A late month rally in stocks propelled by the increasing likelihood that the Republican tax bill would pass both houses of Congress sent US stocks to new all-time highs. The Dow Jones Industrial Average (the “Dow”) surged, as many of the companies that comprise the index stand to benefit from reduced corporate taxes and repatriated profits held abroad. Not to be outdone, mid and small sized company stock prices also rose on the momentum of the tax bill, with both market indexes exceeding the performance of the index for larger sized companies. Non-US equities also moved higher, with developed international stocks posting solid monthly gains, though Emerging Market (“EM”) stocks pared their advance on the last couple of days to finish the month near the flat line. The bond market largely declined during the month, as spreads widened somewhat and the Treasury yield curve flattened by about 13 basis points (“bps”), a sign some bond investors argued that economic growth is slowing. Broad commodity markets posted small negative returns, even though crude oil was up. The Organization of Petroleum Exporting Countries (“OPEC”) was scheduled to meet on the last day of the month to negotiate further production cuts with key non-OPEC producing nations, in their collective efforts to balance the oil market. Industrial metals fell on Chinese housing concerns. Finally, many in the investment community were captivated by the increase in the price of Bitcoin during the month, up a whopping 52% and up 10-fold for the year.

With earnings season effectively over and economic data continuing to paint the picture that US growth remains steady, equity investors turned their attention to politics as the next catalyst for stock returns. The passage of the tax reform bill has been met with much investor skepticism, and stocks prices have reflected that evolving view throughout the month, with both the S&P 500 and the Dow down slightly through mid-month. However, as the likelihood of the bill passing gained momentum, stocks surged into month end, posting their second best monthly advance this year. Equity investors expect that lower tax rates for corporations should boost profitability for US companies, while lower repatriation
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taxes should incentivize companies to bring cash held abroad back to the US to invest in research and development or pay out dividends, providing a further boost to economic growth in either case.

International stocks, on the other hand, somewhat were mixed. Developed international equities finished the month with solid gains driven by Japanese equities, while those from EM countries experienced a late month selloff. European stocks declined more than 2% in euro terms for the month, as Eurozone economic growth accelerated, helping to boost the value of the euro. A more valuable euro puts downward pressure on the earnings of European exporters. In addition, the economic data also suggested that the European Central Bank was more likely to reduce its accommodative policies, further pressuring stocks in the region. Japan, however, surged in yen terms, despite geopolitical tensions rising after North Korea test launched yet another missile. Japanese equities performed well as they should benefit from continued global growth, are attractively priced relative to other equity markets and are under owned by global investors. EM stocks barely held on to positive gains, a result of the steep selloff to close out the month. EM equities suffered as Asian technology stocks paced declines.

Turning to bonds, Treasuries finished the month near flat. There was somewhat of a risk off tone to US bond markets during the month, as Treasuries performed best. Both investment grade and high yield markets declined, as credit spreads widened. Though, still near cycle lows, spreads moved higher as bond investors are increasingly concerned with credit risk. Spreads represent the added yield over Treasuries, rewarding investors for taking credit risk, or the risk that a bond issuer cannot meet principal or interest commitments on a timely basis. Higher spreads suggest investors expect greater compensation to take that additional risk.

In addition, the Treasury yield curve flattened during the month. The difference between the yield on the 10-year and 2-year Treasury bonds narrowed to 63 bps from 77 bps at the start of the month. A flattening of the yield curve has historically been a harbinger of slower economic growth, although in this instance it is more likely the case that the short end of the curve is moving higher in reaction to further Federal Reserve rate hikes and the long end of the curve is reacting lower to still benign inflation readings.

Recessions do not typically occur without the yield curve inverting.

Broad commodity markets fell slightly, despite a solid rally in crude oil. Crude moved higher in anticipation of further production cuts by OPEC and non-OPEC countries at their meeting on November 30. The market was expecting a nine-month cut, inclusive of OPEC members Libya and Nigeria, who were not part of the original agreement. In addition, Russia agreed to the extension cuts, in spite of comments leading up to the meeting that further cuts may no longer be necessary to bring the oil market in balance. These actions combined to support the price of oil and should help to bring oil supplies globally lower in the coming months. Other energy commodities also posted positive returns, with natural gas up more than 6% in part due to colder than normal temperatures in the US. Industrial metals, on the other hand, fell modestly during the month, with copper down more than 2%. Concerns about the stability of the Chinese housing market took centerstage in the metals market, even though Chinese steel rebar futures surged. Fears about overcapacity loomed large during the month, even though supplies have been reduced this year. Gold was largely flat, despite the North Korea missile launch. Agricultural commodities were mixed, as Corn and Wheat fell on supply concerns, but Soybeans and Cotton rose, as planting estimates for both came in below prior readings.

Finally, interest in Bitcoin surged during the month, as the digital currency rose by more than 50%, at one point breaching the $10,000 value. Bitcoin was not alone in the cryptocurrency arena to see such large price spikes, as Ether also jumped. While not traditionally viewed as an asset class, the shear spike in interest this month was enough for a quick mention in this month’s update, as the CME Group announced plans for futures trading in Bitcoin last month.

Should you have any questions about this update or your portfolio, please do not hesitate to contact your Portfolio Manager or Trust Officer.
Unless otherwise noted, performance and return data sourced from Bloomberg, LP as of November 30, 2017.

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This is only an opinion and not a prediction or promise of events to come.

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