# GLOBAL EXCHANGE TRADED FUND STRATEGY

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## Second Quarter 2017 Performance Review

Our global balanced strategy, which allocates among bonds, stocks, and commodities around the world, gained 3% last quarter, boosting the strategy's 12-month return to 8.3%.

Investors' enthusiasm bolstered financial asset prices, helping stocks and bonds around the world deliver another strong quarter. The MSCI AC World Index returned 4.3% for the quarter, and Bloomberg Barclays' Global Aggregate Bond Index gained 2.6%.

It's been a great year for financial markets, with global equities posting a double-digit gain without a substantial setback. What was not anticipated by most observers is that this year's rally has been driven by international equities, instead of US equities. Better results in non-US stocks are attributed to the improved global outlook, healthier corporate earnings, and less European political turmoil.

The Dollar index, a measure of the dollar's value against major currency rates, has been in a slump since early this year, despite the Federal Reserve's tightening efforts. This September, the Fed will begin to reduce its $4 trillion balance sheet, which had helped finance more than 90 months of economic expansion, the third longest on record since 1900. The dollar's current slump is baffling, and US treasury yields are painting a perplexing picture of the US economy. After Trump's victory in November, 10-year US Treasury yields spiked almost one full percent to 2.6%. Six months into Trump's administration, however, yields had dropped to 2.3% by June 30, 2017.

Lower US bond yields suggest a lackluster US growth rate and low inflation expectations. The second quarter US GDP grew 2.6%, whereas their GDP growth estimate last May had been 4%. US inflation softened to 1.6% in June, reflecting weakening commodity prices. The Thomson Reuters/Jefferies CRB Index dropped 5.8% in the last three months, led by energy prices. Crude had been trading below $50 per barrel throughout the second quarter, down 9% from the previous quarter. Wage growth was also poor, increasing only 3% while the unemployment rate stood at 4.4%.

When long rates move lower and short rates rise, the result is a flattening yield curve. Traditionally, a flattening yield curve indicates economic weakness lies ahead. US bonds edged up 1.3% during the quarter, boosted by high yield bonds which outperformed as investors sought returns in a changing economic outlook. Global yield curves, like the US curve, also flattened as weak commodity prices muted inflation fears in Europe. In Japan and China inflation numbers stood below 2%. Lower inflation helped international bonds return 3.4% for the quarter, beating US bonds by nearly 2%. But it also signals that the current global recovery may soon lose its momentum.

At quarter's end, our strategy's equity portion returned 4.3% for the quarter, increasing its 12-month return to 19%, and the bond portion rose 2.3%, paring its 12-month loss. The equity and commodities portion accounted for 56% of the strategy's assets, and bonds accounted for the remaining 44%. Specifically, 25% of strategy assets were invested in US equities, 23% in foreign equities, 23% in US bonds, 21% in foreign bonds and 8% in commodities.