usbancorp Asset Management, Inc.

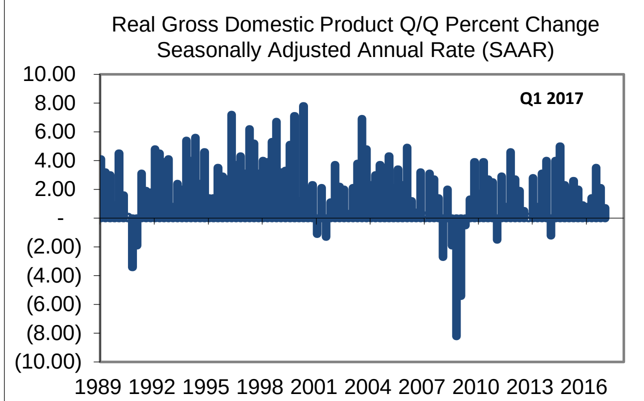
Economic and Financial Markets Monthly Review & Outlook Detailed Report

June 2017

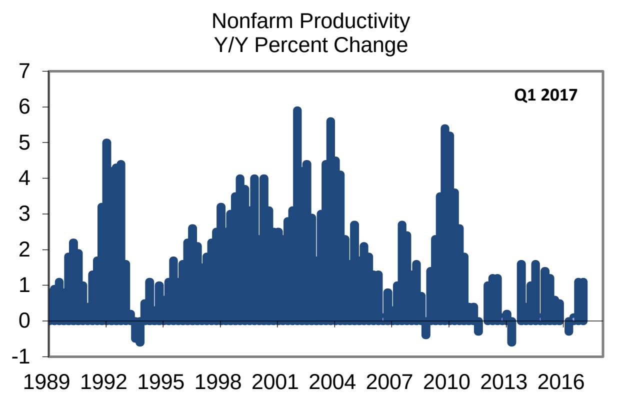
NOT FDIC INSURED NO BANK GUARANTEE MAY LOSE VALUE

Overview of the Economy

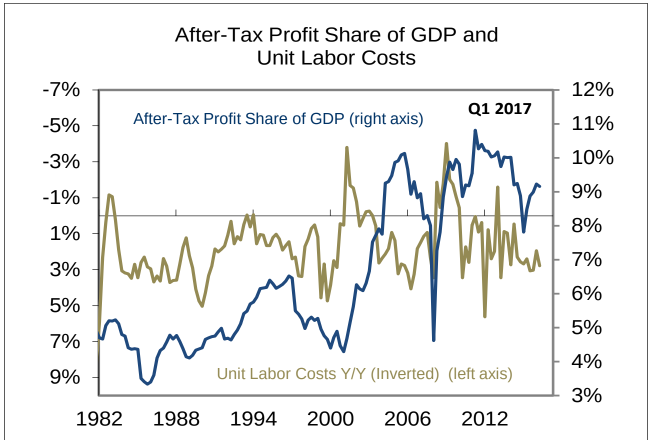
Business and economic confidence indicators remain elevated, albeit with some moderation since post-election highs. Financial markets continue to grind higher, reflecting expectations of continued earnings growth and fairly stable inflation rates. The speed of policy change in Washington remains closely watched. Forecasts for gross domestic product (GDP) growth, including our own expectations, have remained relatively stable. The Federal Reserve (Fed) raised short-term interest rates in June to a range of 1.0% to 1.25%, the fourth increase since the financial crisis. Futures markets are pricing a small likelihood of additional rate increases later in 2017. Perhaps this reflects expected changes in Fed balance sheet management. The initial estimate of first quarter real GDP growth was revised to 1.2% from 0.7%. Consensus estimates for second quarter growth remain in the 3% range. We continue to anticipate full year 2017 growth of 1% to 2%.



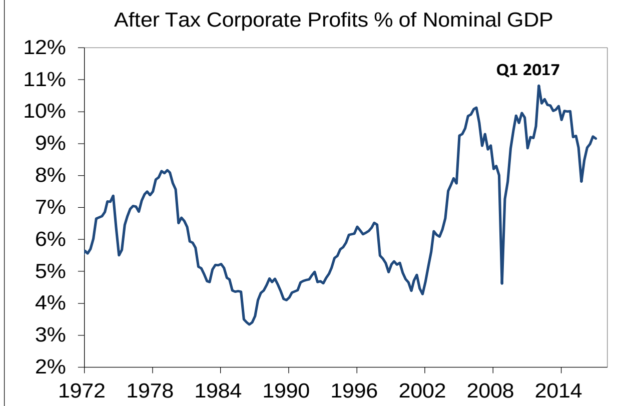
Source: Department of Commerce



Source: Department of Labor



Source: Departments of Commerce, Labor



Source: Department of Commerce

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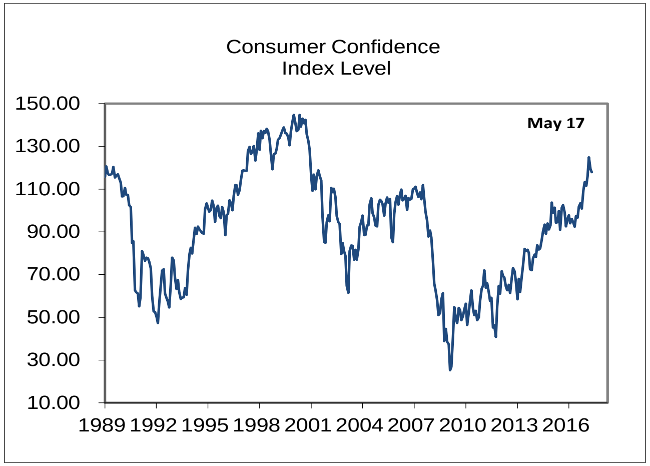
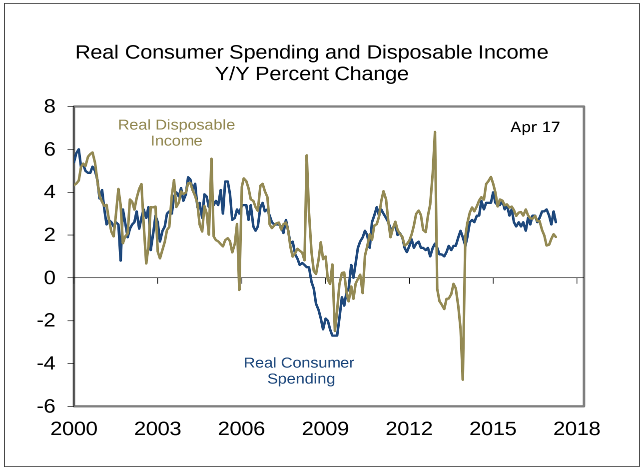
Consumer Expenditures

Growth in real personal consumption expenditures during the first quarter was revised to 0.6% from 0.3%. Real income growth continues to trend around 2%. Consumer confidence decreased slightly in May for the second consecutive month, although current levels have only been exceeded during the tech boom of the late 1990s. Household net worth as a percent of disposable income remained at an all-time high during the first quarter, supported by rising equity markets and strong housing price growth. Savings rates have moved to the lower end of the 5% to 6% range seen over the past several years, reflecting generally elevated levels of confidence and asset values. It is notable that previous cyclical peaks in household net worth and consumer confidence during the past two decades have been followed by disappointing equity returns.



Source: Conference Board



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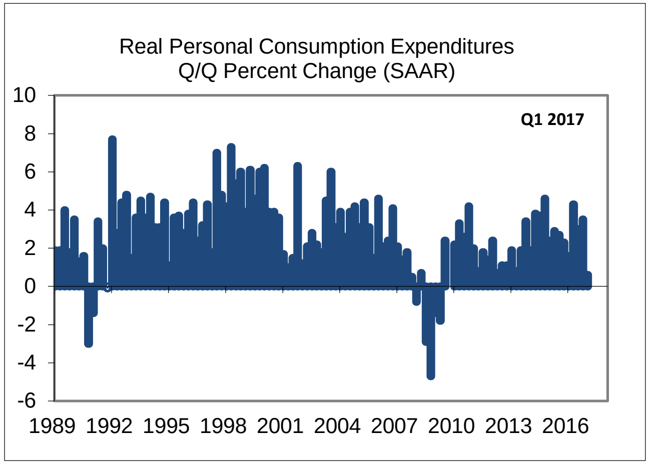

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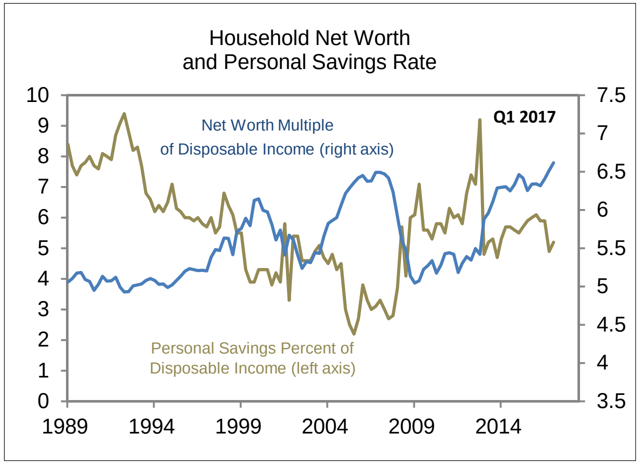

Sources: Department of Commerce, Federal Reserve

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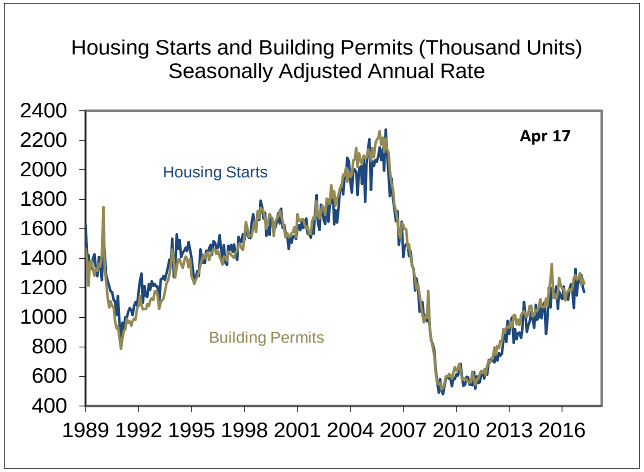
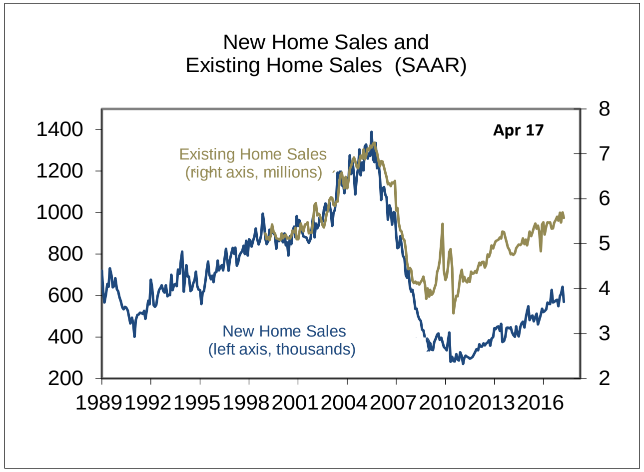
Housing

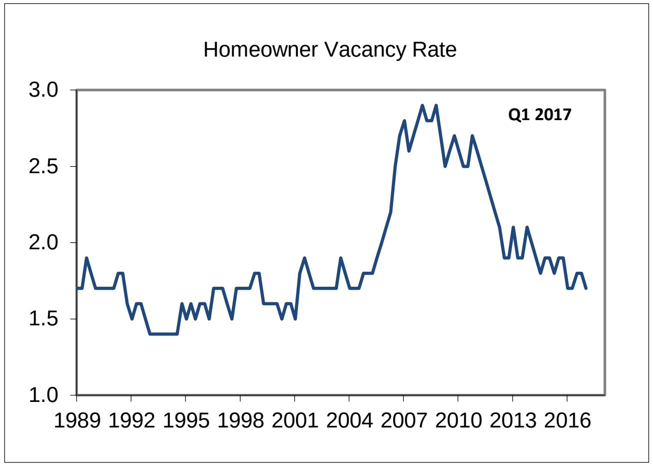
Recent housing data remains generally in line with prior months' trends. Vacancy rates remain low, housing activity (new and existing), remains stable and housing prices continue to increase at a 5% to 6% annual rate. Mortgage rates remained relatively stable during the first half of the year, trending at around 4% after jumping higher post-election last year. While rates are higher than 2016 averages, they remain historically low and should continue as a tailwind for homebuyers this year. Low interest rates have helped keep mortgage payments affordable for homebuyers, even as home price growth continues to outpace average hourly earnings gains. However, strong home price growth in excess of income growth over the last few years has contributed to a decline in the trend of homebuyer affordability, which could eventually slow down the market for home sales.



Source: Department of Commerce



Sources: Department of Commerce, Nat'l Assoc. of Realtors



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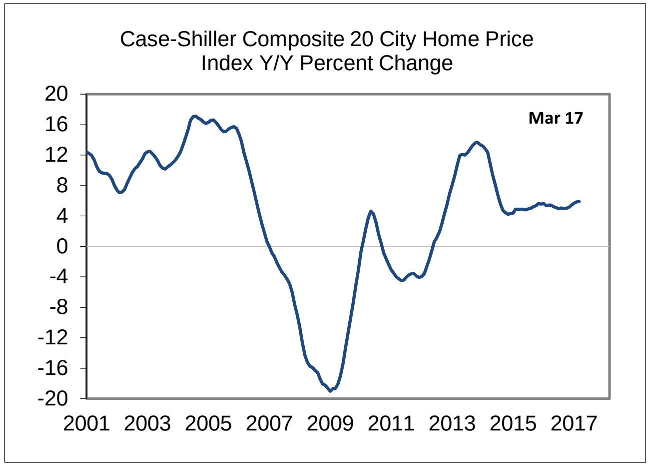

Source: Standard and Poors

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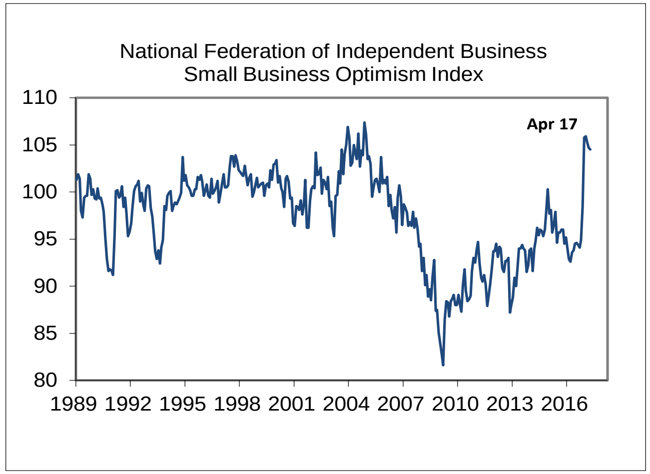
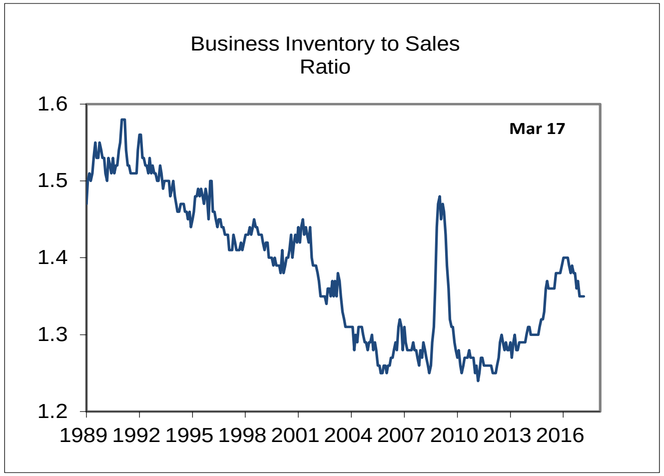
Production and Investment

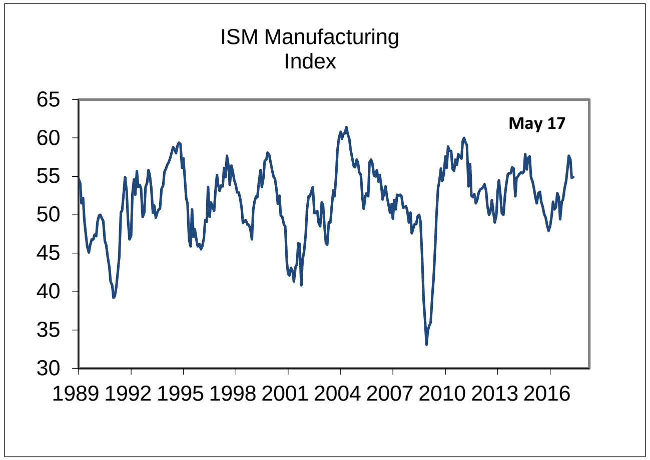
Production and investment data are consistent with moderate economic growth. Survey-based data (manufacturing PMI and small business optimism) remain strong but are beginning to fade, while hard data such as industrial production and capacity utilization are beginning to reflect survey-based data. The business inventory-to-sales ratio has declined in recent months, but remains higher than average non-recessionary periods over the last 20 years. This should be a near-term headwind to investment. Private investment growth was weak in 2016 and only contributed slightly to total year economic growth. We anticipate investment growth will be moderate in 2017, as excess capacity and sluggish demand growth will likely limit new investment spending.



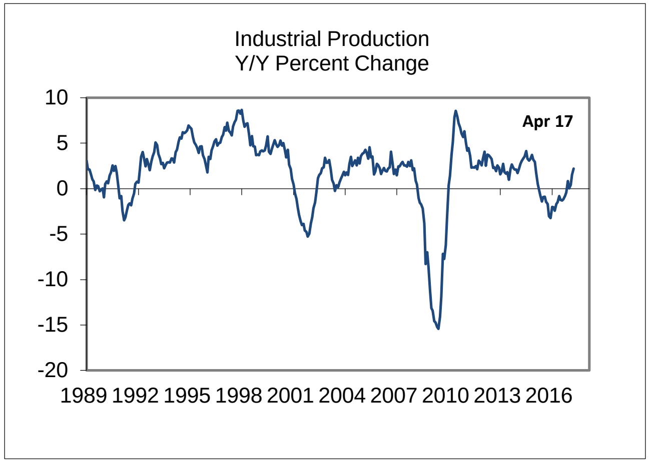
Source: National Federation of Independent Business



Source: Department of Commerce



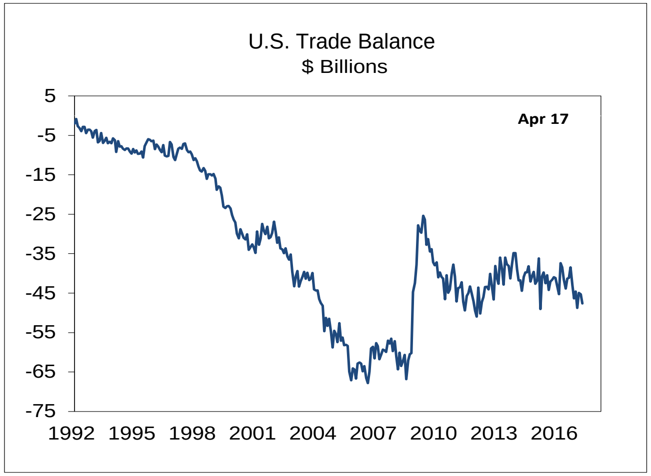
Source: Institute for Supply Management



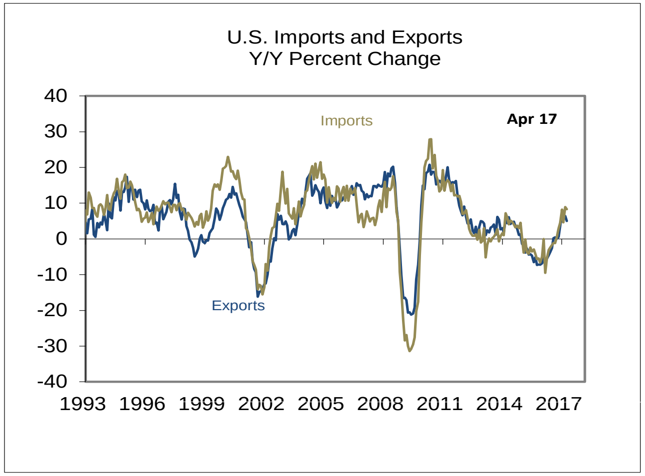
Source: Federal Reserve Board

International Trade

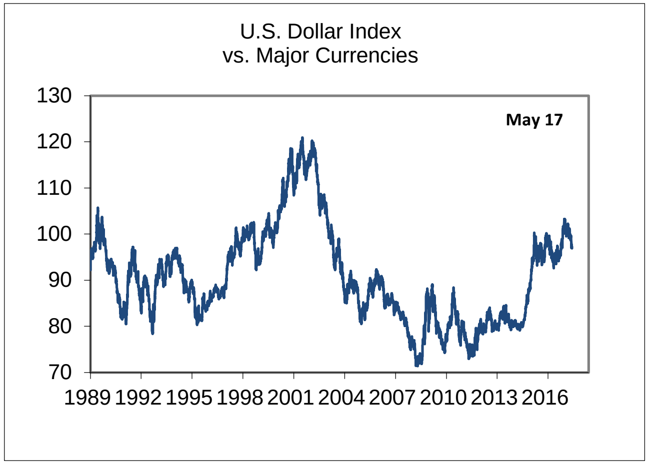
The trade deficit widened significantly in April, after little change in March. Exports declined slightly in April, while imports increased moderately. Real net exports likely had a slight positive effect on first quarter GDP, but the consensus predicts that real net exports will subtract from second quarter GDP. We expect this effect to ripple through to broader global measures in the latter half of the year. The dollar weakened through the first half of 2017, which should provide for a more favorable trade backdrop in early 2018. However, this will depend on continued momentum in major foreign economies.



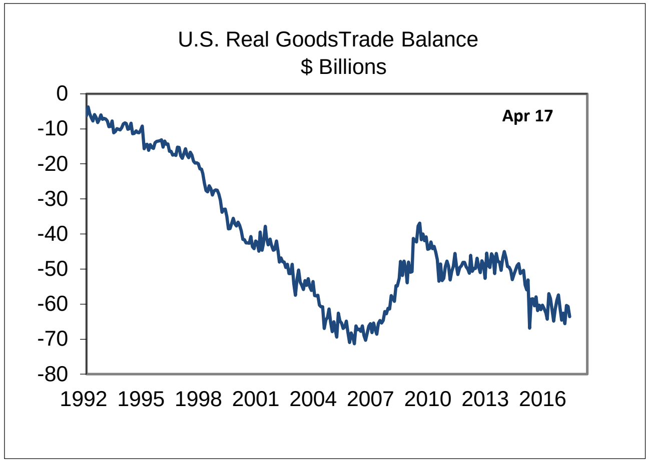
Source: Department of Commerce



Source: Department of Commerce



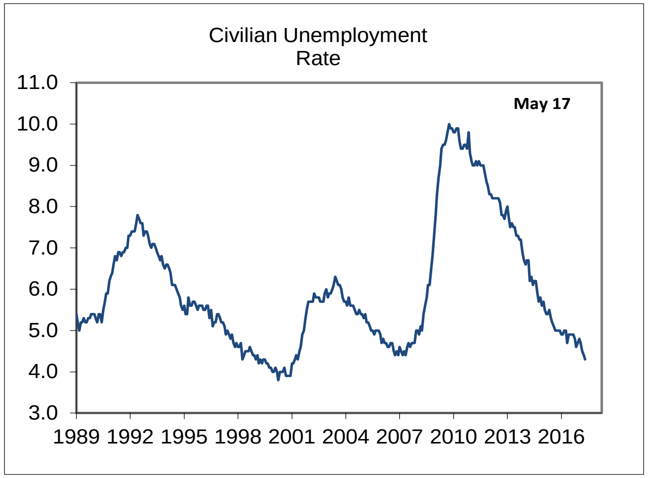
Source: Bloomberg



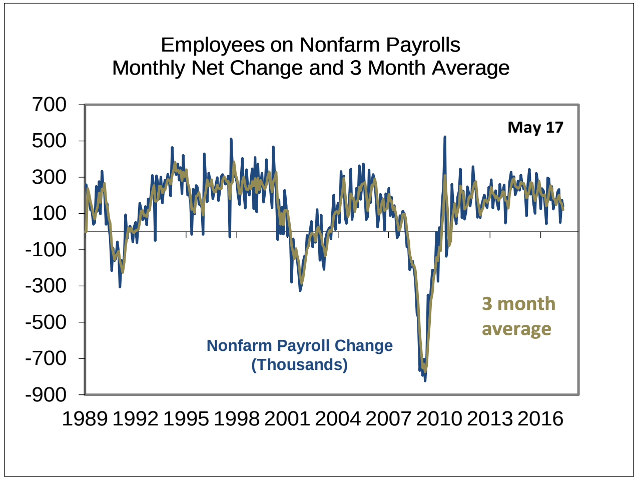
Sources: U.S. Department of Commerce

Labor Market Conditions

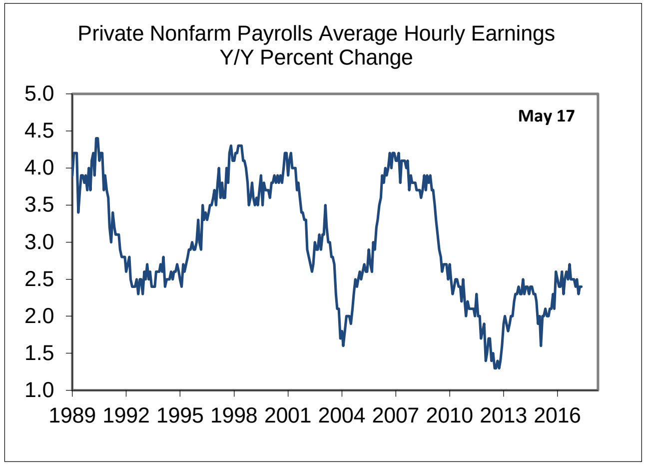
Nonfarm payrolls increased by 138,000 in May. Following the May employment report, the average payroll gain was 121,000 over the trailing three months and 161,000 over the past six months. Payroll growth should continue at a moderate pace in the coming months relative to last year's pace, with the economy at full employment. The report did not significantly affect expectations for the path of Fed rate hikes. Average hourly earnings remain in line with expectations and are consistent with moderate wage growth. Unemployment dropped to a new cyclical low of 4.3% in May. The tight labor market should keep the unemployment rate from falling much further. Additional demand for labor going forward is more likely to raise wages and / or increase the participation rate than reduce the unemployment rate.



Source: Bureau of Labor Statistics



Source: Bureau of Labor Statistics



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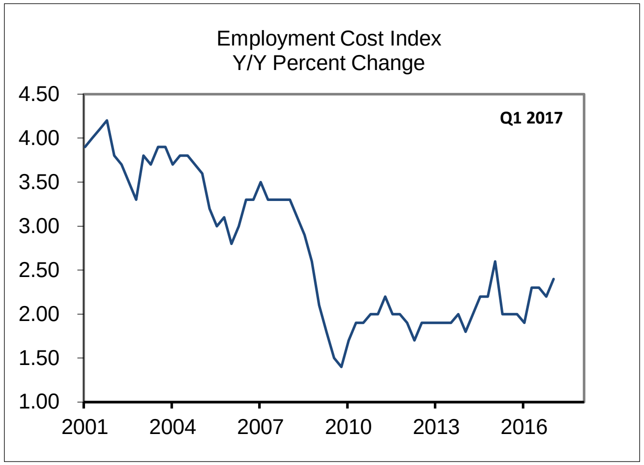

Source: Bureau of Labor Statistics

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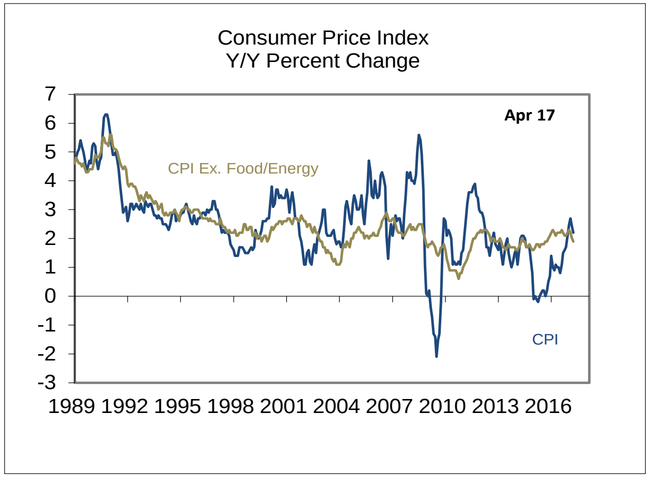
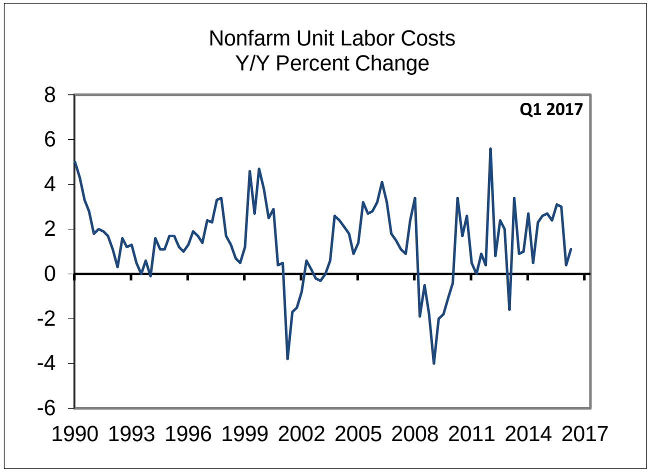
Inflation and Monetary Policy

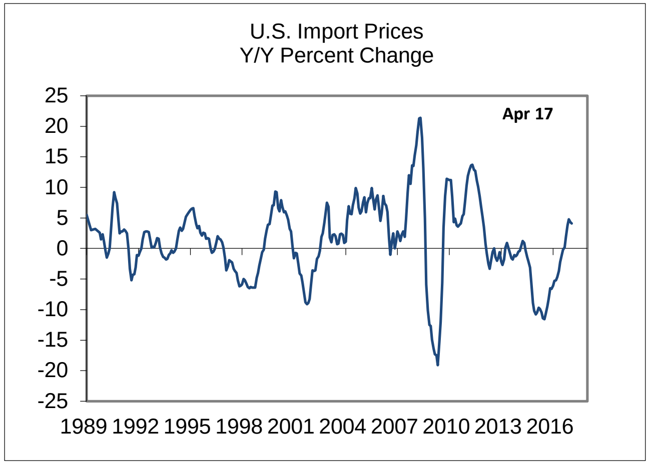
Inflation moderated once again in April to 2.2%. Price growth may continue to slow over the next few months, as early-2017 inflation readings were boosted by low base level energy prices from early in 2016. Oil prices bottomed in February 2016 before rallying through most of the rest of the first half of the year. Core inflation (excluding food and energy costs) has remained in a stable trend of around 2% even as headline inflation has experienced volatility. We expect headline inflation to converge lower towards core inflation later in the year as the effect of energy price changes diminishes. After the June rate hike, markets anticipate the Fed to pause over the next several months. The Fed may also begin normalizing its balance sheet by year end.



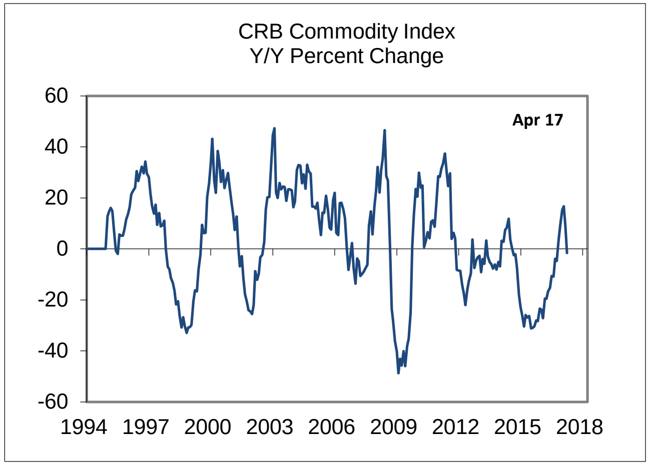
Source: Bureau of Labor Statistics



Source: Federal Reserve Board



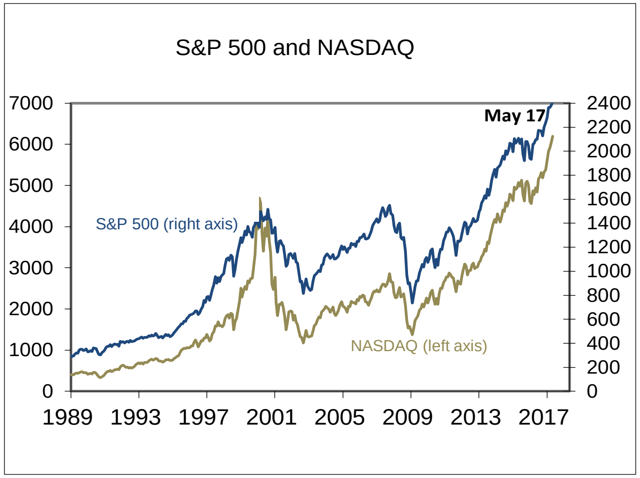
Source: Bureau of Labor Statistics



Source: Reuters

Equity Market

U.S. equity market returns showed mixed performance during May. The Nasdaq Composite Index returned 2.7% and the S&P 500 Index returned 1.4%. The Russell 2000 Index of small cap stocks moved in the opposite direction, returning -2.0%. Realized and implied volatility remain at historical lows. Technology and utility stocks led the market with returns of more than 4%. Energy stocks performed the worst, declining more than 3%. Financial stocks lost more than 1%, reflecting the flattening of the Treasury yield curve. Technology has been the standout performer year-to-date, returning more than 20%, while energy has lost more than 12%. Domestic markets in aggregate have lagged international equities so far in 2017, a reversal of the pattern of the past several years.



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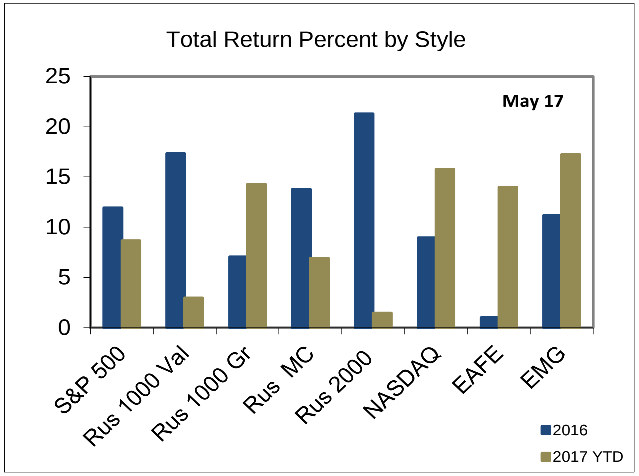

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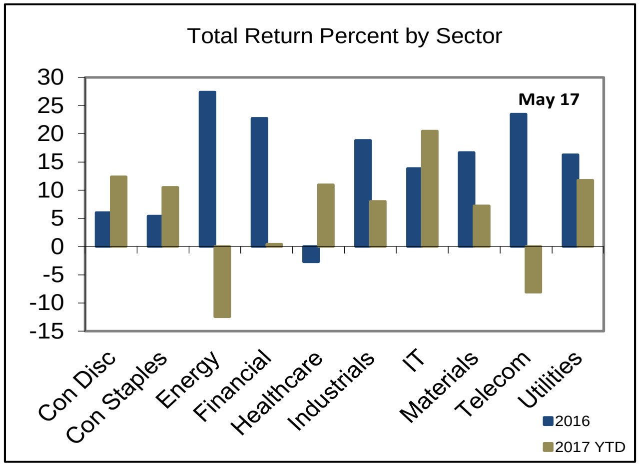
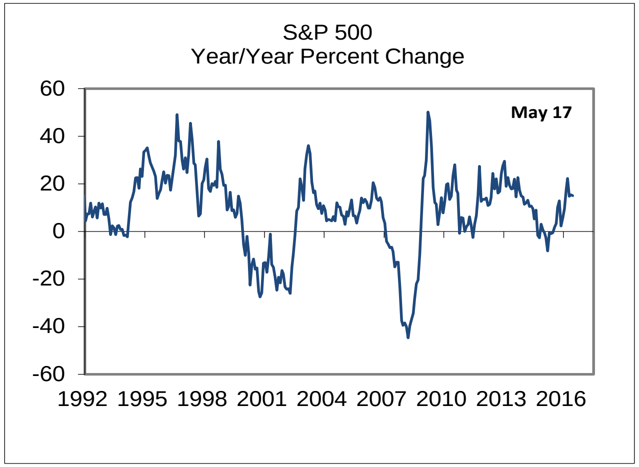


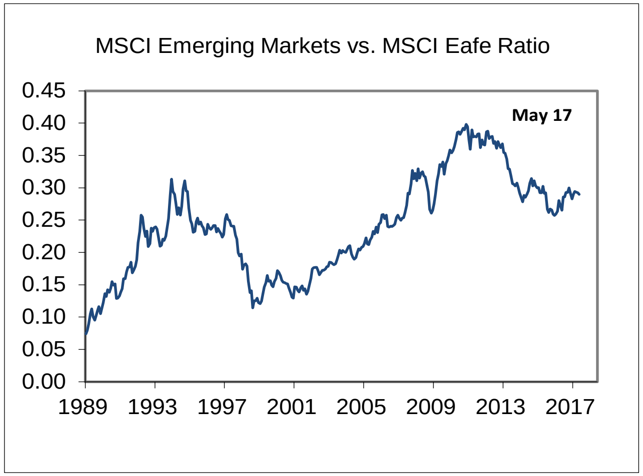
Source: Bloomberg. Based on the S&P 500 Index.



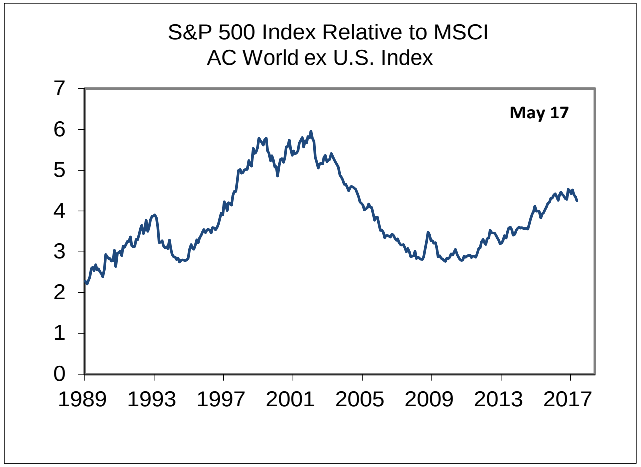
Source: Bloomberg

International Markets

International equities continued their outperformance relative to U.S. stocks in May. EAFE (Europe, Australasia, Far East) returned 3.7% and emerging markets equities returned 3.0%. Europe led all world markets again in May, returning 4.8%, as the market accelerated following the first round of French elections. Emerging markets have been the clear winners, returning 17.3% vs. 9.0% for the S&P 500 year to date. If international stocks maintain their performance advantage over U.S. equities, it would be the first time since 2012 that international stocks outperformed the U.S. in a calendar year.



Source: MSCI Barra



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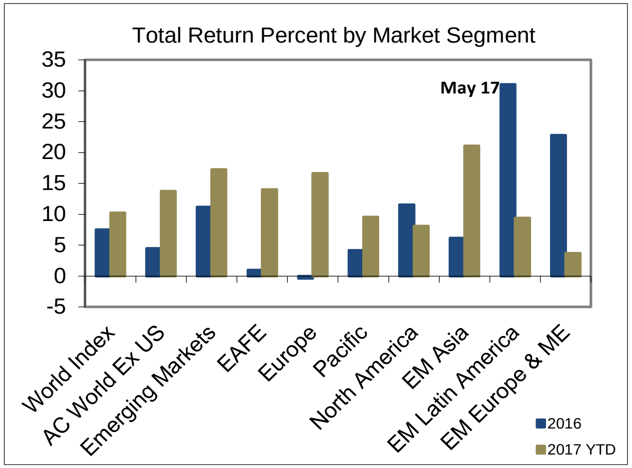

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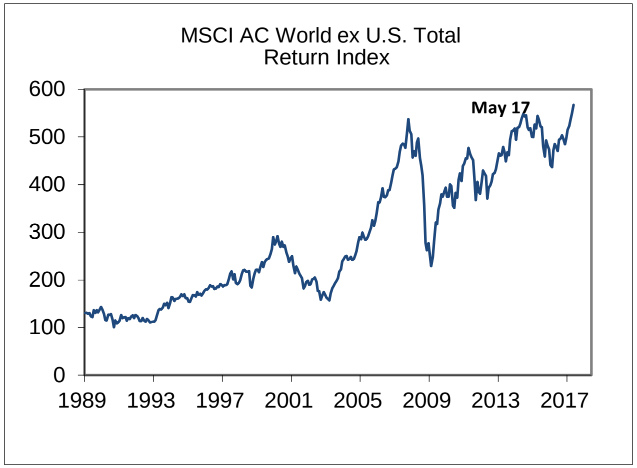
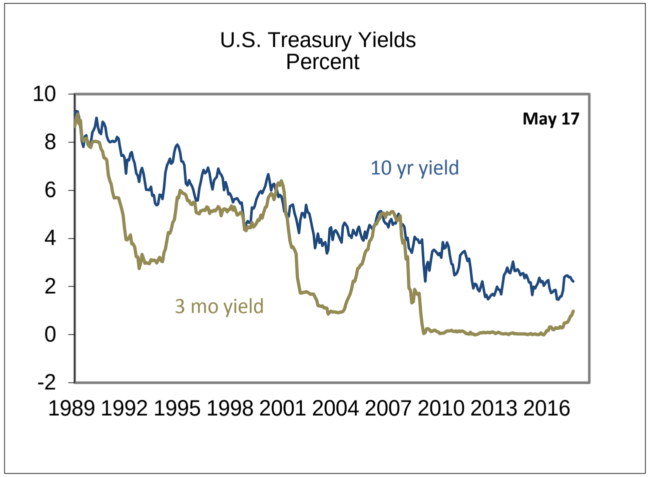


Source: MSCI Barra

Fixed-Income Market

During May, the two- to 30-year U.S. Treasury yield curve moved down and flattened slightly, with the two-year yield roughly unchanged and the ten- and 30-year yields decreasing around 0.1%., Short-term rates have risen since the end of 2016, reflecting continued Fed tightening. Meanwhile, ten-year Treasury yields rose from 2.44% on December 31, to a high of 2.63% on March 13, declined to 2.17% on April 18 and ended May at 2.20%. Credit spreads decreased slightly during May, continuing their April declines. Treasury Inflation-Protected Securities was the worst-performing fixed income sector in May, with a negative total return of -0.04%.



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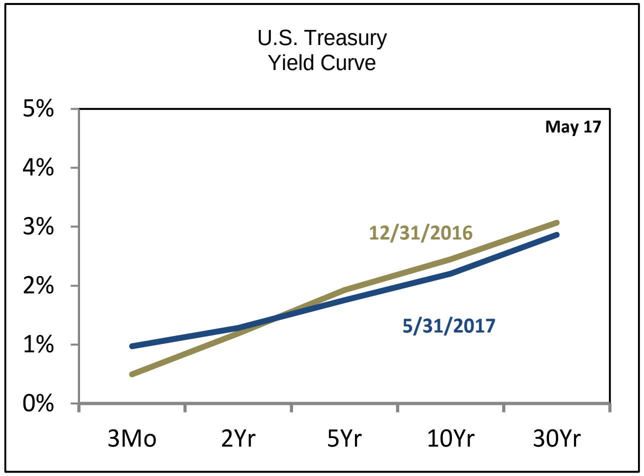

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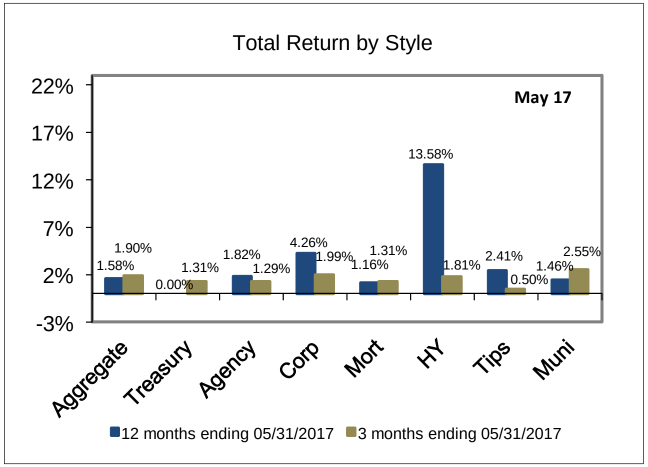
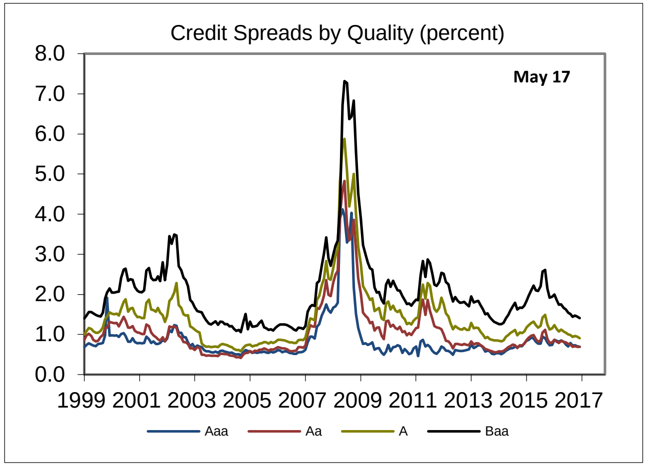


Source: Barclays Capital. Based on the Barclays U.S. Aggregate Bond Index.



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Economic, Rates and Earnings Forecast

	2016 (A)	2017 (F)	2018 (F)	2017 Bloomberg Consensus*	2018 Bloomberg Consensus*
Real GDP (Q4/Q4)	2.1%	1.0% - 2.0%	1.0% - 2.0%	2.20%	2.30%
Personal Consumption Expenditures	3.1%	1.0% - 2.0%	1.0% - 2.0%		
Investment	0.1%	1.0% - 2.0%	1.5% - 2.5%		
Net Exports ($)	-$563B	-$620B	-$620B		
Government Spending	0.2%	1.0%- 2.0%	1.0%- 2.0%		
Unemployment Rate* **	4.7%	4.3%	4.3%	4.40%	4.30%
CPI* **	2.1%	1.5% - 2.5%	1.5% - 2.5%	2.30%	2.30%
CPI Excluding Food and Energy* **	2.2%	1.5% - 2.5%	1.5% - 2.5%		
Fed Funds* **	0.50% - 0.75%	1.00% - 1.50%	1.00% - 2.00%	1.50%	
10 Year Treasury* **	2.44%	1.50% - 2.50%	2.00% - 3.00%	2.71%	
Corporate Earnings (S&P Operating)	$106.26	$120.00	$123.00	$128.51**	$145.80**
Trade Weighted Dollar* **	102.21	98 - 108	95 - 105		
*Bloomberg - June 9,2017					
**Standard and Poors - June 9, 2017					
***End of Period Level					

(A) Actual

(F) Forecast

Index Definitions

The **Barclays U.S. Aggregate Bond Index** represents securities that are SEC-registered, taxable and dollar denominated. The index covers the U.S. investment grade fixed rate bond market, with index components for government and corporate securities, mortgage pass-through securities and asset-backed securities.

The **MSCI EAFE Index** is an equity index which captures large and mid cap representation across Developed Markets countries around the world, excluding the U.S. and Canada.

The **MSCI Emerging Markets Index** captures large and mid cap representation across 21 Emerging Markets (EM) countries

The **MSCI ACWI (All Country World Index) Index** is a free float-adjusted market-capitalization-weighted index that is designed to measure the equity market performance of developed and emerging markets.

The **MSCI ACWI (All Country World Index) Index** ex U.S. is a free float-adjusted market-capitalization-weighted index that is designed to measure the equity market performance of developed and emerging markets, excluding the United States.

The **MSCI World Index** is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of developed markets.

The **MSCI EM (Emerging Markets) Asia Index** is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of emerging markets in Asia.

The **MSCI Europe Index** is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of the developed markets in Europe.

The **MSCI Europe & Middle East Index** is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of the developed markets in Europe and the Middle East.

The **MSCI EM (Emerging Markets) Latin America Index** is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of emerging markets in Latin America.

The **MSCI North America Index** is designed to measure the performance of the large and mid cap segments of the U.S. and Canada markets.

The **MSCI Pacific Index** is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of the developed markets in the Pacific region.

The **Russell 1000® Growth Index** is a market-capitalization-weighted index that measures the performance of those Russell 1000 companies with higher price-to-book ratios and higher forecasted growth values.

The **Russell 1000® Value Index** is a large-cap value index measuring the performance of the largest 1,000 U.S. incorporated companies with lower price-to-book ratios and lower forecasted growth values.

The **Russell 2000® Index** is composed of the 2,000 smallest stocks in the Russell 3000® Index and is widely regarded in the industry as the premier measure of small-cap stock performance.

The **Russell Midcap Index** measures the performance of the mid-cap segment of the U.S. equity universe. The Russell Midcap is a subset of the Russell 1000® Index.

The **S&P 500® Index** is a capitalization-weighted index of 500 stocks designed to measure the performance of the broad domestic economy.

Disclosure

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Past performance does not guarantee future results.

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