

Data from June 2007 through June 2017. Past performance is no guarantee of future results. It is not possible to invest directly in an index.

New Oxford Location

We have moved our office to 2153 South Lamar Boulevard, Suite 200. Pictured Kathy Atkins, Art Smith, and Brook Hodges.

Barnes Pettey has babies!

Meet Annie James Bowen, born May 14. Pictured with Annie James are her proud big sister, Ellison, and her mom Strider.

Meet Vivian Ping Yee, born to Meghann and Andrew Yee on April 28.

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-Standard & Poor's 500 (S&P 500) measures changes in stock market conditions based on the average performance of 500 widely held common stocks. S&P 500 represents approximately 68% of the investable U.S. equity market. MSCI EAFE (Europe, Australasia, Far East): a free cost-adjusted market capitalization index that is designed to measure developed market equity performance, excluding the United States & Canada. The EAFE consist of the country indices of 21 developed nations.
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- MSCI Emerging Markets is designed to measure equity market performance in 25 emerging market indexes. The index's three largest industries are materials, energy, and banks. International investing involves special risks, including currency fluctuations, differing financial accounting standards, and possible political and economic volatility.
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