Investment Review and Outlook **January 2018**

"We Have Come A Long Way"

Nine years ago (2008) the U.S. economy was contracting at the fastest rate in more than 50 years and the economy was losing hundreds of thousands of jobs a month. The Federal Reserve initiated quick and decisive action utilizing "Quantitative Easing" in an effort to stabilize the decline. The Federal Funds rate was lowered significantly and the Fed began buying both U.S. Government bonds and mortgage backed securities to stabilize credit markets. These actions by the Fed were coordinated with increased government spending to increase employment and help stabilize the economic decline. As a result of the Fed's actions, total assets on its balance sheet increased from $900 Billion in 2008 to $4.5 Trillion at the end of 2017. Concurrently, U.S. public debt increased from $9 Billion to $20 Billion today.

During this same period from 2009 thru 2016 the U.S. economy grew at a modest 2% rate and inflation remained consistently below the Fed's long term target of 2%. However, beginning in the second quarter of 2017 economic growth began to increase at a 3% annual rate and inflation has slowly moved up closer to an annual rate of 2%. The improvements appear to be the result of the fact that the majority of all sectors of the economy are now growing as opposed to in the past when not all sectors were contributing.

The U.S. economy is comprised of three major sectors: consumer, business and government. Until recently government and consumer spending were the major contributors to the growth in the U.S. economy. The changes that have helped to increase the growth of the U.S. economy are primarily two fold. Government spending has continued to increase although with a change. The current and future expected increase in government spending is primarily in the defense budget. At the same time business capital spending, which had been flat to down since 2008, has begun to increase as there is a need to catch up from a long period of under spending on the part of business. The combination of the increase in government spending on defense and the need to make up for the many years of under investing on the part of business has created improved economic growth. These changes have begun to be recognized in the macro-economic statistics reported by government. Prior to the improvement in business spending U.S. government reports on economic growth were for modest growth. It is now believed that the government statistics measuring economic activity were weighted heavily towards manufacturing and not fully reflective of a service economy.

As the U.S. economy has become more of a service and technologically based economy, using statistics of the past economy did not accurately reflect improving economic activity. Due primarily to the improvement in manufacturing by businesses, the measures reporting economic activity have improved. Unemployment at close to 4%, down from 10% in 2008, is basically a full employment economy as the economy generally will have 2% unemployment reflecting people transitioning from one job to another. Consumer confidence is at a 17 year high as is investor confidence which is reflected in equity stock prices. Although stock market indices are registering new highs, they are not an accurate view of equity markets. Both the S&P Index and the Dow Jones Industrial Average are heavily weighted to a limited number of companies and therefore are not representative of the total equity market. As such there are companies' stocks that have not participated in the stock market rise and could become attractive investments with broadening of economic growth.

As the economic advance improves the prospects for a broader number of companies, wages and prices are likely to increase at a faster rate than in the past. This will likely increase inflation which will place upward pressure on interest rates. Higher interest rates are a dual edge sword for investors. Bond prices are likely to decline as interest rates rise. However, investors who own individual bonds in their portfolios will be able to reinvest the bond maturities at higher interest rates and thus receive greater income. Investors in bond mutual funds, unfortunately will be negatively impacted as the value of the Bond Funds decline reflecting lower bond prices from the higher interest rates. Fortunately all AHB client bond portfolios own only individual bonds and will be able to protect their portfolio values as well as reinvest at maturity to receive a greater income from the higher available interest rates.

AHB has also come a long way from 2008. Both our clients and we have benefited from our investment philosophy and strategy of seeking to achieve "reasonable risk adjusted investment return" in client Equity, Balanced and Bond portfolios. With our thanks to all those loyal long term clients as well as the many new clients who have chosen AHB to manage their assets in Separately Managed Portfolios (SMA's) we have increased the firm's' assets under management from $437 million at the end of 2008 to $2.0 Billion at the end of 2017. To service this growth and that of anticipated future growth we have increased the number of professionals in research, portfolio management, trading and administration. We have also made significant investments in technology to maintain our position at the cutting edge of advances in all areas. This has positioned AHB to be able to serve our current clients as well as the anticipated growth in new clients and assets under management we expect going forward.

Our good wishes for both a Happy & Healthy New Year to you and your loved ones.