Winslow, Evans & Crocker, Inc.[SM]

OCTOBER 2017 GLOBAL ECONOMICS & CAPITAL MARKET COMMENTARY

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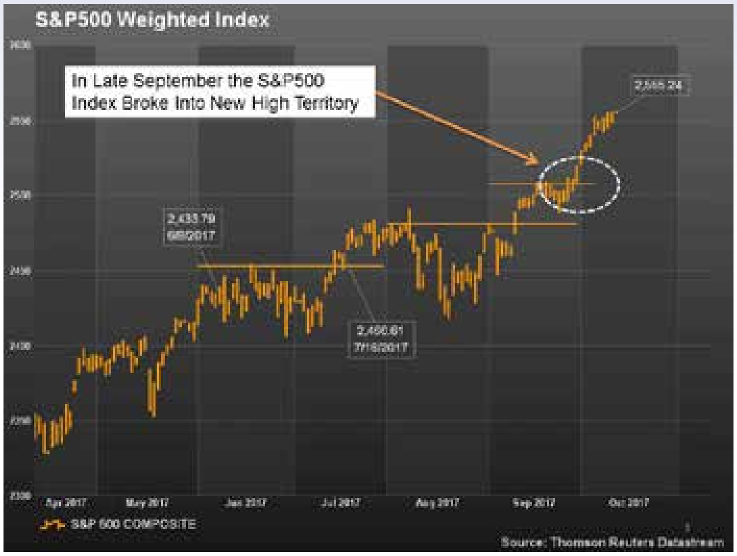
Market Barometer Updates: Leading Indicators, Valuation and Increasing Inflation

In last month's publication we outlined several of our market barometer indicators and found that none were signaling the onset of a bear market. Although the S&P500 was flat for the month of August it rose about 2% in September and continues to rise as of this writing in October. As we will discuss below many of these indicators have, in the interim, improved markedly.

CHART 1

1



CHARTS 2-3

As you can see in Charts #1 and #2 the S&P500 has broken out to new highs this past month in both the market capitalization weighted index and the equal weighted index. This is indicative of broad market strength.This is further confirmed by the fact that both the measures of market breadth and market momentum have been moving up together, Chart #3. You can also see in Chart #3 that, in the late 1990’s, the market’s breadth had collapsed while the market continued to go up. This signaled that the rally was shallow and likely to be short lived.

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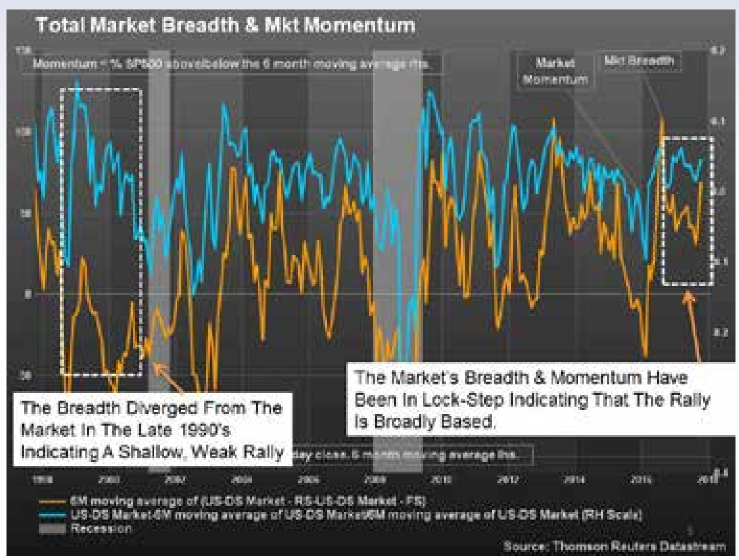

CHARTS 4-5

We pointed out last month that the market's progress has been driven by earnings, as shown in Chart #4, rather than valuation. As shown in Chart #5, the market's twelve month forward price earnings ratio has remained in a narrow range of between 17.3x to 18x since the beginning of the year. This ratio may break out to the upside as the domestic and global leading indicators continue to strengthen.

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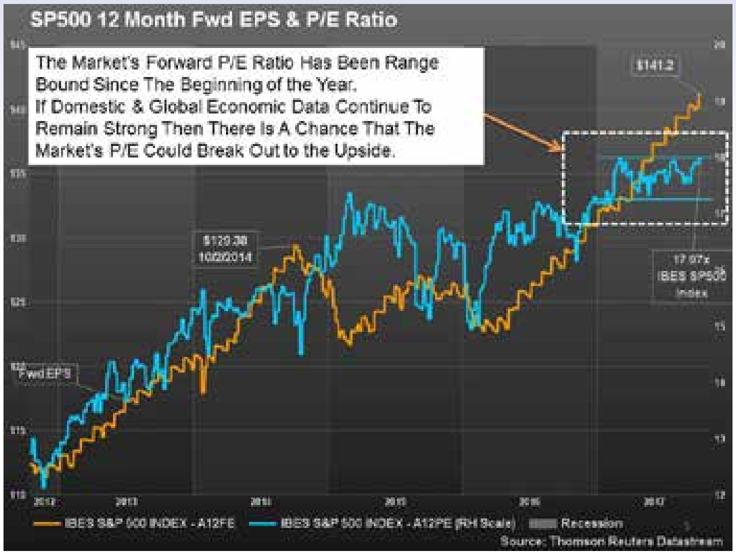

CHARTS 6-7

One of the domestic leading indicators that we mentioned last month is the ISM Manufacturer's Survey which, in September, hit a new high for this economic cycle, Chart #6. This chart demonstrates the very strong correlation this survey has with the growth in the market's earnings and, if the past correlations hold, is pointing to even stronger growth over the next quarter. Adding to this economic tailwind is the fact that global leading indicators are also at multi-year highs, Chart #7.

Our conclusion from the above observations is that we are not nearing a recession that could derail the equity markets. There will certainly be corrections but, for now, the underpinnings of the market remain very sound.

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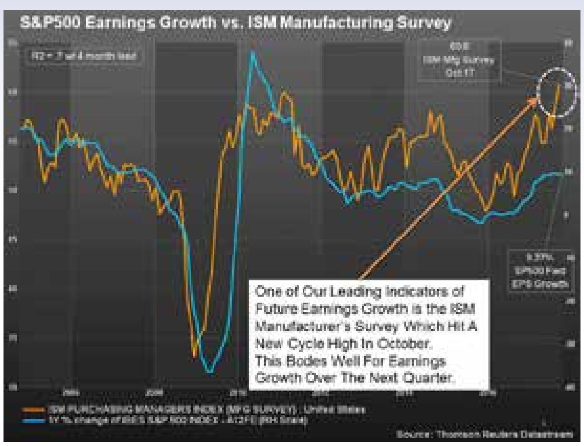

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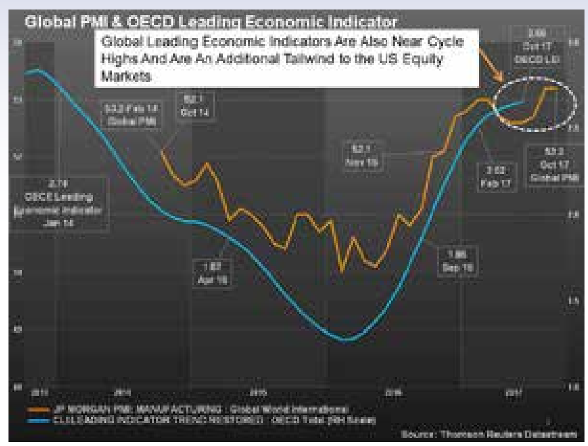

CHARTS 8-9

In last month's report we also explored the mystery of why inflation has remained so low in the face of strengthening economic data and examined a number of leading indicators that could warn us of a change. In the interim a number of these indicators have, indeed, begun to signal that inflation should soon be increasing. The first indication of this is that we had a strong uptick in the growth of Average Hourly Earnings in the September non-Farm Payrolls report to +2.54% year/year, Chart #8. This chart also shows that the number of job openings, the JOLTS report, is at a record high which implies that wages should continue to increase. Two other non-labor related leading indicators of inflation are the Producers Price Index (PPI) and the ISM Prices Paid Survey.

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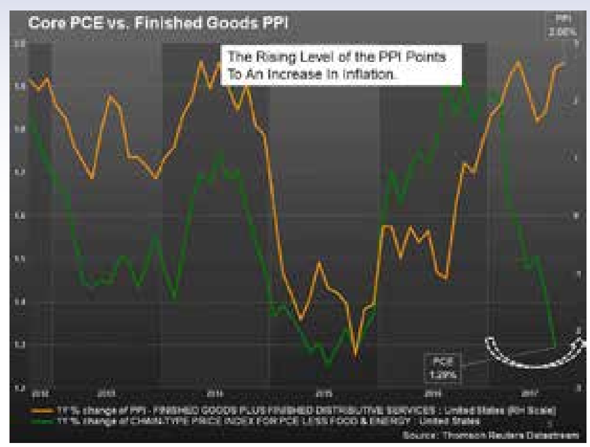

CHARTS 10-11

In Charts #9 and #10 we have compared these two time series to the core Personal Consumption Expenditures (PCE) price index, the US Federal Reserve's favored measure of inflation. Both the PPI and the ISM survey are at or near five year highs and imply a strengthening in the PCE inflation data over the next quarter. Chart #11 demonstrates how interest rates and inflation expectations have risen over the past month in response to stronger economic data and leading inflation indicators.

In conclusion, we are maintaining our position that the underpinnings of the equity markets and the economy remain solid. We are also of the opinion that inflation will be increasing over the next several quarters as the economy gets stronger and the tight labor market places upward pressure on wages. We therefore maintain our overweight positions in equities and, for fixed income, we have a short duration bias.

Please consult with your investment advisor if you would like to discuss how the above comments may impact your portfolio.

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