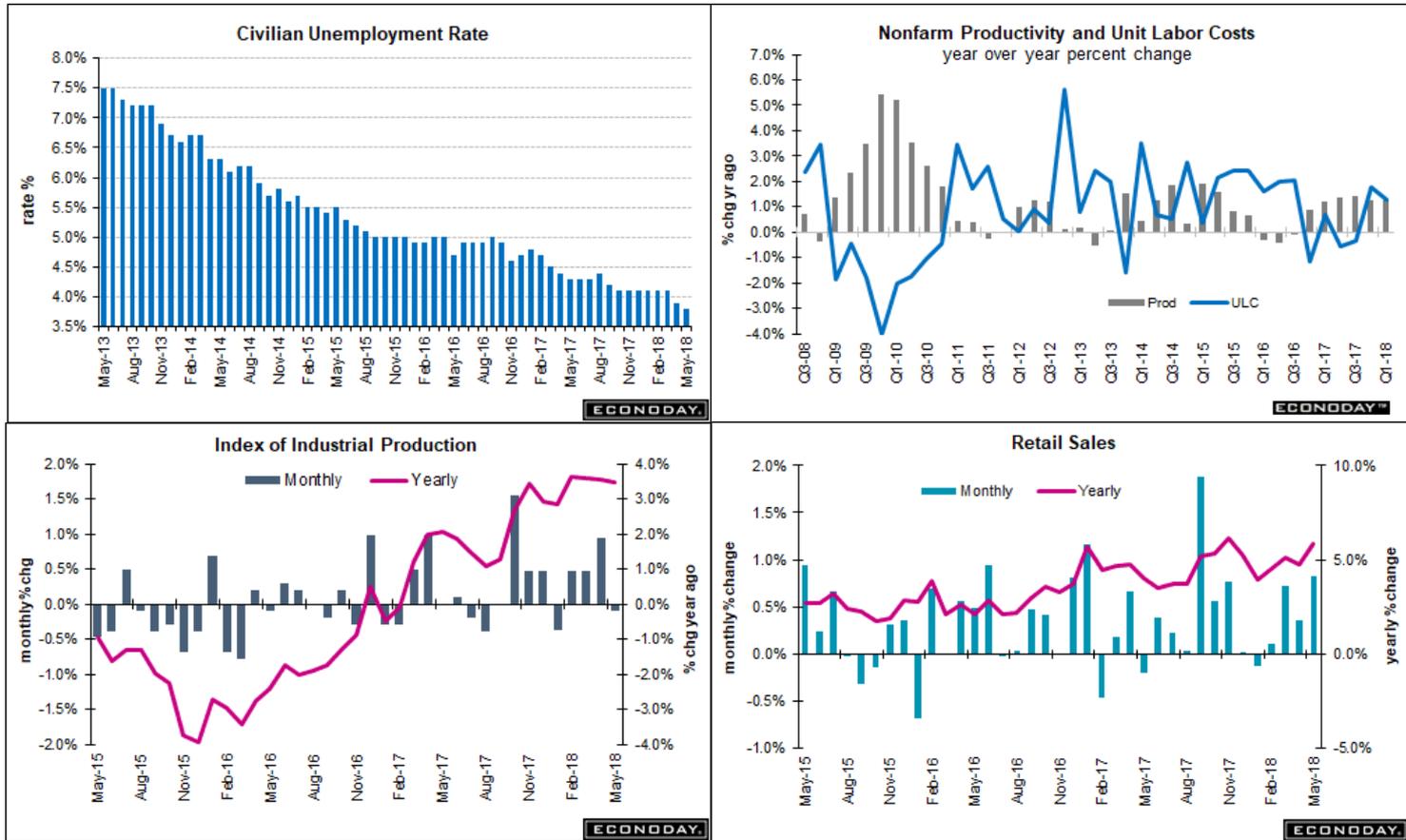


## Interesting Charts and Commentary

The U.S. economy continues to chug along steadily. This economic expansion, while less robust than historical standards, is now one of the longest in history. Unemployment has reached decade lows while industrial production and productivity continue to increase. Even retail sales growth has picked up.



The Small Business Optimism Index increased in May to the second highest level in the NFIB survey's 45-year history.

- Compensation increases hit a 45-year high at a record net 35 percent.
- Positive earnings trends reached a survey high at a net three percent.
- Positive sales trends are at the highest level since 1995.
- Expansion plans are the most robust in survey history.
- A net 19 percent of small business owners are planning price increases, a signal of a strong economy.
- A net three percent reported positive profit trends, up four points and the best reading in the survey's history.
- In addition, a net 15 percent reported higher nominal sales in the past three months, the sixth consecutive strong month for sales.

### Small Business Optimism

*Owners reporting Increased Profits, Compensation, & Plans to Expand*

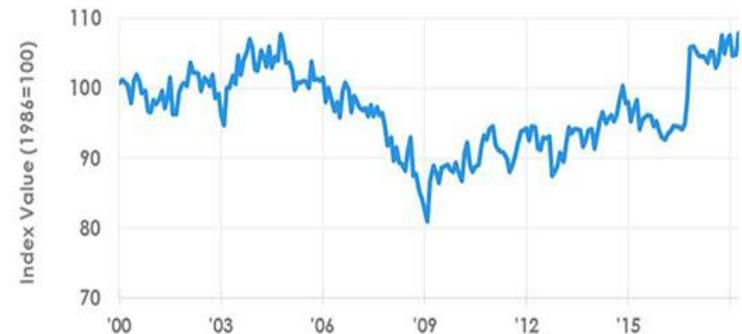
Index Component	Net %	Change From Apr.
Plans to Increase Employment	18%	▲ 2
Plans to Make Capital Outlays	30%	▲ 1
Plans to Increase Inventories	4%	▲ 3
Expect Economy to Improve	37%	▲ 7
Expect Real Sales Higher	31%	▲ 10
Current Inventory	-4%	▬ 0
Current Job Openings	33%	▼ -2
Expected Credit Conditions	-5%	▲ 1
Now a Good Time to Expand	34%	▲ 7
Earnings Trends	3%	▲ 4



NFIB.com/sboi

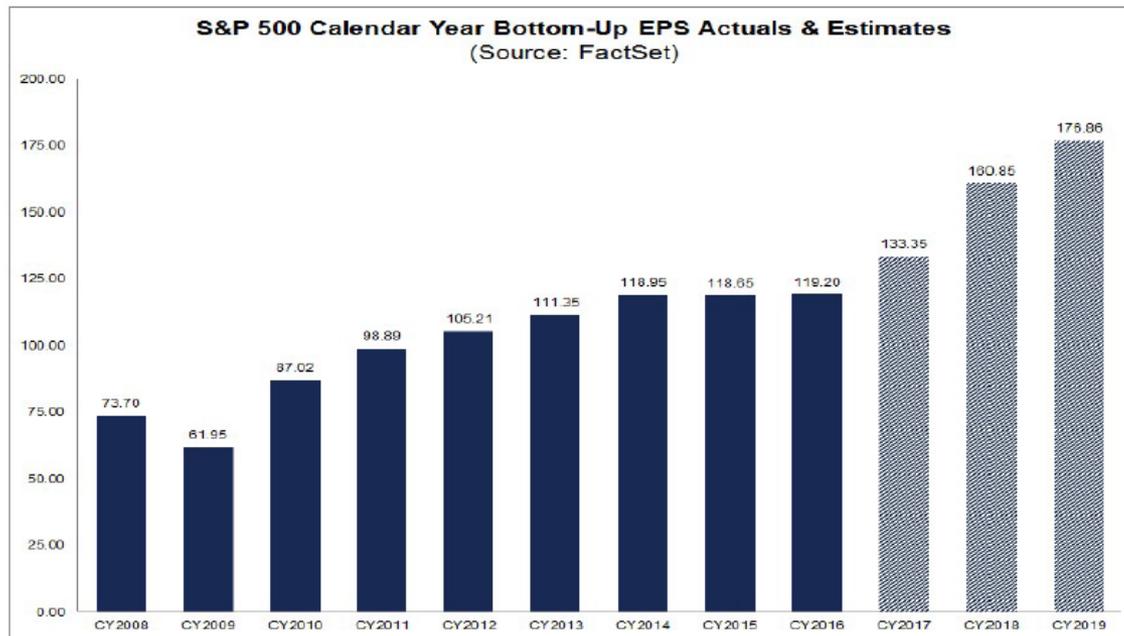
### Small Business Optimism Index Increased to 107.8

Based on 10 survey indicators, seasonally adjusted, Jan. '00 – May '18

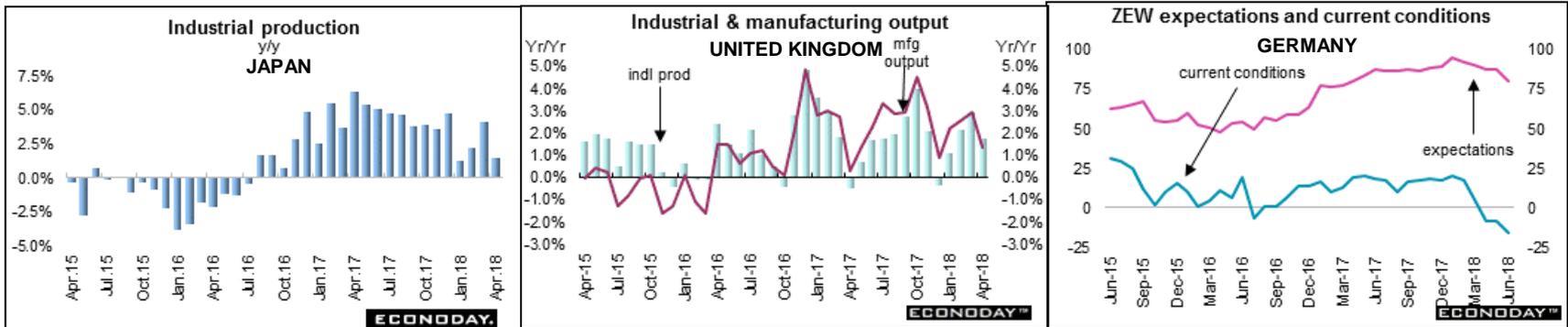


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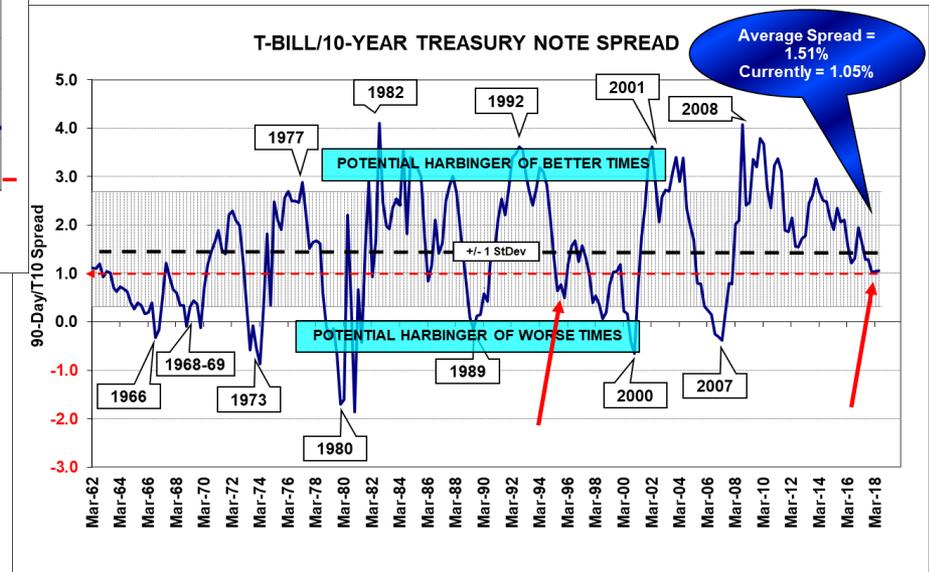
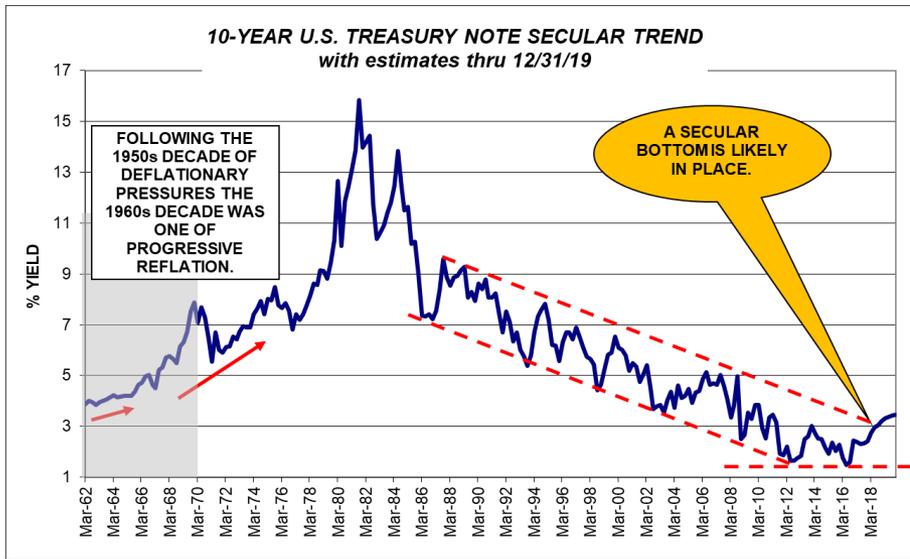
Such optimism prevails among larger companies as well. Helped by recent tax cuts and business legislation, S&P 500 companies are delivering accelerating earnings growth in 2018 and appear on track for double-digit growth in 2019. For Q1 2018, the blended earnings growth rate for the S&P 500 was 24.6%. For Q2 2018, the estimated earnings growth rate for the S&P 500 is 19.0%.



While the U.S. has been gathering momentum, growth in other economies around the globe has decelerated somewhat, perhaps signaling that what has been termed “The Synchronized Global Expansion” is mature. Either way, the trade-weighted U.S. dollar has strengthened, and foreign currencies generally have weakened, putting pressure on emerging and developing economies.



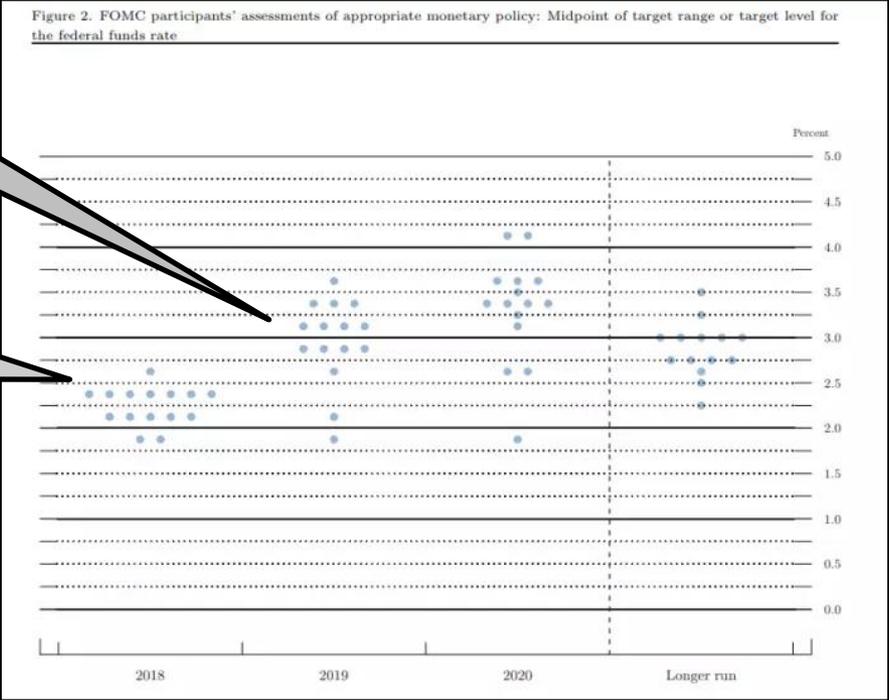
More signs of a secular bottom in interest rates have appeared, and U.S. rates generally have risen a bit this year. The increases in short-term rates (3-month T-bills) have outpaced those for longer-term rates (10-year Treasury notes), causing the portion of the yield curve between these two points to “flatten”. While this trend bears monitoring, the yield curve typically doesn’t signal a recession until after it inverts, with long-term rates falling below short-term ones.



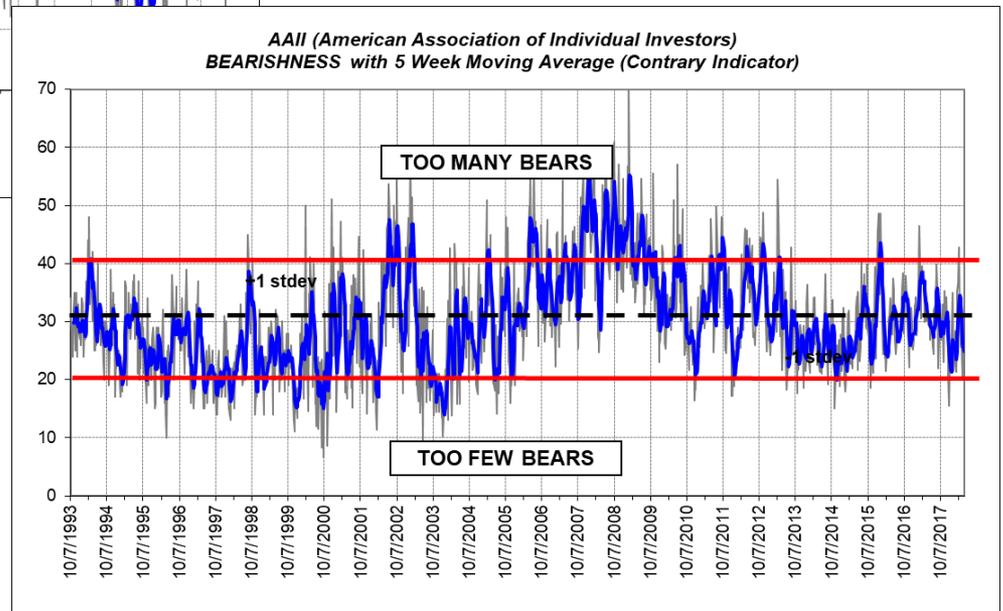
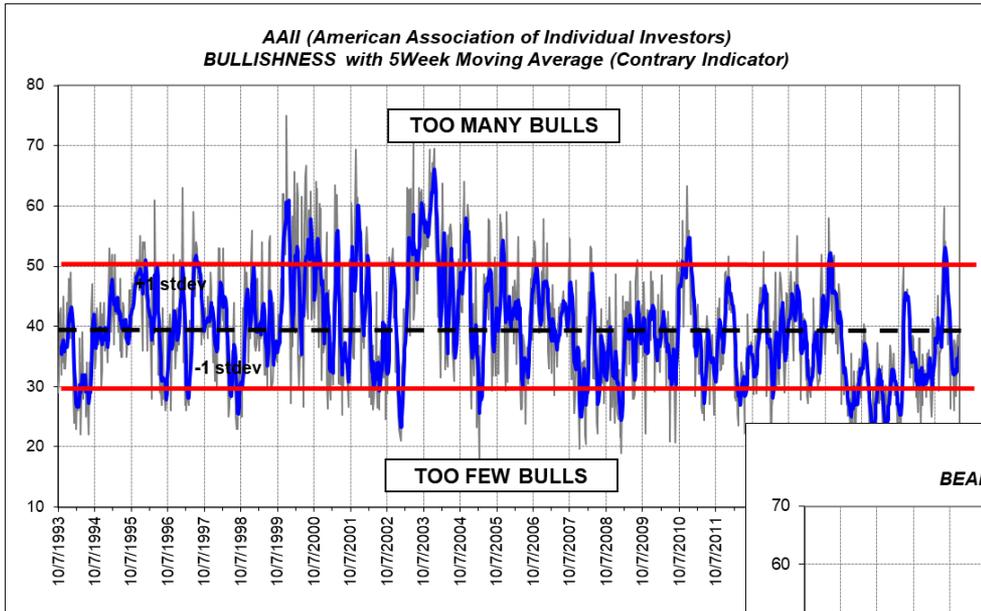
According to Federal Reserve Chairman Jerome Powell, the economy is in “great shape”, with steady growth, modest inflation, and “normalizing” rates. However, based on the current expectations of Fed governors (shown below) and the possibility that growth is peaking, markets are concerned that the Fed could overshoot, raising rates too much too soon.

3 more rate hikes in 2019

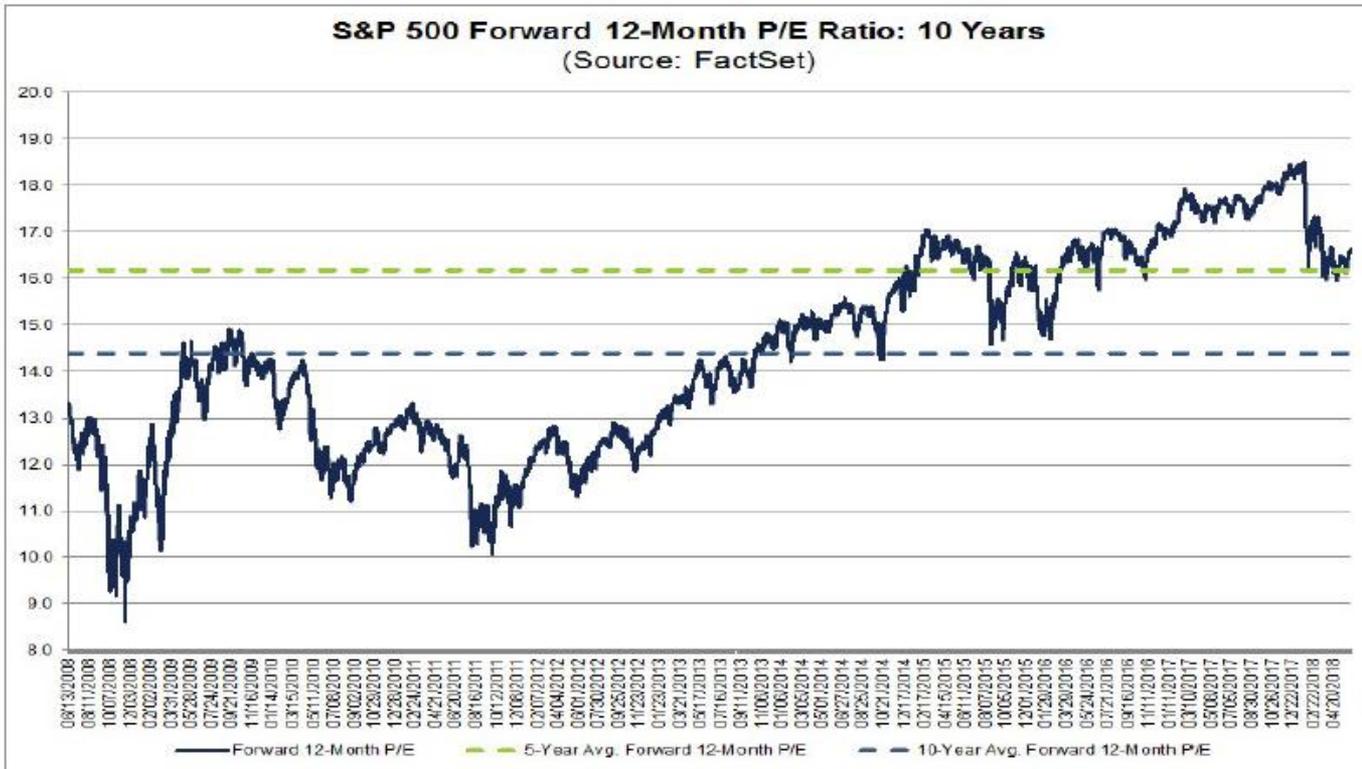
4 rate hikes for 2018



The February 2018 stock market correction dramatically reduced investors' optimism. Since sentiment often is a contrarian indicator, we view this development as a positive.



February’s correction also reduced the market’s valuation to more reasonable levels, ones which largely have persisted to the present. The S&P 500 Index currently is trading at approximately 16.6x forward estimates. This level exceeds the ten-year average (14.4x), but it is supported by current expectations for earnings growth and interest rate policy. However, equity markets often struggle during periods when inflation and interest rates rise concurrently. During such periods, market multiples tend to contract unless earnings and revenues continue to advance.



## Commentary

- The U.S. economy continues to advance, with unemployment at decade lows. Industrial production and productivity continue to increase, and growth in retail sales has appeared (finally). The Small Business Optimism Index increased in May to the second highest level in the NFIB survey's 45-year history.
- The “Synchronized Global Expansion” may be maturing, with growth in non-U.S. and emerging markets decelerating somewhat. The trade-weighted U.S. dollar has strengthened, and foreign currencies generally have weakened.
- The yield curve (3-month T-bills versus 10-year Treasury notes) has flattened but remains positively sloping. The U.S. has likely put in a secular bottom in yields.
- Federal Reserve Chairman Jerome Powell, recently characterized the U.S. economy as being in “great shape”, reflecting steady growth and modest inflation. These trends appear to give the Fed more cover to continue raising/“normalizing” interest rates in 2018 and 2019. Recent activity in the markets suggest that investors are concerned that the Fed could overshoot.
- The February 2018 stock market correction reduced investor optimism and P/Es. We view these developments as positives.
- The S&P 500 currently is trading at approximately 16.6x forward estimates, a level that is much closer to the ten-year average, and one that appears to be supported by earnings trends and interest rate policy. Looking ahead, actual positive earnings and revenue growth is paramount.

**Disclosure:**

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