Goodman Financial
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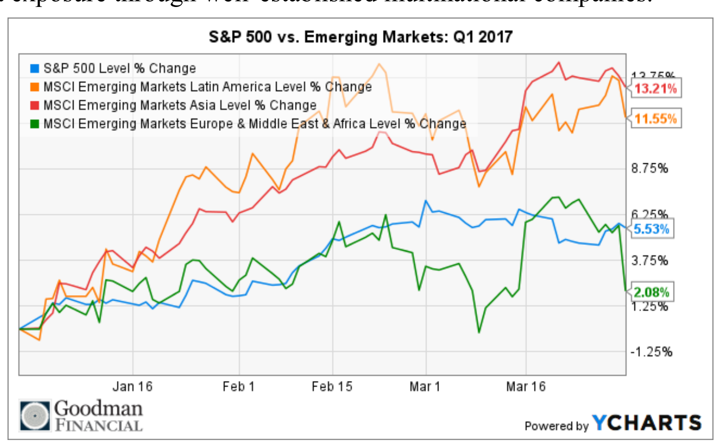
FIRST QUARTER 2017 MARKET & ECONOMIC REVIEW

Major Equity Market Indices: First Quarter 2017

Index	Description	First Quarter 2017*				
		12/31/16	High	Low	3/31/17	QTD Return
S&P 500	A market-capitalization weighted index of 500 large U.S. companies.	2,238.83	2,400.98	2,245.13	2,362.72	5.53%
DJIA	Dow Jones Industrial Average or "The Dow"; A price-weighted average of 30 major U.S. companies.	19,762.60	21,169.11	18,603.14	20,663.22	4.56%
Nasdaq Composite Index	A market-capitalization weighted index comprised of over 3,000 companies, mostly in the technology and biotech industries.	5,383.12	5,928.06	5,397.99	5,911.74	9.82%
NIKKEI 225	A price-weighted index comprised of Japan's top 225 most established companies.	19,114.37	19,668.01	18,650.33	18,909.26	-1.07%
MSCI Emerging Markets	An index comprised of 23 MSCI indices from emerging economies including Brazil, China, India, Mexico, Russia, South Africa, and the UAE.	862.27	974.95	858.02	958.37	11.15%
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.	361.42	380.48	359.92	381.14	5.46%

* Excludes effects of dividends — Sources: YCharts, Wall Street Journal

- The first quarter was generally good for the equity markets worldwide. The Nikkei, Japan's main benchmark, was the only index above to lose ground. The fourth quarter of 2016 saw the Nikkei grow at stout rate of 16.2%, so a combination of rationalizing valuations and taking profits in the first quarter of 2017 probably led to the decline.
- The Dow broke through the 20,000 mark for the first time and went on a streak of all-time highs from January through March 1st, only to give back about a third of quarterly gains during the balance of March. An impasse in Congress over healthcare reform contributed to the index's retreat. Politics has weighed heavily on the market over the past few quarters, perhaps too much so. We continue to focus on fundamentals, so we pay attention to policy with lasting, real-world impacts—not transient, beltway politics.
- The best performer during the quarter was the MSCI Emerging Markets index. These markets—which tend to be in commodity-dependent countries—have benefitted from stable oil prices and improved investor sentiment. MSCI further distills emerging markets down to the continental level. The graphs below depict the continental indexes and their performance against the S&P 500.
- While there is growth in emerging economies, there continues to be considerable risks unique to each country. Note that some of the growth in the value of U.S. stocks, as well as those of other developed countries, is due to the expansion of operations into emerging economies. More and more consumer goods companies and service companies are opening up shop in once-neglected economies. At this point, we still prefer to gain emerging market exposure through well-established multinational companies.



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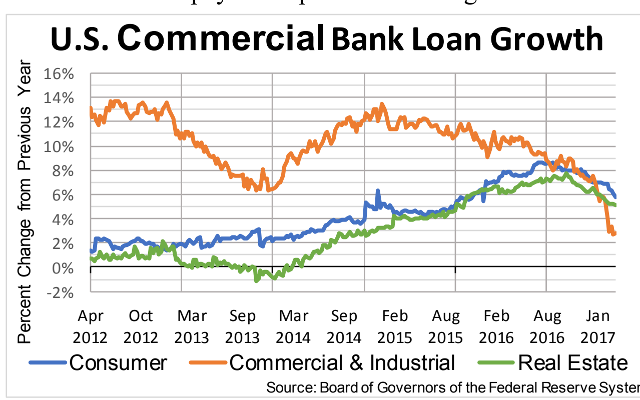
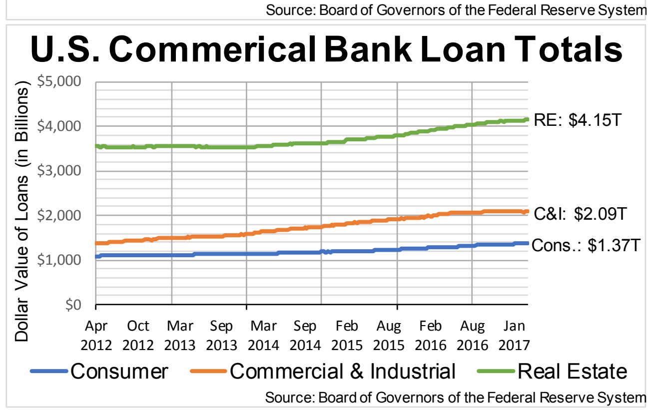
Fixed Income: First Quarter 2017

First Quarter 2017						52-Week Range	
Description	12/31/16	3/31/17	QTD Change in Basis Points*	Description	3/31/17	Low	High
90 Day Treasury Bill	0.51%	0.76%	25	Federal Funds Rate Target	0.75%-1.00%	0.25%-0.50%	0.75%-1.00%
10 Yr. Treasury Note	2.45%	2.40%	-5	Prime Rate (U.S.)	4.00%	3.50%	4.00%
30 Yr. Treasury Bond	3.06%	3.02%	-4	LIBOR (3-Month)	1.15%	0.62%	1.16%
15 Yr. Mortgage Rate	3.42%	3.33%	-9	5-Year CD	1.29%	1.17%	1.29%
30 Yr. Mortgage Rate	4.21%	4.13%	-8	HELOC ($30,000)	4.86%	4.55%	4.96%

* One basis point is equal to 1/100th of 1%, or 0.01% Sources: YCharts, Wall Street Journal

- The Federal Open Markets Committee of the U.S. Federal Reserve voted in March to raise the Fed Funds target rate by 25 bps to 0.75% - 1.00%. The March meeting minutes revealed that the Fed has a positive, though cautious, outlook on the U.S. economy. Changes to the Fed Funds rate tend to have a greater impact on short-term rates than on long-terms rates, as has been borne out by the narrowed spread between the 90-day and 10-year treasurys, from 1.94% on December 31st to 1.64% on March 31st.
- The minutes also revealed that the Fed would soon begin "normalizing" its balance sheet, the process by which the Fed stops reinvesting interest and matured bond proceeds and eventually sells the bonds accumulated during quantitative easing. The effective impact of this is to raise interest rates, especially on long-term bonds.
- The Fed's decision to raise rates atypically narrowed the margin between what banks pay on deposits and charge on loans. The decision to normalize the balance sheet is likely welcomed by banks as an impetus to raise loan rates beyond what is offered by rate hikes.
- Over the past 5 years, commercial bank lending has grown at a compounded annual rate of 5.36%, from $7.01 trillion in March 2012 to over $9.11 trillion in March 2017, a growth rate spurred on by low rates. (The graphs exclude loans categorized as "Other" worth $1.02 trillion in 2012 and $1.52 trillion in 2017.) The graphs to the right depict year-over-year lending growth in the U.S. since March 2012.
- While commercial bank lending is still growing, the rate of growth tapered off noticeably during the quarter, especially so for Commercial & Industrial loans (a catch-all category for most business loans).
- The causes of the slowdown are up for debate, but plausible reasons include businesses waiting to see new tax rules that may influence the timing of investments and the energy industry taking a more cautious approach to borrowing (and banks taking a more cautious approach to lending to the energy industry). There's also the fact that a larger denominator makes the same dollar value represent less growth.
- Banks are able to support loan demand, with deposit growth outpacing loan growth. Deposits at all commercial banks grew 6.10% over the past 5 years to $11.62 trillion, so the ratio of loans to deposits actually decreased from 81% to 78%, according to U.S. Fed data.
- There appears to be plenty of dry powder in banks' arsenals to enable the current economic expansion. While loan rates are expected to rise, rates will still be low in the context of the past few decades. Borrowers and banks alike still have room to grow in this business cycle.





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Economic Indicators: First Quarter 2017

Indicator	Description	12/31/16	3/31/17	QTD Change
Average Weekly Initial Claims for Unemployment Insurance	The number of new filings for unemployment insurance benefits. **A decrease in the number of claims suggests fewer layoffs.** *Most economists believe claims below 300,000 indicate a healthy labor market environment.*	253,750	250,000	-1.48%
Unemployment Rate	The percentage of total labor force that is unemployed but actively seeking employment. **The unemployment rate remains below 5%.** *The U.S. Federal Reserve targets a long-run unemployment rate of between 4.5% and 5%.*	4.7%	4.50%	-20 bps
Average Weekly Earnings	The average weekly salary earned by private, nonfarm employees. **Average weekly earnings slightly increased. This suggests more disposable income for consumers and could be the result of a tightening labor market.**	$893.71	$896.60	0.32%
Index of Consumer Sentiment	This index reflects consumer attitudes towards the state of the economy. **Consumer confidence backed off its 13-year high but remains strong.**	98.20	96.90	-1.32%
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 high consumer confidence and lower unemployment.**	$196,658	$197,577	0.47%
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.**	$64,676	$64,737	0.09%
US Capacity Utilization: Manufacturing *	The ratio of production capacity being used to produce finished products compared to the total capacity available. **Capacity utilization increased slightly, in line with increased new orders and confidence.**	75.5%	76.3%	75 bps

*These items are as of 02/28/17, the date of the most recently published statistics

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

U.S. Economic Health

The table above and the graphs below continue to paint the U.S. economy as being in growth mode. The sluggish, somewhat disappointing recovery we experienced since the recession is bearing the fruits of higher wages and lower unemployment. Importantly, the unemployment figure has continued to drop concurrently with a rising labor force participation rate. This is important to note because some of the improvement to the unemployment rate following the recession was due to individuals dropping out of the labor force (and falling off the Bureau of Labor Statistics' radar). Seeing that wages are keeping up with—and in many years exceeding—inflation is a good indication that employers are seeing enough business to enable raises.

A rising participation rate is a double-edged sword, though. On a macro level, more people are providing for themselves and their families, earning a paycheck, paying taxes, and potentially furthering their lot in life. On a micro level, individuals are seeing more competition for work. More people willing to work could translate into less overtime or slower wage growth. Why give a raise or pay overtime wages when you have another person to offload the work to? As is always the case, the economic pendulum continues to swing, so we continue to monitor these and other indicators in an effort to understand where it is swinging and why.