



Market Perspectives

STAY INVESTED, BUT EXPECT MORE MODERATE RETURNS

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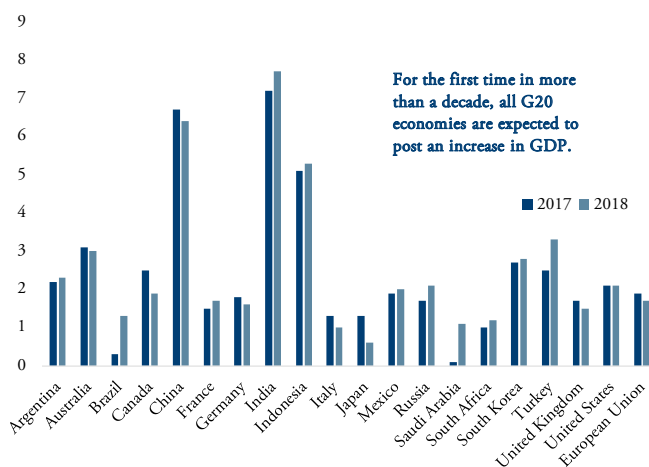
It's certainly been a remarkable year for global equity investors. The S&P 500 looks set to deliver gains of more than 20% in 2017, while emerging markets in Asia are delivering 40% gains. This is in contrast to Investment Grade bond investors earning approximately 2%. Although dysfunction in Washington and heightened geopolitical tensions are valid sources of concern, investors have remained focused on improving economic growth, rising corporate profits and the upcoming changes to the tax code. We project that equity returns could be in the 5-7% range in 2018 as rising corporate profits and steady consumer spending should help extend the bull market.

2017 saw a global economic and stock market expansion. For the first time in a decade, we believe the economies of all 45 countries followed by the OECD are growing, and 33 of them are poised to accelerate (see Figure 1). Moreover, we see few obvious clouds on the horizon for the world economy. Business surveys have improved in recent months, inflation has remained low, and the expansion is forecast to continue through next year.

Most importantly for investors, the upturn in the world economy is fueling an impressive recovery in corporate profits.

Figure 1

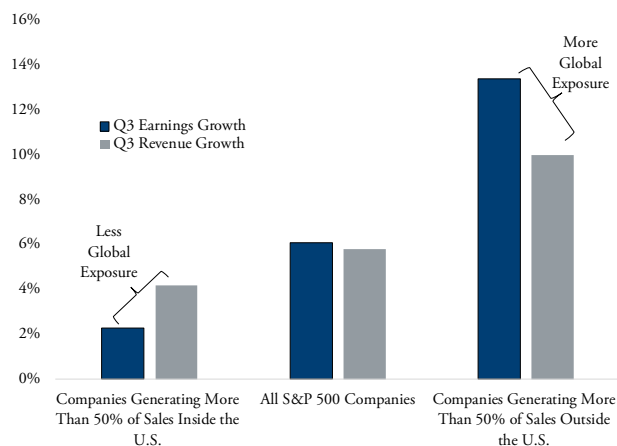
Global Synchronized Upturn (GDP Growth Forecasts)



Source: Organisation for Economic Cooperation and Development. As of November 30, 2017.

Figure 2

Global Demand Driving U.S. Earnings Growth



Source: FactSet. As of Q3 2017.

S&P 500 earnings are on track to increase 10% in 2017 thanks in large part to the ongoing strengthening in global demand (see Figure 1). Now add to this a significant reduction in the corporate tax rate to 21%, and we think U.S. corporate earnings could rise another 10-14% in 2018 (see Figure 3).

There's an old saying that bull markets are born on pessimism, grow on skepticism, mature on optimism, and die on euphoria. We don't think we are in that final stage yet. Although valuations of major markets look full with recent price gains, they do not appear too expensive to prohibit further price gains. In fact, research shows that factors such as the state of the business cycle, business sentiment, and corporate earnings are actually more important in regard to near-term return expectations (see Figure 4).

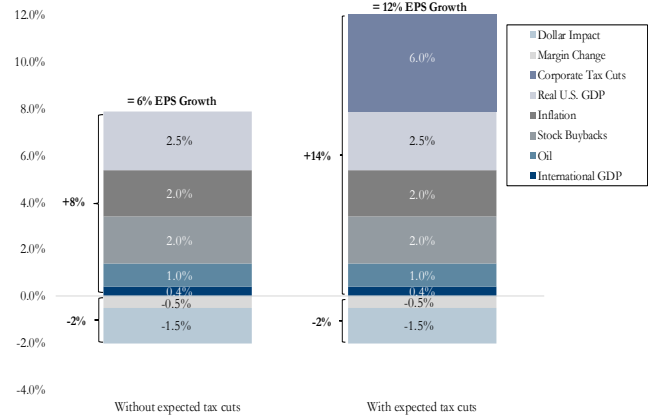
Still, it would be wise not to extrapolate 2017's performance into 2018, nor to expect the same smooth ride of steady monthly market advances. Corporate profit growth forecasts have risen substantially, and much of that increase appears to have already been priced into the market. At 13 months and counting, we are in the longest period in S&P 500 history without a 3%+ correction, and with the expectations bar now

set quite high heading into next year, pullbacks are expected, and we feel this would be healthy.

We've been enjoying a period of steadily rising stock prices for over eight years now, and if, as we expect, the bull market continues beyond August, it will be the longest ever. Ultimately, our optimism remains rooted in the positive fundamental outlook. Bear markets rarely occur outside of economic downturns, and current recession risk appears low both at home and abroad.

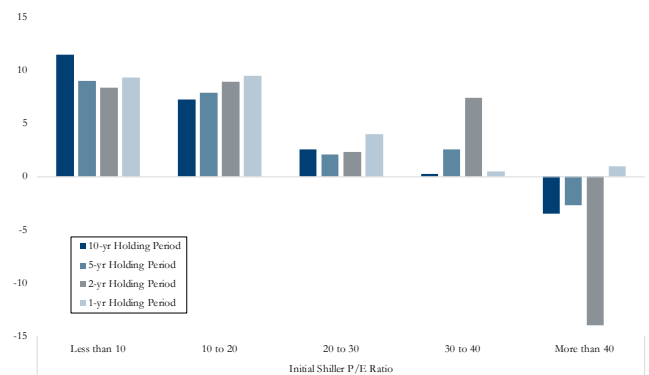
Given all this, our advice for investors is to stay invested but also to lower expectations. For many years, our asset allocation has been steadfastly overweight U.S. large cap, high dividend, and EM Asia equities, and we remain overweight going into 2018. Global economic growth will likely continue to lift earnings; however, we do appear to be entering the later stages of the market cycle and investors should remain disciplined. The final stages of a market cycle can be rewarding, but this year's impressive market gains are unlikely to be repeated and investors should expect more moderate returns in 2018.

Figure 3
Tax Cuts Could Affect Our EPS Outlook



Source: City National Rochdale. As of December 21, 2017.

Figure 4
Annualized Real Total Return



Source: BCA Research. As of December 31, 2016. Based on S&P 500 data since 1881.

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