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Winfield Quarterly

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Customized Investment Portfolios and Private Wealth Advisory Services

MARKET COMMENTARY

A synchronized global economic recovery appears to be underway in 2017. For the first time in years, no major economy seems susceptible to an imminent recession. Global GDP growth is largely in sync with the slow but steady recovery in the United States, and across the world virtually no economies are projected to shrink in 2017. According to the World Bank, the global economy is expected grow 2.7% in 2017 and 2.9% in 2018 versus 2.4% in 2016, thanks in large part to declining unemployment rates, rising commodity prices, and low interest rates.

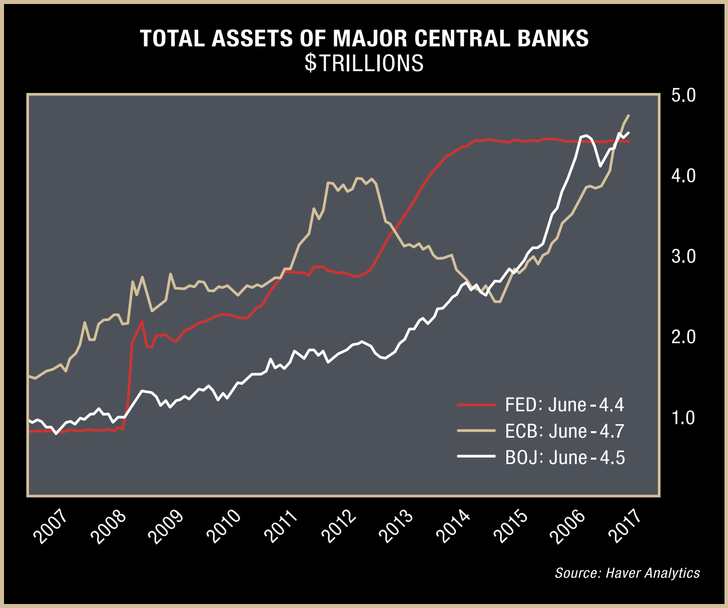
Global equity markets responded favorably to improving economic fundamentals. The MSCI Europe Australasia, Far-East (EAFE) Index rose 6.1% during the second quarter while the S&P 500, the Dow Jones Industrial Average (DJIA) and the NASDAQ Composite gained 3.1%, 4.0%, and 4.2% respectively. Through the first half of the year, the MSCI EAFE climbed 13.8%, the S&P 500 9.3%, the DJIA 9.3%, the NASDAQ 14.7%, and the MSCI Emerging Markets Index 18.6%.

At the end of the first half of 2017, the S&P 500 average stood at 2,423, up 258% from the market bottom of 677 on March 9, 2009. The bull market is now 99 months in duration, only exceeded by the 113-month bull market from October 1990 to July 1998. Investors are understandably asking if the stock market has reached a top, and when the next correction will begin. The threats of systemic and exogenous events provide plenty of consternation to moderate investor enthusiasm. While exogenous events are difficult to predict, systemic threats are often open to analysis. Perhaps the greatest systemic threat to global markets in the coming years is the coordinated reduction of monetary stimulus by the world's central banks. Since the height of the financial crisis in 2009, the US Federal Reserve Bank, the European Central Bank (ECB), and the Bank of Japan (BOJ) have used an unprecedented combination of low interest rates and liquidity to thwart the economic downturn. Nine years later, global interest rates remain near all-time lows and central bank balance sheets have ballooned from under $3 trillion to over $13 trillion today. The graph to the right illustrates the remarkable growth of the world's central banks' balance sheets.

As the graph indicates, the US Federal Reserve all but halted balance sheet expansion in 2015 while the ECB and BOJ continued to purchase assets through the middle of 2017. As of the end of the second quarter, the ECB's balance sheet of $4.7 trillion had surpassed both the balance sheets of the US Federal Reserve and BOJ. However, as the global recovery has gained traction, the need for monetary stimulus has diminished. At its most recent meetings, the Federal Reserve indicated its intention to gradually reduce its $4.4 trillion balance sheet to $2.0 trillion by 2021, and in recent weeks, the ECB announced its plan to taper asset purchases.

In addition to shrinking balance sheets, central banks are slowly raising interest rates. The US Federal Reserve has already increased its lending rate four times since the end of 2015 from near 0% to the current fed funds rate of 1.00%-1.25%. In June, the ECB declared victory over deflation, signaling what many believe is an end of accommodative policies. Over the past year, global bond yields have jumped in reaction to central banks' positioning. The yield of the 10-year Treasury ended the second quarter of 2017 at 2.39%, up from an all-time low of 1.37% almost exactly a year ago. In Europe and Japan, bonds with negative yields have finally crossed above zero. The yield of the 10-year German Bund is up from -0.17% in June 2016 to 0.56% in June 2017, and the yield of the 10-year Japanese Government Bond rose from -0.29% to 0.07% during the same 12-month period.

As central banks sell bonds to reduce balance sheets and raise rates to slow inflation, the money supply shrinks and bond prices fall. This strategy is the reverse of monetary stimulus in which central banks buy bonds to increase the money supply and lower rates to encourage investment and loans. The systemic risk to financial markets during a deleveraging cycle is significant and in this case unprecedented. In essence, the US Federal Reserve, the ECB, and the BOJ are attempting to reduce a cumulative $13 trillion of government assets without disrupting economic progress. The solution to a successful unwind rests with global growth and the capability of the world's economies to absorb the banks' assets.



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While global GDP growth is expected to remain below 3% in 2017, there are reasons to expect an acceleration in the second half of the year and into 2018:

Unemployment – The US unemployment rate reached 4.3% in May, a 16-year low, and in Europe, the unemployment rate dropped to 9.3%, a post-financial crisis low. Moreover, job growth is still running above the rate to keep unemployment steady.

Earnings growth – As described in our April Market Commentary, S&P 500 earnings are expected to grow 8% in 2017 while earnings in Europe and Emerging Markets will grow even faster.

Improving business spending – Global Purchasing Managers' Indexes are widely followed leading economic indicators. Recent data show a pick-up in purchasing managers' spending, particularly in Europe which has lagged the rest of the world since 2015.

China – The Chinese economy expanded 6.9% year-over-year in the March quarter of 2017, compared to 6.8% growth in the fourth quarter 2016. The first quarter was the strongest expansion since the third quarter of 2015, supported by faster rises in industrial output, retail sales and fixed-asset investment while fiscal spending surged. With the 19th National Congress of the Communist Party of China due to select the next generation of leaders this fall, political incentives are to ensure credit tightening does not choke off growth.

Tax reform – In our January Market Commentary, we reviewed a variety of fiscal policy changes outlined by the Trump administration to decrease taxpayers' burden and stimulate capital expenditures. While the prospects for near term progress on tax reform continue to fade as Congress grapples with a replacement for the Affordable Care Act, the Trump administration remains committed to fiscal stimulus before the end of the year.

We continue to expect ongoing challenges to fixed income investing as the economy improves and central banks remove stimulus. While the gap between US and international equity valuations closed during the second quarter, we continue to believe that on a relative basis, international equities offer attractive opportunities.

QUALIFIED CHARITABLE DISTRIBUTIONS

Qualified Charitable Distributions (QCDs) allow taxpayers to make charitable contributions from an IRA directly to a charity and to exclude that amount from income. Not everyone qualifies – the rule only applies to IRAs, not plans, and only for those IRA owners or beneficiaries who are 70 ½ years old or older. The QCD is excluded from income and can satisfy the annual Required Minimum Distribution (RMD), up to the $100,000 QCD limit. No charitable deduction is permitted for this amount, but excluding RMD income lowers the tax bill.

The QCD can also increase other tax benefits. When income is lower, more deductions and other tax benefits are allowable which lowers total tax liability.

If you are required to take an annual distribution and are interested in charity, consider speaking with your accountant about a QCD.

MARKET PERFORMANCE

	2Q 2017	2017 YTD
Dow Jones	4.0%	9.3%
S&P 500	3.1%	9.3%
Nasdaq	4.2%	14.7%
Russell 2000	2.5%	5.0%
MSCI EAFE	6.1%	13.8%
Barclays Agg	1.4%	2.3%

WHEN TO WORK WITH WINFIELD

PRIVATE INDIVIDUAL INVESTORS

- Manage accumulated wealth, inheritances and settlements

ENDOWMENTS AND FOUNDATIONS

- Manage assets with a long-term growth strategy while meeting investment policy requirements

BUSINESS OWNERS

- Customize investment portfolios to lessen risk of concentrated assets
- Defer taxable earnings in profit sharing plans
- Manage and advise 401(k) plans

BUSINESS PROFESSIONALS

- Customize investment portfolios, manage stock options and consolidate 401(k)/IRA plans to lessen risk of concentrated assets

RETIREES

- Customize investment portfolios with the option of drawing income
- Management of IRAs, trusts and taxable accounts

www.winfieldinc.com

700 West St. Clair Avenue, Suite 404 • Cleveland, OH 44113

(216) 241-2575 • (888) 322-2575 • fax: (216) 241-4774