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Outlook as of July 2017

WORLD ECONOMY

- Most countries around the world continue to enjoy non-inflationary economic growth with very little near-term recessionary risk, despite the prevailing notion that it is getting rather late in the cycle of recovery and expansion from the 2007/2008 global financial crisis.
- The US economy most likely needs the jolt of fiscal stimulus promised in the election to break out of the agonizingly slow growth in which it is currently mired. Expansionary government tax and spending policies can help offset the monetary policy tightening being conducted by the Fed.
- Surprisingly strong first half growth in both the UK and continental Europe may slow somewhat in the second half, due mainly to the impact of lower oil prices on the UK and slowing export growth caused by currency strength in Europe.
- Monthly economic statistics in Japan have been unusually volatile, particularly in the capital spending sectors. The overall economy should grow 1.0% to 1.5% this year, but GDP growth remains vulnerable to the impact of the strong yen in the near term, as well as to the country's unfavorable demographic situation in the long run.
- The Chinese government appears committed to holding economic growth to 6.5% for all of 2017. Inventories and employment continue to contract as the previous over- investment in manufacturing capacity is corrected, but continued government spending should prevent any near term collapse, which could roil the global economy and markets.

MONETARY POLICY & CURRENCIES

- In its quest to normalize monetary policy after a decade of unprecedented ease, the Federal Reserve must tighten in a slow growth environment with very few signs of inflation. Markets will be very sensitive to the delicate implementation of this task. Thus, policymakers need to be cautious and very clear in their intent as they gradually raise rates and reduce the Fed's bloated balance sheet.
- Similarly, the ECB needs to be cautious about its messaging around the removal of quantitative easing in the Eurozone. We do not expect an announcement of plans to taper bond purchases until the end of the year.
- Despite recent inflationary pressures, the Bank of England should hold steady to current rate policy, as lower energy prices and the strengthening pound should mitigate the rising prices.
- The Bank of Japan will continue on its current easing path as economic growth is not expected to be strong enough to reach the 2% inflation goal. Continued yen appreciation would be particularly damaging in this growth-challenged economy.
- The dollar has weakened considerably year-to-date on slower US relative economic growth, disappointment on the outlook for fiscal policy expansion, and a cautious Fed tightening message. With US GDP growth expected to improve in the second half of the year, we expect the dollar to move higher against most currencies, although we are nearing the end of the long bull market cycle.

BOND MARKETS

- The Treasury yield curve steepened a bit at the end of June, which should calm concerns that a flatter curve is a harbinger of recession. Fed tightening and balance sheet reduction should cause rates to increase across the maturity spectrum.
- The sharp decline in energy prices in June is beginning to pressure the High Yield asset class, which has a roughly 15% weighting in energy-related bonds. Caution is warranted in the space, although credit quality remains strong outside energy and energy producers have notably reduced their cost structure to where they are largely profitable at current price levels.
- Outside some of the high profile issuers with daunting pension obligations, municipal credit conditions are favorable and municipal yields across the maturity curve should move in tandem with changes in Treasury yields.
- Current yields on most developed market debt obligations are too low to warrant the risk of a spike in yields caused by improved economic growth or unanticipatedly early monetary policy tightening by their central banks.
- The controlled slowdown in China and the gradual nature of Fed tightening have allowed emerging markets debt to produce strong returns compared to other fixed income asset classes. The yield advantage to government bonds should continue to attract investors over the coming months.

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EQUITY MARKETS

- Halfway through 2017, US equity markets are already close to their year-end targets. Any further multiple expansion will be dependent on the prospect of stimulative fiscal policy being passed by Congress by the start of 2018, to offset the impact of the monetary policy normalization already in process.
- European equities have generally outperformed other developed markets year-to-date, due to continued extreme monetary accommodation, populist defeats in recent elections, and strong earnings aided by the weaker currency last year. While relative performance contracted a bit last month, these fundamental factors should continue to drive equity performance.
- Cheap valuations are attracting investors to Japanese equities where the dominant large cap companies benefit from the improved global economic growth environment. We continue to believe that any further equity appreciation is dependent upon a much weaker yen, to allow export growth to compensate for weak domestic spending
- Renewed rumblings of looming protectionist measures out of Washington could pressure emerging markets equity prices over the coming months. Lower commodity prices are another near term headwind to the asset class.

ALTERNATIVES & COMMODITIES

- The OPEC production cuts announced earlier in the year should prevent oil prices from repeating the sharp declines experienced in early 2016. With many overseas exporters reliant on sales to meet their domestic budget obligations, the global supply overhang, coupled with continued cost reductions by US shale producers, should keep prices contained for the balance of the year.
- Gold prices rose earlier in the year on heightened growth and inflationary expectations; however, the reality of low overall inflation and moderate economic growth should keep prices contained around current levels.
- We expect industrial metals prices to drift higher in the coming months, buoyed by synchronous global growth and expectations that Congress will pass a large US infrastructure investment program by year-end. This should counteract any softness due to reduced demand from China.
- Persistently low market volatility has stymied many hedge fund managers since the financial crisis. Policy normalization by central banks should create a more favorable environment for investors seeking to mitigate risks from unstable markets or policy/geopolitical uncertainty.
- High asset valuations make it difficult for private equity managers to buy assets at reasonable prices. We maintain our focus on seasoned, disciplined managers and continue to seek value in dislocated markets and those experiencing disruption from technological or regulatory change.

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Ben Pace is the Chief Investment Officer and a member of the Investment Committee. Prior to joining Cerity Partners, Benjamin Pace was Chief Investment Officer and Head of Global Investment Solutions for Deutsche Bank Private Wealth Management in the U.S. Ben has more than 25 years of experience in investment management. Prior to joining Deutsche Bank in 1994, he managed equity income funds for two investment organizations.

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