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WEALTH ADVISORS

Forward Thinking. Mutual Success. Peace of Mind.

Third Quarter 2017

Market Update & Outlook

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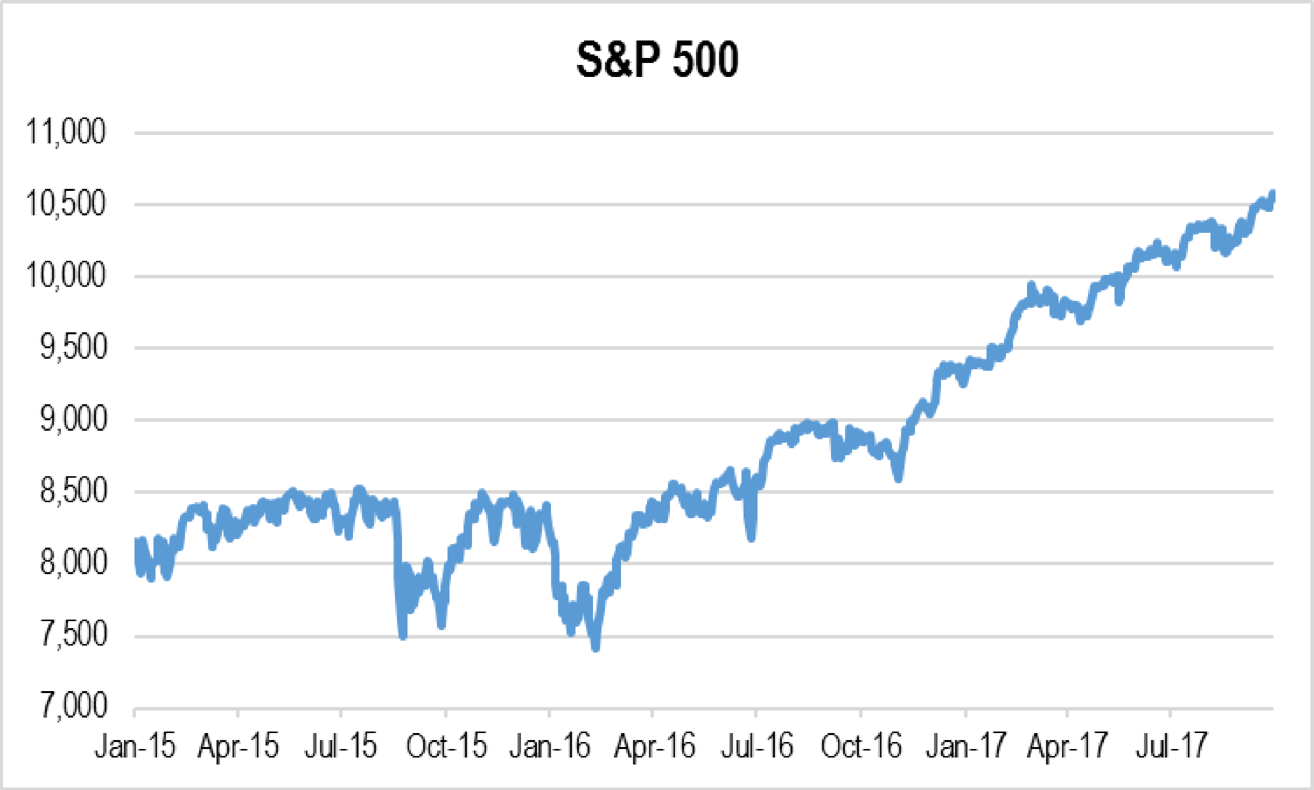
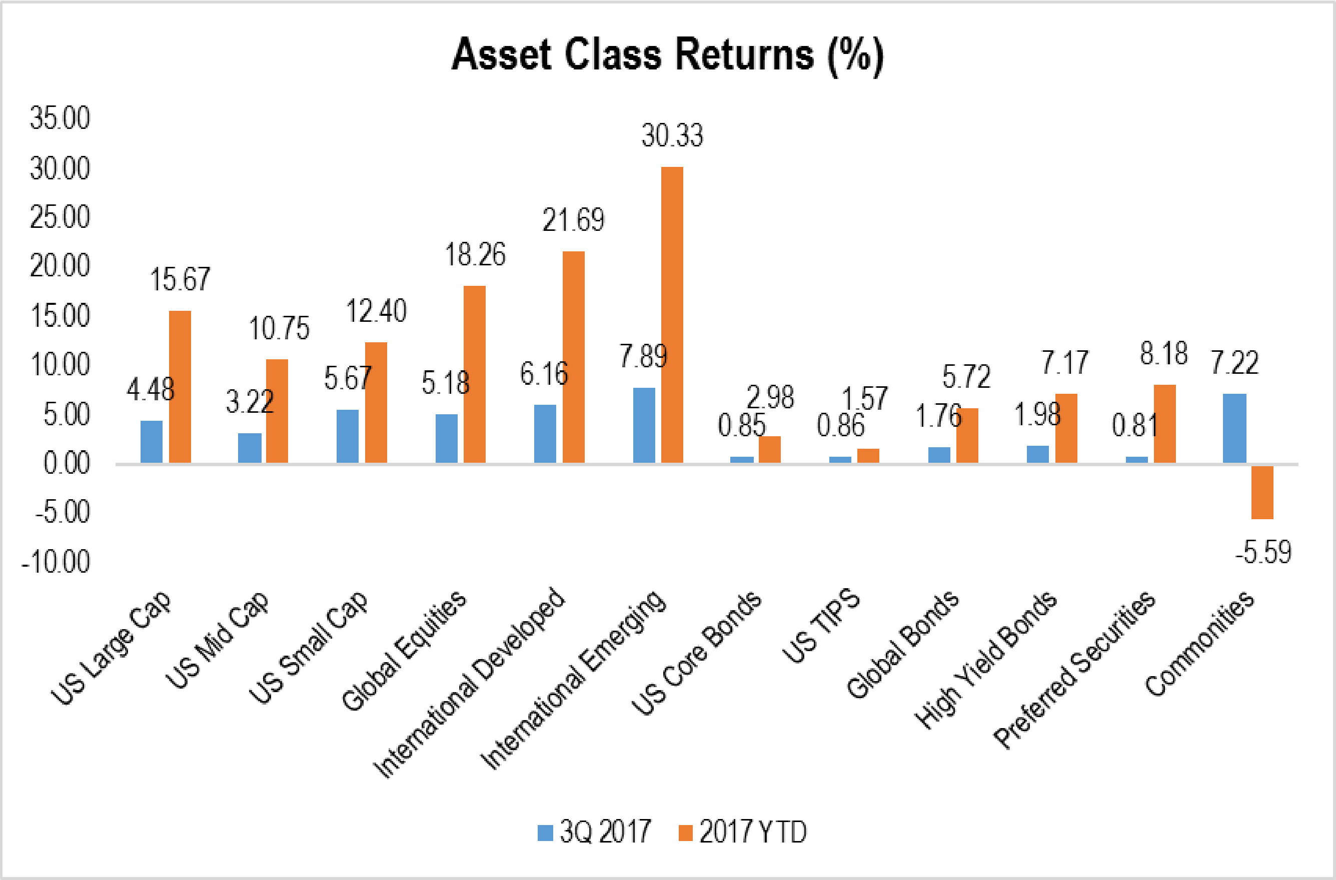
Q3'17: S&P 500 Continues Winning Ways



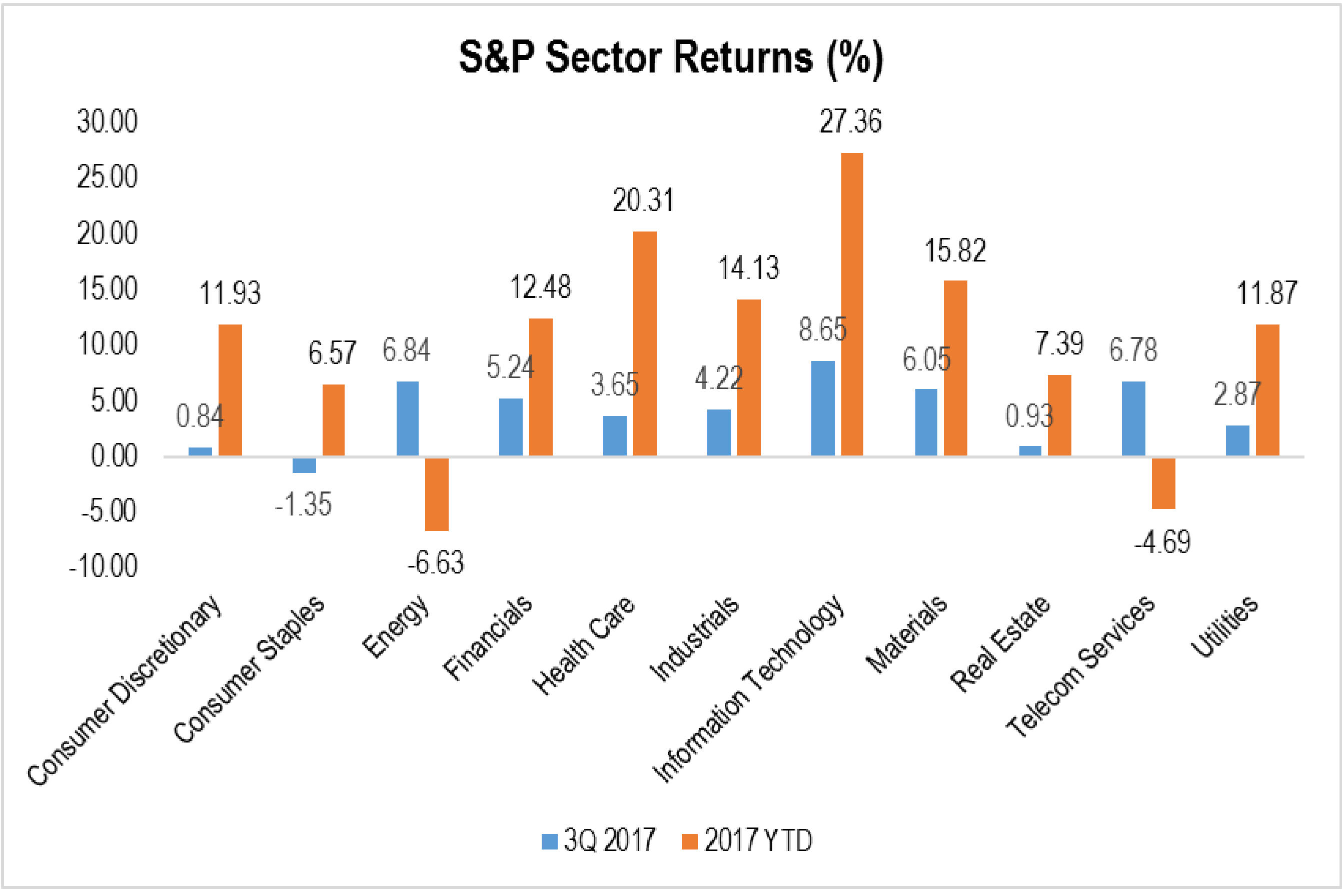
Source: Morningstar Direct

Strong Performance Across Asset Classes



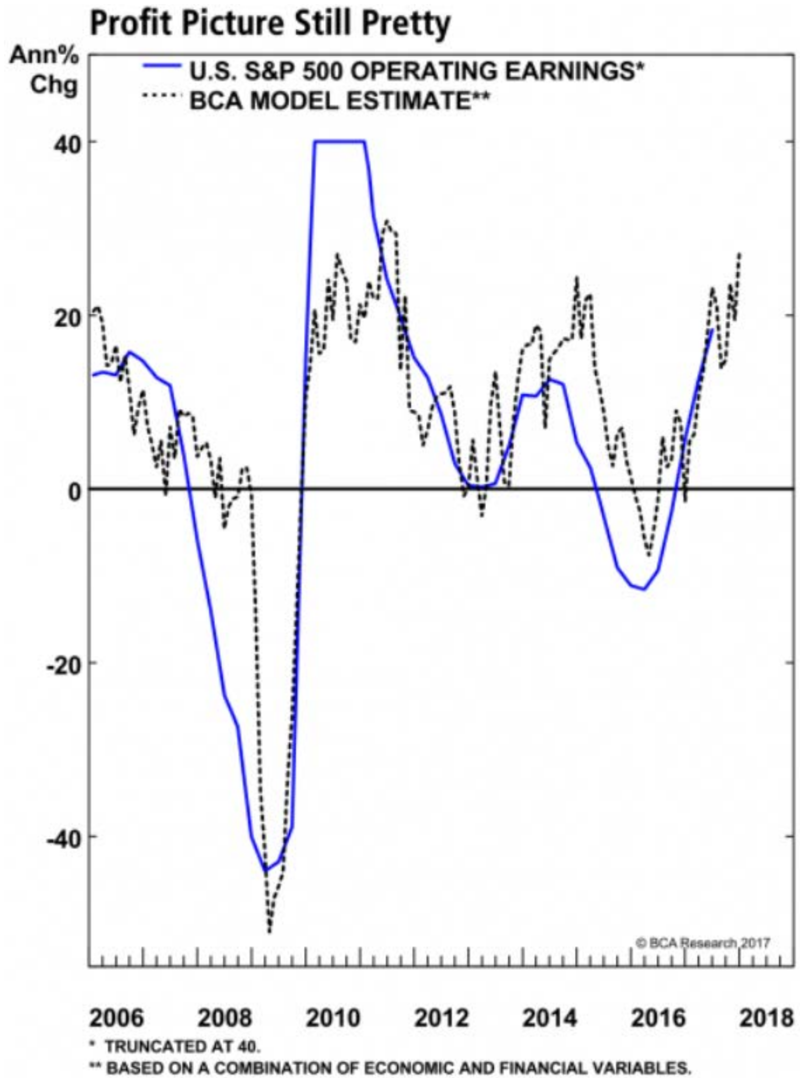
Source: Morningstar Direct

Some Lagging Sectors Did Well in Q3

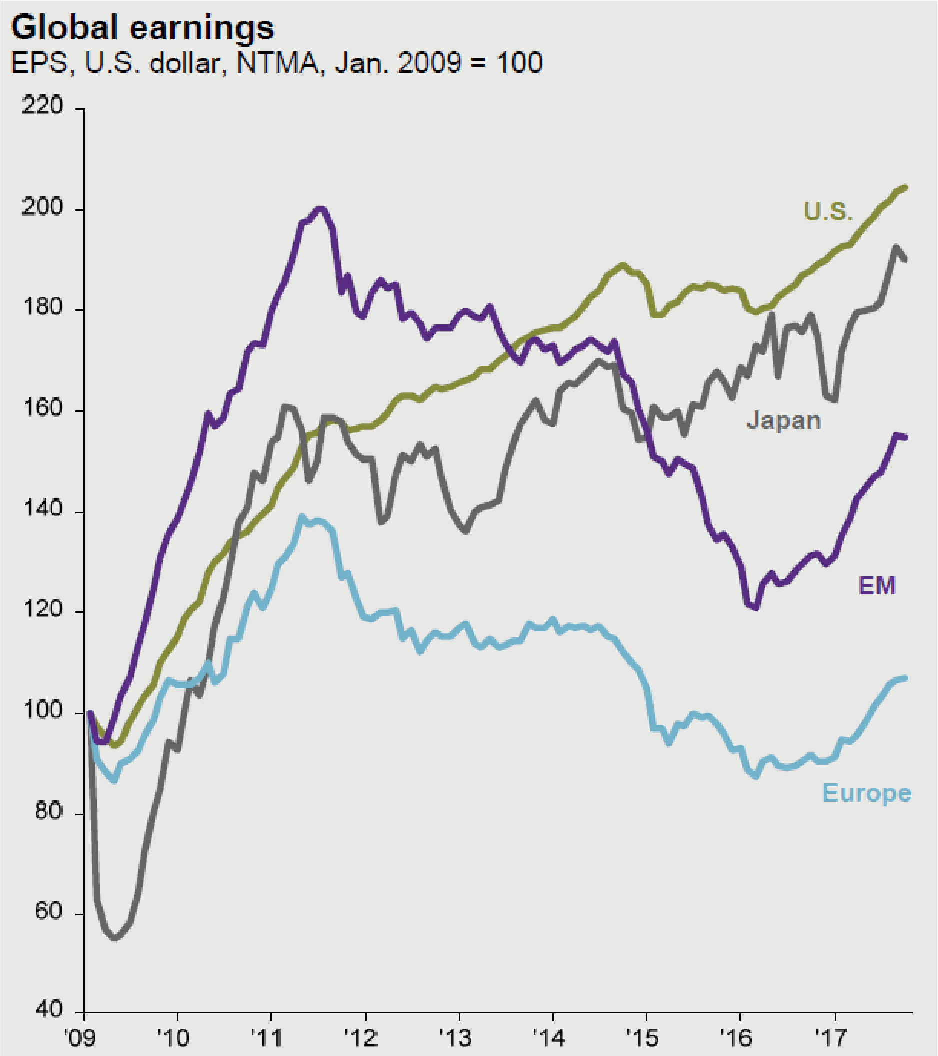


Source: Morningstar Direct

Earnings Driven Recovery

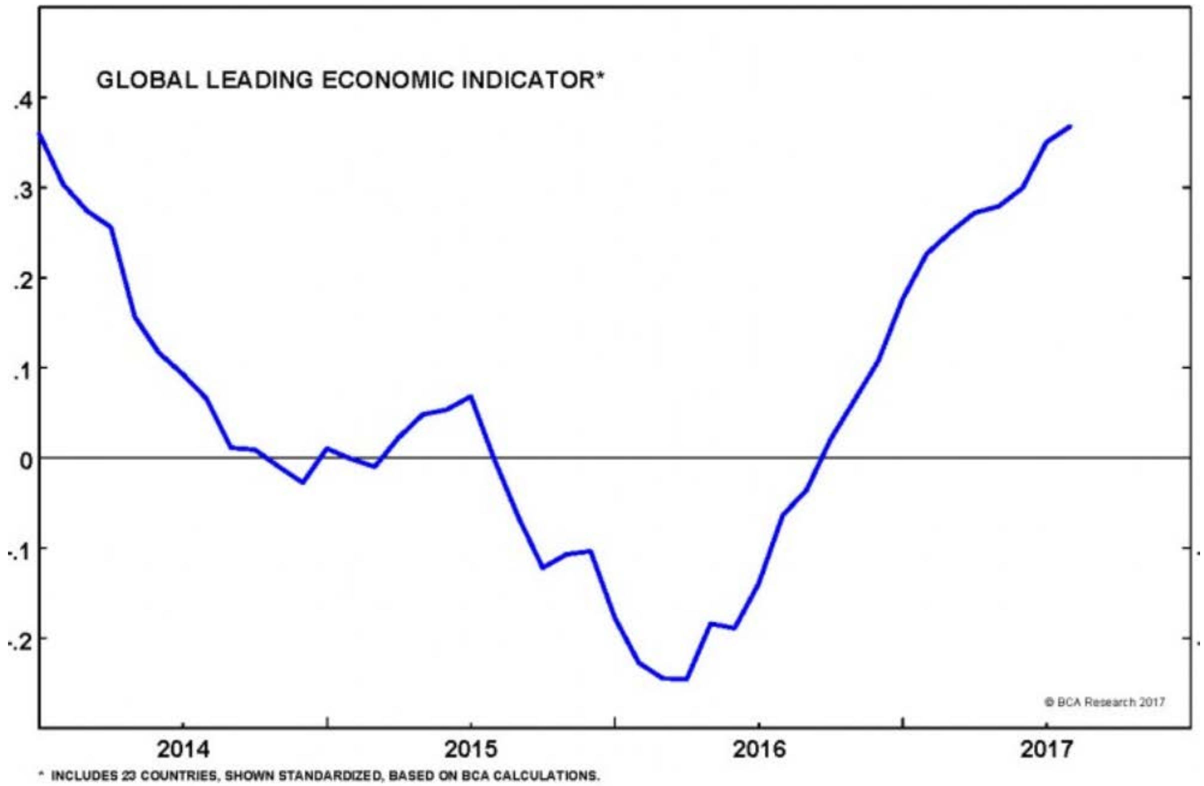


Earnings Driven Recovery, Both Here and Abroad



Source: JPMorgan

It’s the Economy – Positive Leading Indicators



It’s the Economy – Stellar Recent Anecdotes

- Services ISM at a 12-yr. high of 59.8
- Manufacturing ISM at 60.8, activity at 13-yr. high
- Durable goods orders up 2%
- Latest read on auto sales stronger than expected, best in 12 months
- Unemployment rate 4.2%, wages growing

It's the Economy – Manufacturing Momentum

Global Purchasing Managers' Index for manufacturing

		2015 Oct	2015 Nov	2015 Dec	2016 Jan	2016 Feb	2016 Mar	2016 Apr	2016 May	2016 Jun	2016 Jul	2016 Aug	2016 Sep	2016 Oct	2016 Nov	2016 Dec	2017 Jan	2017 Feb	2017 Mar	2017 Apr	2017 May	2017 Jun	2017 Jul	2017 Aug	2017 Sep
	Global	51.0	51.0	50.7	50.9	50.0	50.6	50.2	50.1	50.4	51.0	50.8	51.1	52.0	52.1	52.7	52.8	53.0	53.0	52.7	52.6	52.6	52.7	53.2	53.2
	Developed Markets	52.5	52.3	52.0	52.1	50.8	50.9	50.5	50.4	51.2	51.5	51.2	51.5	52.6	53.0	53.8	54.2	54.1	53.9	54.1	54.1	53.9	54.0	54.2	54.6
	Emerging Markets	49.0	49.2	49.0	49.4	48.9	50.2	49.5	49.5	49.3	50.3	50.1	50.3	51.0	50.8	51.1	50.8	51.3	51.6	50.9	50.6	50.8	50.9	51.7	51.3
Developed	U.S.	54.1	52.8	51.2	52.4	51.3	51.5	50.8	50.7	51.3	52.9	52.0	51.5	53.4	54.1	54.3	55.0	54.2	53.3	52.8	52.7	52.0	53.3	52.8	53.1
	Canada	48.0	48.6	47.5	49.3	49.4	51.5	52.2	52.1	51.8	51.9	51.1	50.3	51.1	51.5	51.8	53.5	54.7	55.5	55.9	55.1	54.7	55.5	54.6	55.0
	Japan	52.4	52.6	52.6	52.3	50.1	49.1	48.2	47.7	48.1	49.3	49.5	50.4	51.4	51.3	52.4	52.7	53.3	52.4	52.7	53.1	52.4	52.1	52.2	52.6
	UK	54.5	52.4	51.2	52.2	50.9	51.3	49.6	50.5	53.1	48.4	53.0	55.6	54.2	53.4	55.8	55.4	54.6	54.3	57.2	56.4	54.2	55.2	56.7	55.9
	Euro Area	52.3	52.8	53.2	52.3	51.2	51.6	51.7	51.5	52.8	52.0	51.7	52.6	53.5	53.7	54.9	55.2	55.4	56.2	56.7	57.0	57.4	56.6	57.4	58.1
	Germany	52.1	52.9	53.2	52.3	50.5	50.7	51.8	52.1	54.5	53.8	53.6	54.3	55.0	54.3	55.6	56.4	56.8	58.3	58.2	59.5	59.6	58.1	59.3	60.6
	France	50.6	50.6	51.4	50.0	50.2	49.6	48.0	48.4	48.3	48.6	48.3	49.7	51.8	51.7	53.5	53.6	52.2	53.3	55.1	53.8	54.8	54.9	55.8	56.0
	Italy	54.1	54.9	55.6	53.2	52.2	53.5	53.9	52.4	53.5	51.2	49.8	51.0	50.9	52.2	53.2	53.0	55.0	55.7	56.2	55.1	55.2	55.1	56.3	56.3
	Spain	51.3	53.1	53.0	55.4	54.1	53.4	53.5	51.8	52.2	51.0	51.0	52.3	53.3	54.5	55.3	55.6	54.8	53.9	54.5	55.4	54.7	54.0	52.4	54.3
	Greece	47.3	48.1	50.2	50.0	48.4	49.0	49.7	48.4	50.4	48.7	50.4	49.2	48.6	48.3	49.3	46.6	47.7	46.7	48.2	49.6	50.5	50.5	52.2	52.8
Emerging	China	48.3	48.6	48.2	48.4	48.0	49.7	49.4	49.2	48.6	50.6	50.0	50.1	51.2	50.9	51.9	51.0	51.7	51.2	50.3	49.6	50.4	51.1	51.6	51.0
	Indonesia	47.8	46.9	47.8	48.9	48.7	50.6	50.9	50.6	51.9	48.4	50.4	50.9	48.7	49.7	49.0	50.4	49.3	50.5	51.2	50.6	49.5	48.6	50.7	50.4
	Korea	49.1	49.1	50.7	49.5	48.7	49.5	50.0	50.1	50.5	50.1	48.6	47.6	48.0	48.0	49.4	49.0	49.2	48.4	49.4	49.2	50.1	49.1	49.9	50.6
	Taiwan	47.8	49.5	51.7	50.6	49.4	51.1	49.7	48.5	50.5	51.0	51.8	52.2	52.7	54.7	56.2	55.6	54.5	56.2	54.4	53.1	53.3	53.6	54.3	54.2
	India	50.7	50.3	49.1	51.1	51.1	52.4	50.5	50.7	51.7	51.8	52.6	52.1	54.4	52.3	49.6	50.4	50.7	52.5	52.5	51.6	50.9	47.9	51.2	51.2
	Brazil	44.1	43.8	45.6	47.4	44.5	46.0	42.6	41.6	43.2	46.0	45.7	46.0	46.3	46.2	45.2	44.0	46.9	49.6	50.1	52.0	50.5	50.0	50.9	50.9
	Mexico	53.0	53.0	52.4	52.2	53.1	53.2	52.4	53.6	51.1	50.6	50.9	51.9	51.8	51.1	50.2	50.8	50.6	51.5	50.7	51.2	52.3	51.2	52.2	52.8
	Russia	50.2	50.1	48.7	49.8	49.3	48.3	48.0	49.6	51.5	49.5	50.8	51.1	52.4	53.6	53.7	54.7	52.5	52.4	50.8	52.4	50.3	52.7	51.6	51.9

Source: JPMorgan

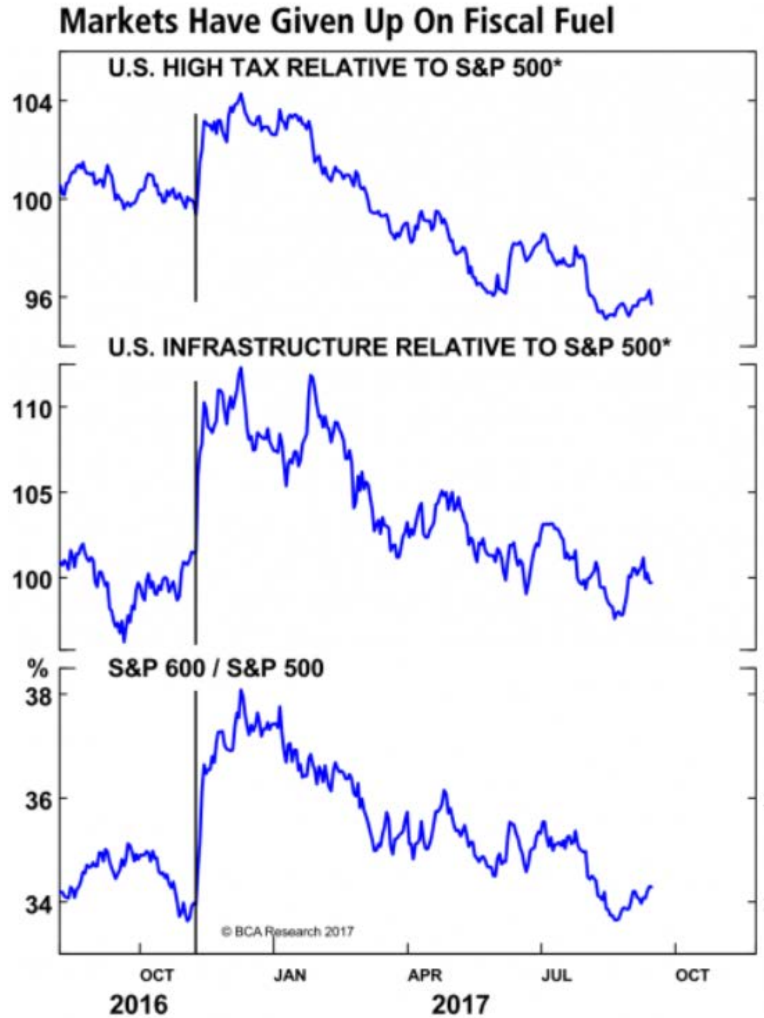
Earnings Growth Should Continue into Next Year

After three years of going nowhere, the earnings outlook is bright.

S&P 500 Consensus EPS	
2014	$119.31
2015	$118.48
2016	$119.10
2017E	$131.56
2018E	$146.30

Source: Thomson

Surprisingly, Fiscal Stimulus Has Not Materialized



* SHOWN REBASED TO AUG. 2016 = 100; SOURCE: GOLDMAN SACHS; BLOOMBERG FINANCE L.P.
NOTE: VERTICAL LINE DENOTES U.S. PRESIDENTIAL ELECTION DATE.

Lack of Stimulus Has Left Interest Rates Low…

Source: Federal Reserve Bank of St. Louis

…And Kept a Lid on Inflation

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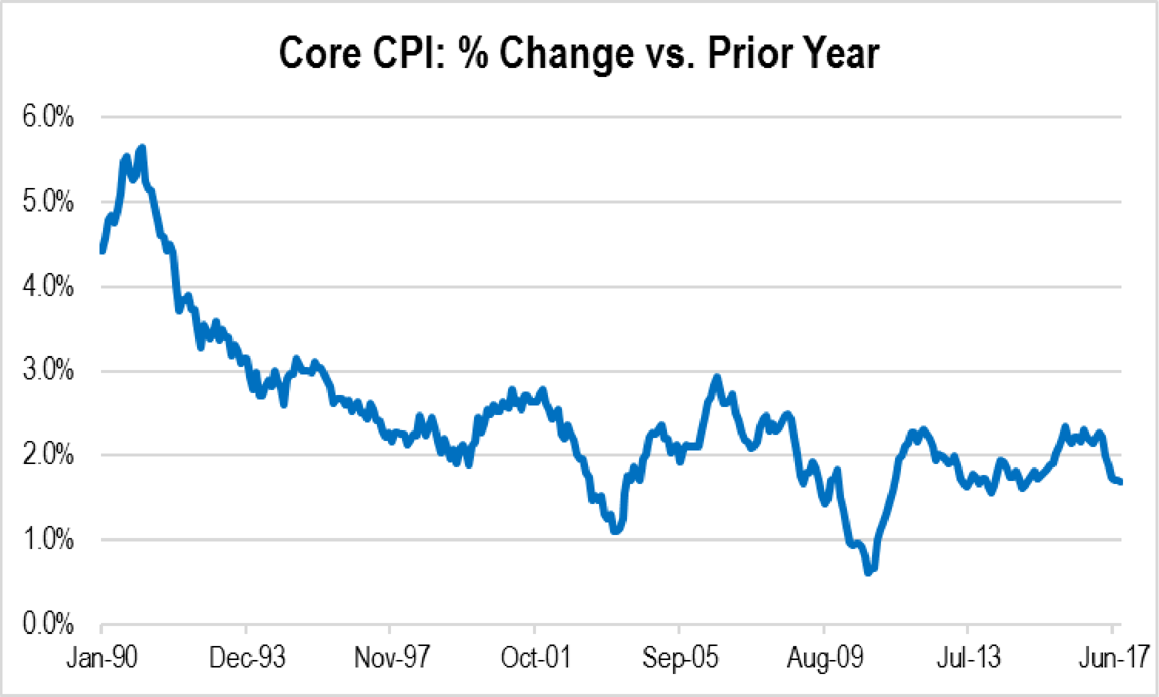
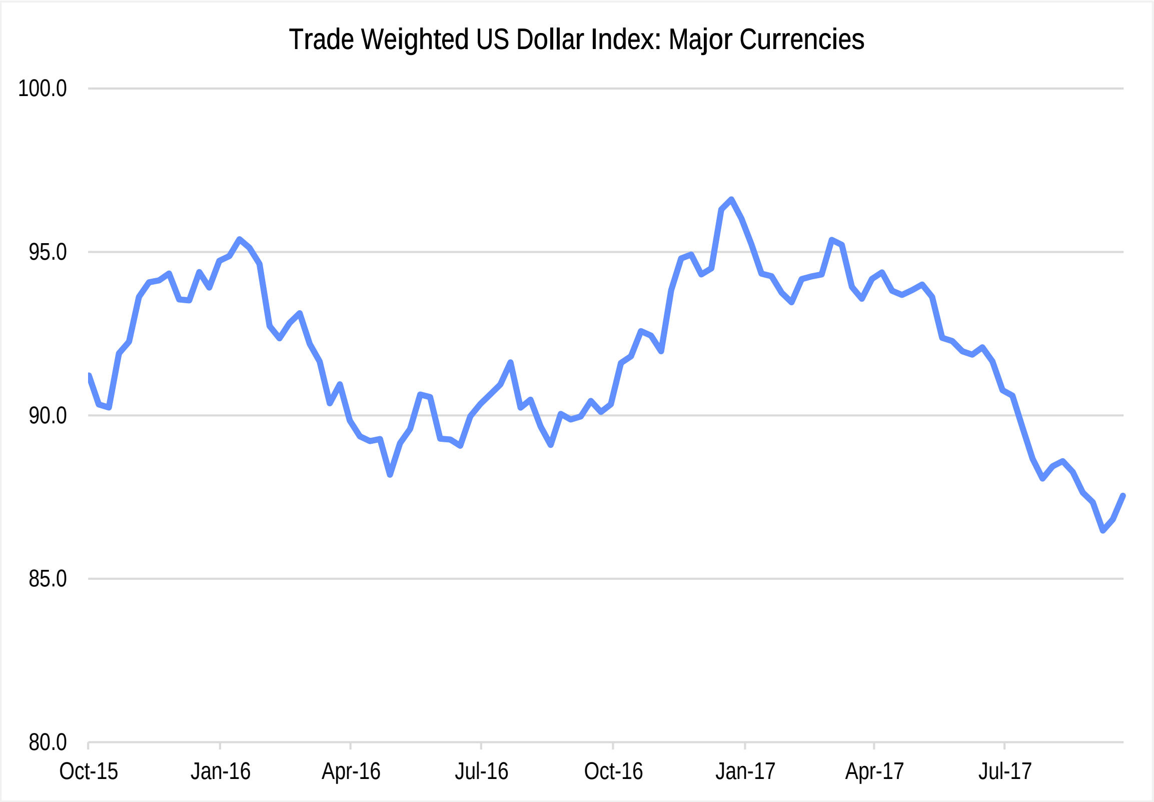


Source: Federal Reserve Bank of St. Louis

Dollar Surged After Election and Has Weakened Since

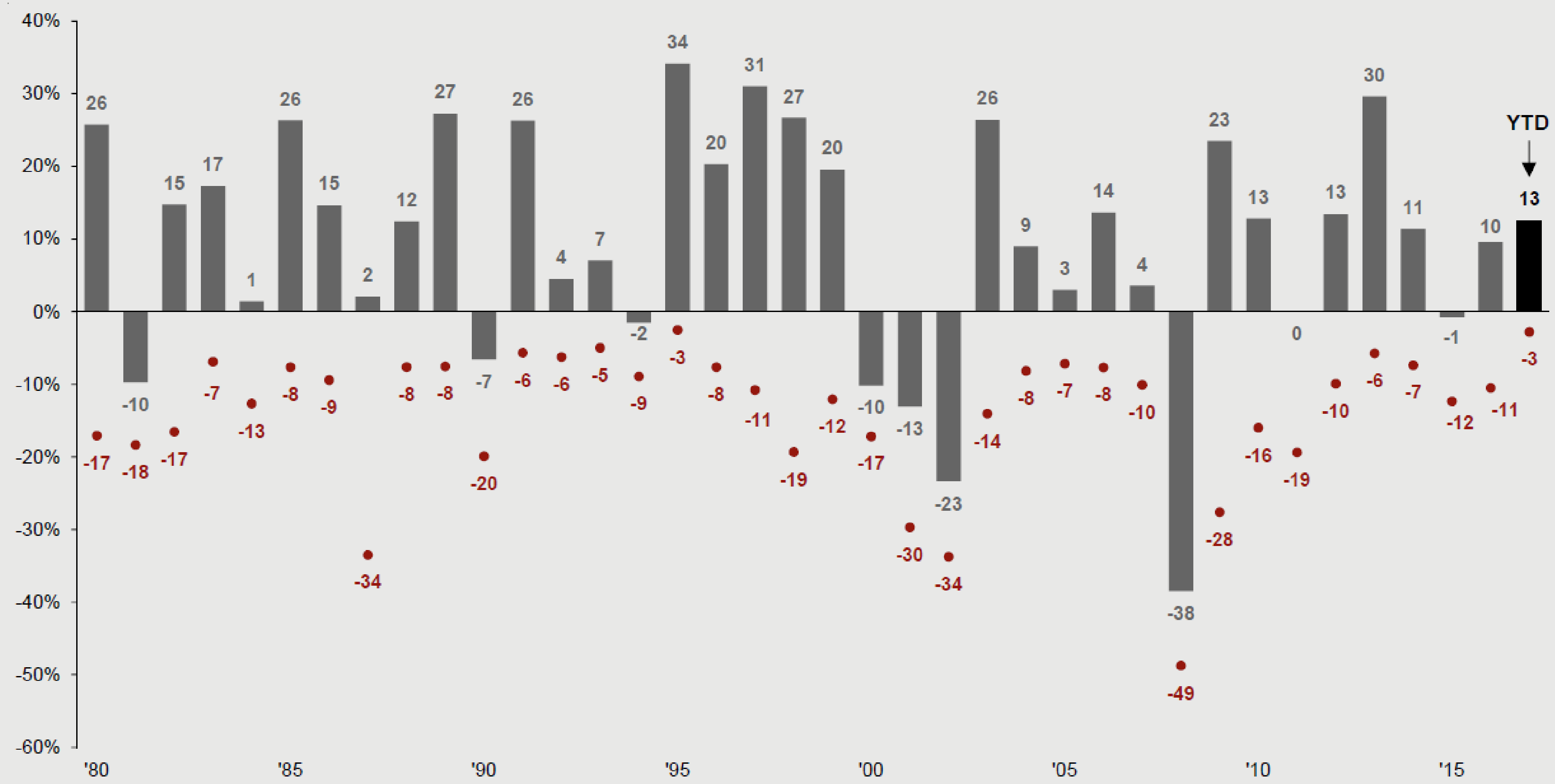


Source: Federal Reserve Bank of St. Louis

Keeping Your Balance – No Meaningful Drawdown This Year

S&P 500 intra-year declines vs. calendar year returns

Despite average intra-year drops of 14.1%, annual returns positive in 28 of 37 years



Source: JPMorgan

Keeping Your Balance – Portfolio Rebalancing

- Asset classes produce different returns over time that can change a portfolio's asset allocation, a concept known as "drift".

- The long run up in stocks can skew the intended risk/return characteristics of a portfolio. Portfolios should be reviewed regularly and rebalanced to recapture their original risk/return characteristics.

- Our research suggests that most investors do not rebalance, likely because it may seem counterintuitive to sell the winners and buy the laggards

- Rebalancing is a formal component of our investment process. In fact, where appropriate, we recently performed a portfolio rebalancing for our clients. This is an important tool we use to minimize risk relative to a portfolio's original targets and in the process, minimize surprises.

Heritage Market Views

Monetary Policy — **Neutral**

The Fed has raised the Fed funds rate three times since December. It passed on raising Fed funds at its most recent meeting but signaled that a December increase is likely. As expected, the Fed officially announced it is going to shrink its balance sheet. A tightening cycle has begun but is in the context of an improving economy. Moreover, interest rates are increasing from emergency levels struck during the financial crisis. Credible research shows that stock valuations will not be affected unless there is a substantial increase in rates. If inflation begins to percolate, the Fed would likely tighten more aggressively, which in turn could impact the outlook for equities.

Fiscal Policy — **Accommodating**

With another effort to repeal and replace ACA having failed, Congress has turned its attention to tax reform with the House presenting its plan. While the "Trump trade" has stalled, hopes for at least a cut in the corporate tax rate have started to rise. The current administration is business friendly and continues to use executive orders to push deregulation and some growth initiatives. Thus far, the handoff from monetary policy stimulus to fiscal policy stimulus has been botched.

Economic Fundamentals — **Positive**

Economic data broadly is improving. Second quarter GDP came in at 3.1%. vs. 1.2% in Q1. Manufacturing activity is at a 13-year high, service sector activity is at a 12-year high, auto sales are at a one-year high, durable goods orders are positive, and the unemployment rate keeps falling, now at 4.2%. Economic momentum is surprisingly strong.

Market Dynamics — **Positive**

Optimistic on growth both here and abroad. Elevated valuations in the U.S. imply muted returns but developed and emerging markets are trading more inexpensively. Earnings are in a synchronized global recovery and so are markets. There are few signs of speculative excess across asset classes.

U.S Equities — **Neutral**

The S&P 500 is trading at 18x 2017 earnings, about three percentage points higher than the long-term average multiple. Given elevated valuations, prospective returns are likely to be more muted. Importantly, the earnings outlook for next year is for continued growth that could be augmented by tax reform. In the context of improving earnings and still low interest rates, we see the market as reasonably priced but also see the potential for further gains next year. The Russell 2000 is trading at 25.1x earnings. Given the U.S.-centric nature of their business, these companies are expected to be the biggest beneficiaries of a cut in the corporate tax rate.

International Equities — **Positive**

The MSCI EAFE index is trading at a slight discount to the LT average multiple of around 16x. Various economic indicators are improving and earnings should improve. EM is through a four-year earnings recession and the profit outlook has improved markedly. EM is up almost 31% YTD, but the sector still trades for 12.8x earnings.

Bond Yields & Credit — **Neutral**

We continue to favor shorter durations as the path of least resistance for rates seems higher. Developed market yields are unattractive across the globe, and this continues to support a bid for US Treasuries. The expanded opportunity set to add income through country selection, including EM, and credit selection remains an attraction for global bonds. High yield spreads have narrowed and we are cautious on taking incremental credit risk but there is no recession in sight based positive economic fundamentals.

Commodities — **Neutral**

Oil inventories have become more favorable and OPEC seems inclined to keep cuts in place (even with the usual cheating) and the price of oil has moved back above $50. Given long-term supply/demand dynamics, most notably that it is fairly easy for nonconventional drillers in the U.S. to increase production, the price of crude is likely to remain in the $45-$55 range. Industrial commodities like copper have rallied recently based on the upturn in global economic activity.

U.S. Dollar — **Neutral**

Weakness year-to-date in the dollar has been surprising given interest rate differentials but a shifting focus to growth rate differentials may explain depreciation.

Disclosures

Past performance is no guarantee of future results. No assurance can be given that an investor will not lose invested capital. This performance is neither a composite performance nor actual performance experienced by any past or present client.

The “Hypothetical” or “Historical” performance is a simulated historical calculation of how this portfolio of managed assets would have performed over the period indicated. Performance calculations are based on the indicated asset weights presented and assume annual rebalancing. No annual rebalance is captured for time analysis periods less than one year in length. “Hypothetical” or “Historical” performance of the portfolio is shown Gross of the manager fees and Gross of Investment Advisory Fees. Performance of mutual funds is shown net of fees based on published expense ratios.

Definitions:

S&P 500: The Standard & Poor's 500 Index is an index of 500 stocks seen as a leading indicator of US equities and a reflection of the performance of the large cap universe, made up of companies selected by economists.

Russell 2000: The Russell 2000 index is an index measuring the performance approximately 2,000 small-cap companies in the Russell 3000 Index, which is made up of 3,000 of the biggest U.S. stocks.

MSCI ACWI: A market capitalization weighted index designed to provide a broad measure of equity-market performance throughout the world. The MSCI ACWI is maintained by Morgan Stanley Capital International, and is comprised of stocks from both developed and emerging markets.

MSCI EAFE: The MSCI EAFE Index serves as a benchmark of the performance in major international equity markets as represented by 21 major MSCI indexes from Europe, Australia and Southeast Asia.

Emerging Markets: Emerging Market Equity is represented by the MSCI Emerging Markets Index. The MSCI Emerging Markets Index is an index created by Morgan Stanley Capital International designed to measure equity market performance in global emerging markets. It is a float-adjusted market capitalization index that consists of indices in 23 emerging economies.

Investment Grade Corporates: Investment Grade Corporate bonds are represented by the iShares iBoxx $ Investment Grade Corporate Bond ETF. The iShares iBoxx $ Investment Grade Corporate Bond ETF seeks to track the investment results of an index composed of U.S. dollar-denominated, investment grade corporate bonds.

Global Bonds: Global bonds are represented by the BoAML Global Broad Market Index. The Global Broad Market Index tracks the performance of investment grade public debt issued in the major domestic and eurobond markets, including global bonds.

TIPS: Treasury Inflation Protected Securities are represented by the BBgBarc US Treasury US TIPS Index. The index includes all publicly issued, U.S. Treasury inflation-protected securities that have at least one year remaining to maturity, are rated investment grade, and have $250 million or more of outstanding face value.

High Yield Corporates: High Yield Corporates are represented by the BBg US Corporate High Yield Index. The Bloomberg Barclays U.S. Corporate High Yield Bond Index is composed of fixed-rate, publicly issued, non-investment grade debt, is unmanaged, with dividends reinvested.

Preferred Stock: Preferred stock is represented by the BoAML: Preferred Stock Adjustable Rate Index.

US Treasurys: US Treasurys are represented by the BBgBarc Aggregate Bond Treasury Index.

Commodities: Commodities are represented by the Bloomberg Commodity Index.

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