Schroeder | Capital Management, LLC
Global Investment

Investment Review and Outlook – Summer 2017

The American consumer appears to be more cautious of late. First, it was the carmakers reporting lower sales for June and revising their 2017 forecasts downward. Then, it was the retail sector that posted declining activity at restaurants, sporting goods outlets, and department stores. Finally, a recent report showed a drop in consumer sentiment.

Elsewhere, much of the economic picture is better. In June, U.S. industrial production advanced nicely, the second solid improvement in three months, while factory capacity utilization was higher. Housing starts and building permits also rose during June. Finally, employment numbers contained a positive surprise in job growth for the month with upward revisions for both April and May and a modest rise in wages.

Encouraging as these trends are, we are being cautious in looking out over the next several months. For over a year, the economic expansion has been a bit inconsistent with strong reports often followed by readings not as robust. This occurred again during the second quarter. The expansion continues to proceed in underwhelming fashion and the absence of excesses likely explains the longevity of the upturn.

On balance, we think the economy will hold its own during the balance of 2017. Our sense is that business activity will strengthen during the third and fourth quarters, despite some retracement in consumer spending, enabling GDP growth for the full year of about 2.2% compared with 1.6% in 2016.

Significantly important, as an influence on the level of economic expansion that occurs during 2018, will be Federal Reserve policy as it attempts to unwind years of extensive monetary accommodation, without breaking the economy's forward momentum. Today, the Fed released the following statement:

> *"In view of realized and expected labor market conditions and inflation, the Committee decided to maintain the target range for the federal funds rate at 1 to 1-1/4 percent. The stance of monetary policy remains accommodative, thereby supporting some further strengthening in labor market conditions and a sustained return to 2 percent inflation."*

Our sense is that the Fed will continue to tighten the monetary reins in small, regularly spaced intervals over the next 18 to 24 months with the next increase possibly coming toward the end of 2017.

In addition to Fed policy, enacting stimulative proposals advocated by the Trump Administration will be very important to 2018 GDP growth. Approval of a new tax bill for both individuals and corporations, including a tax repatriation plan for business assets held abroad, and a broad-based infrastructure bill that encourages capital spending and job growth, would be very positive developments.

Meanwhile, corporate earnings reports for the recently concluded second quarter are largely exceeding expectations. A continuing, solid showing on this front is important for the stock market bulls to be reassured. The stock market retains its resilience, with equities extending their gains on good news and often rebounding quickly when reports disappoint, whether related to the economy, global matters, or domestic political events. This sequence suggests decent further staying power for the U.S. equity market.

Investment Strategy: We think the careful addition of quality stocks with strong fundamentals, especially in selective overseas markets where economic development is improving, remains a prudent investment strategy. Mindful of the longevity of the present bull market run, our research currently favors revisiting healthcare, selected financials, industrials (aerospace/defense, machinery, transportation) and some technology issues. Many companies within these industries appear well-poised to have continuing success, developing above average revenues and profits for the balance of 2017 and into 2018.

G. Frederick Schroeder, CFA
President and Chief Investment Officer

July 26, 2017