Goodman FINANCIAL
MONEY MANAGER • FINANCIAL ADVISOR • PHILANTHROPY

5177 Richmond Avenue, Suite 700
Houston, Texas 77056

Phone: (713) 599-1777
Toll free: (877) 599-1778
Fax: (713) 599-1811
www.goodmanfinancial.com

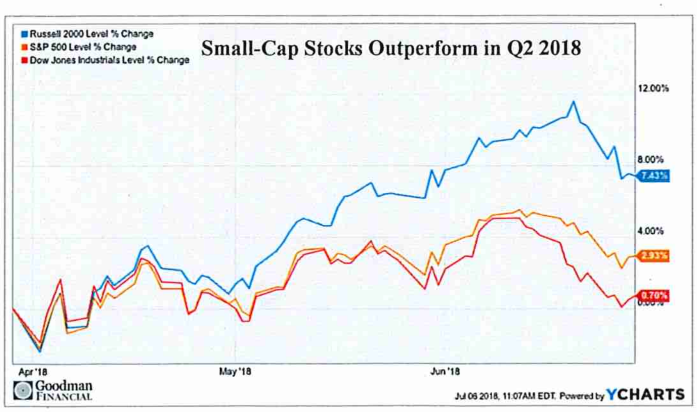
SECOND QUARTER 2018 MARKET & ECONOMIC REVIEW

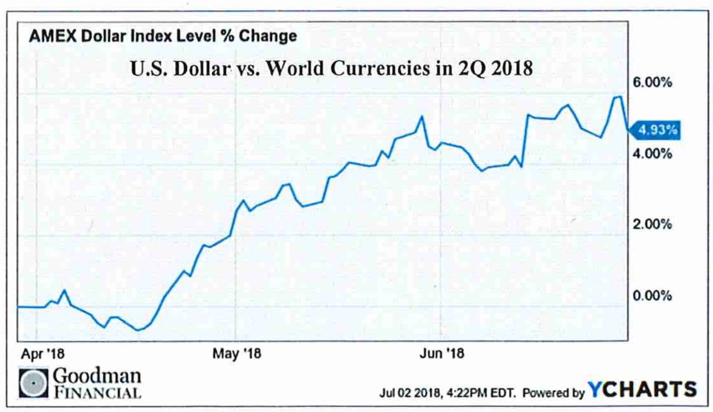
Major Equity Market Indexes & Commentary

Index	Description	3/31/18	Low Close	High Close	6/30/18	QTD Return*
S&P 500	A market-capitalization weighted index of 500 large U.S. companies.	2,640.87	2,581.88	2,786.85	2,718.37	2.93%
DJIA	Dow Jones Industrial Average or "The Dow"; A price-weighted average of 30 major U.S. companies.	24,103.11	23,644.19	25,322.31	24,271.41	0.70%
Nasdaq Composite Index	A market-capitalization weighted index comprised of over 3,000 companies, mostly in the technology and biotech industries.	7,063.44	6,870.12	7,781.51	7,510.30	6.33%
Russell 2000	A market-capitalization weighted index tracking U.S. small-cap stocks.	1,529.43	1,492.53	1,706.99	1,643.07	7.43%
NIKKEI 225	A price-weighted index comprised of Japan's top 225 most established companies.	21,454.30	21,292.29	23,002.37	22,304.51	3.96%
MSCI Emerging Markets	An index comprised of 23 MSCI indices from emerging economies including Brazil, China, India, Mexico, Russia, South Africa, and the UAE.	1,170.88	1,046.71	1,184.13	1,069.52	-8.66%
Stoxx Europe 600	An index comprised of 600 companies based in one of 18 EU countries including Austria, Belgium, Denmark, France, Germany, Ireland, Spain, and the United Kingdom.	370.87	367.33	396.94	379.93	2.44%

* Excludes effects of dividends — Sources: FactSet

- Major U.S. stock indices gained during the second quarter of 2018, with the Dow Jones up 0.70%, the S&P 500 up 2.93%, and the NASDAQ Composite continuing its winning ways with a gain of 6.33%.
- As seen in the chart below, small-cap stocks as represented by the Russell 2000 index were the champions this quarter, up 7.43%. As these companies are more U.S. domestic-focused, they are less impacted by the potential negative effects of global trade wars than their large-cap peers. Smaller company are also getting a bigger positive impact to earnings from the new tax law.
- Returns were mixed within S&P 500 sectors. Energy stocks led all sectors in Q2, up 12.7%. Other positive sectors include Consumer Discretionary, Technology, and Real Estate, while Consumer Staples, Financials, Industrials and Telecom posted losses.
- The big loser in the quarter was the MSCI Emerging Markets Index, which was down 8.7% in Q2. This index was hit both by emerging markets currencies coming under pressure (see the chart below) as well as by heightened concerns about fallout from global trading wars, especially since mainland China and Hong Kong combined comprise 30.7% of the index.
- European stocks as represented by the STOXX Europe 600 increased 2.4% in Q2, erasing some of its Q1 losses. Japanese stocks as represented by the Nikkei 225 index were up 3.96%, also erasing some of its Q1 losses.
- As seen below, the U.S. dollar increased by 4.9% as measured by the AMEX Dollar Index (DXY). Such increases tend to depress asset returns denominated in other currencies such as foreign stocks, as well as assets like gold.





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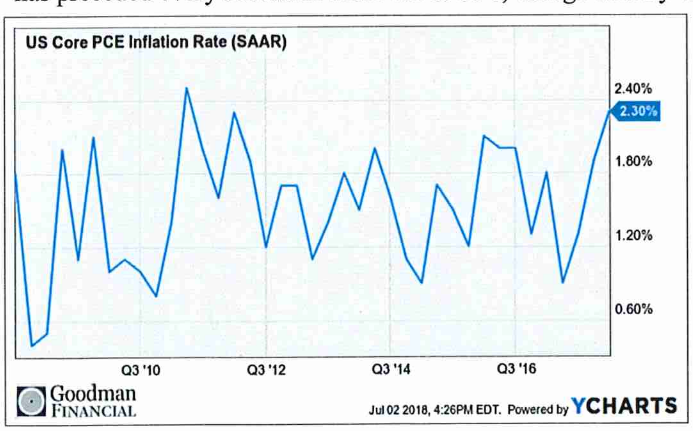
Fixed Income Rates & Commentary

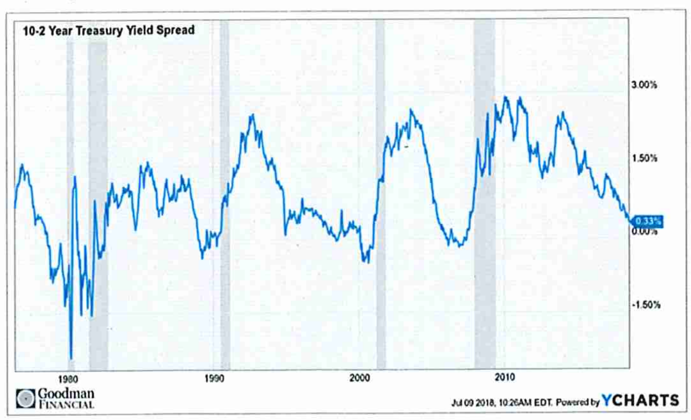
Description	3/31/18	6/30/18	QTD Change in Basis Points*	Description	6/30/18	52-Week Range	
						Low	High
90 Day Treasury Bill	1.73%	1.93%	↑ 20	Federal Funds Rate Target	1.75%-2.00%	1.00%-1.25%	1.75%-2.00%
10 Yr. Treasury Note	2.74%	2.85%	↑ 11	Prime Rate (U.S.)	5.00%	4.25%	5.00%
30 Yr. Treasury Bond	2.97%	2.98%	↑ 1	LIBOR (3mo.)	2.34%	1.30%	2.37%
15 Yr. Mortgage Rate	3.86%	3.99%	↑ 13	5-Year CD	1.74%	1.39%	1.74%
30 Yr. Mortgage Rate	4.40%	4.53%	↑ 13	New-car Loan (48mo.)	3.74%	2.85%	4.28%

* One basis point is equal to 1/100th of 1%, or 0.01%

Sources: FactSet, Wall Street Journal, U.S. Treasury

- Bonds had mixed returns in Q2 as interest rates increased modestly. The widely followed Barclay's Aggregate Bond Index Composite posted a loss for Q2 of 0.2%.
- The Federal Open Markets Committee of the U.S. Federal Reserve (the Fed) voted during its mid-June meeting to raise the Fed Funds Target Rate range by 25 bps to 1.75% to 2.00%. The markets had been expecting such a decision. This is the seventh rate hike since the Fed started raising the Fed Funds rates in late 2015.
- The Fed signaled that two further rate hikes are likely this year—one more than they had previously signaled—which would leave the target rate at a range of 2.25%-2.50% by year end. This more aggressive hiking stance is likely due to increasing inflationary pressures. As seen in the graph below, the Fed's most closely watched inflation measure, the PCE Core inflation rate increased recently to 2.3%, above the Fed's stated 2% target and the highest since 2012. This increase is due to increasing wage pressures, increasing freight and transportation costs, and the pass-through effects of higher oil prices.
- As seen above, the 30-year mortgage rate increased in the quarter to 4.53%. It had risen as high as 4.62%, the highest rate since May 2011. This has raised some fears in the market that higher mortgage rates will cause a housing slowdown. But, the most recently published May 2018 housing starts came in at 1.35 million homes, the most since July 2007. We believe that pent-up housing demand from the Millennial generation will continue to drive housing starts and that much higher mortgage rates would be needed to dampen that demand.
- As we discussed in our "June 2018 Market Commentary," the difference between current yields on the 10-year and 2-year treasuries (the so called "10-2 spread") has narrowed to the lowest level since August 2007. This can be seen in the chart below where the difference at quarter-end was 0.33%. This is something that is beginning to receive attention from market participants and that GFC is watching closely. If the 10-2 spread drops below zero then a condition know as "yield inversion" exists - something that has preceded every recession since the 1980's, though usually with a lag.





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Economic Indicators

Indicator	Description	3/31/18	6/30/18	QTD Change
Average Weekly Initial Claims for Unemployment Insurance (Thousands)	The number of new filings for unemployment insurance benefits. **Claims stayed low for another quarter, suggesting strength in the labor market.** *Most economists believe claims below 300,000 indicate a healthy labor market environment.*	228.25	224.50	-1.6%
Unemployment Rate	The percentage of total labor force that is unemployed but actively seeking employment. **The unemployment rate remains near low level last seen in early 2001.** *The U.S. Federal Reserve targets a long-run unemployment rate of between 4.5% and 5%.*	4.1%	4.0%	-10 bps
Average Weekly Earnings	The average weekly salary earned by private, nonfarm employees. **Wages rose during the quarter, likely a result of a tightening labor market. This suggests more disposable income for consumers and may attract more workers to join the labor force.**	$924.60	$930.81	0.67%
Index of Consumer Sentiment	This index reflects consumer attitudes towards the state of the economy. **Consumer confidence declined since March but stayed near post-recession highs.**	101.4	98.2	-3.16%
Manufacturers' New Orders for Consumer Goods and Materials (Millions) *	The number of new orders placed for consumer goods. **New orders increased, indicating higher demand for U.S.-produced consumer goods and validating still-high consumer confidence and low unemployment.**	$207,820	$208,729	0.44%
Manufacturers' New Orders for Nondefense Capital Goods, Excluding Aircraft (Millions) *	This index is the producer's counterpart of new orders of consumer goods and materials. **New orders for nondefense capital goods increased during the quarter, suggesting increased business confidence in the economy.**	$66,478	$68,069	2.39%
US Capacity Utilization: Manufacturing *	The ratio of production capacity being used to produce finished products compared to the total capacity available. **Utilization declined modestly but remains within the mid-70% range it has been in since 2012.**	76.0%	75.8%	-20bps

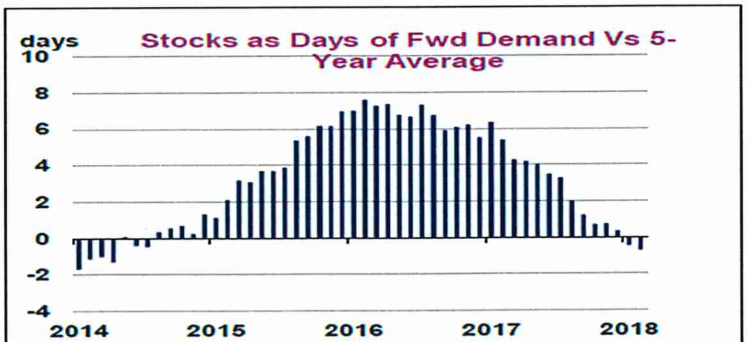
*These items are as of 5/31/18, the date of the most recently published statistics

Sources: Federal Reserve Bank of St. Louis, The University of Michigan, U.S. Census Bureau, U.S Department of Labor

U.S. Economic Health

- Initial Claims for Unemployment Insurance continued their downward trend, making post-recession lows during Q2 and reaching the lowest level since December 1969, when amazingly, the U.S. population was nearly one-third lower than it is today.
- The unemployment rate ended the quarter at 4.0%, having reached as low as 3.8% in May - a level last seen in April 2000.
- As noted on page 2, inflation continued its upward trend to near post-recession highs and now exceeds the Fed's 2% target. As seen above, many widely followed measures of U.S. economic growth continue to be positive. The new tax law appears to have caused many consumers and companies to be more optimistic about the near-term future.
- Rhetoric and threats around trade tariffs and an impending trade war do not seem to have impacted U.S. economic growth so far. The implementation of actual tariffs (if they do occur) and resulting retaliation would likely have negative effects to the economy.
- Oil prices rose 11% during the quarter and are up 23% in 2018. This is due to the fact that the world continues to draw down crude oil inventories. As seen below, when inventories are analyzed on a "days of consumption" perspective, they are now below 5-year averages...and continue to decline. It's no wonder OPEC recently announced an increase in their production quotas - the world needs those barrels.

Worldwide Crude Oil Inventories



Source: International Energy Agency (EIA)