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INVESTMENT COUNSEL

Market Observations
July 2017

Roll out those lazy, hazy, crazy days of summer. You'll wish that summer could always be here.

Charles Tobias

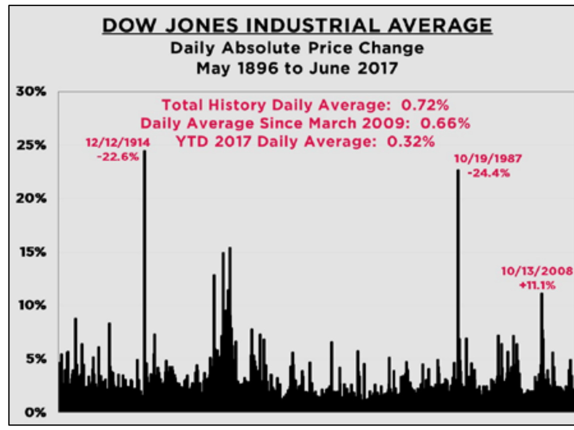
LAZY-HAZY-CRAZY DAYS

While Charles Tobias' lyrics and Nat King Cole's rendition celebrate summer, this sentiment can apply to the current investment environment. In this summer of 2017, daily market movements can be best described as a bit lazy, the outlook ahead remains ever hazy, and political activity seems at times a touch crazy. Much has been made of reduced market volatility and its potential implications. A review of both market and economic patterns can provide perspective.

Perspective

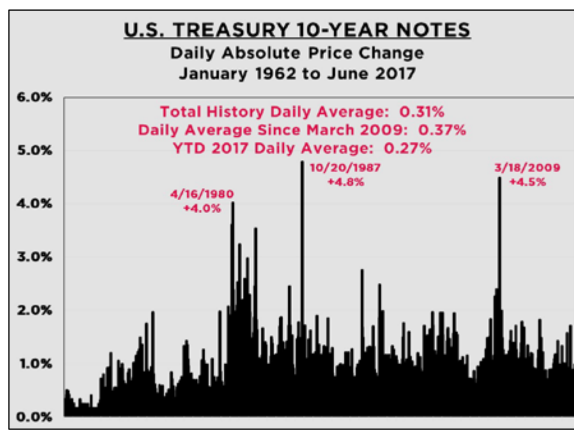
Commentators have addressed recent relatively low stock market volatility with a suggestion of investor complacency. Chart I shows the daily price volatility for the Dow Jones Industrial Average ("DJIA") over its very long history. Over the current bull market, DJIA volatility has been below the long-term average. For the year-to-date, DJIA volatility has been well below average. Some notable one-day volatility extremes have been highlighted in Chart I, but equally notable is that 50% of all daily DJIA price changes were less than ±0.5%.

Chart I



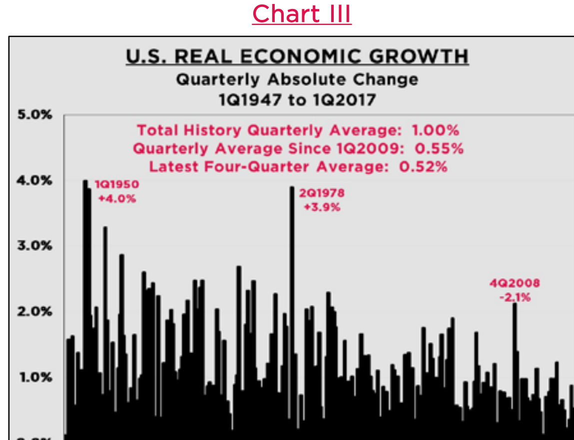
The pattern of bond market volatility is different as shown in Chart II. Daily yields, available for 10-year U.S. Treasury notes since 1962, were used to determine daily price changes. Bond market volatility in the year-to-date was negligibly lower than the long-term average but higher than the long-term average throughout the bull market for stocks. What could seem like a paradox with yields remaining near historically low levels is explainable by simple bond "math." The sensitivity of bond prices increases as yields decline. As a result, the same change in daily yield has resulted in a greater relative change in bond price during this period of relatively low yields.

Chart II



Rather than being complacent, investors may have benefitted from a more stable economic environment that has reduced general uncertainty. Chart III shows the quarter-to-quarter change in real economic growth (GDP) since the inception of this data. Over the more recent time horizons, economic activity clearly has been less volatile even though the overall level of growth itself has been below average.

Chart III



Investment Implications

For stocks, bonds and the overall economy, statistical averages smooth over extreme outcomes and meaningful trends, both favorable and unfavorable. Periods of lower volatility can give way to less favorable interim outcomes. As extreme weather days do not offset the overall benefit of summertime, volatility itself does not diminish the potential for longer term investment opportunities. Sometimes an umbrella is needed. At all times, effective portfolio diversification is prudent.