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“Minds are like parachutes. They only function when they are open.” *-James Dewar*

The U.S. equity and fixed income markets remained resilient during the third quarter. Despite this resiliency, client conversations often revolve around issues they fear will result in the demise of the current economic growth cycle. The primary concerns revolve around recent emerging market turmoil, ongoing trade tensions, the mid-term elections and the risk of overly aggressive monetary policy. In this edition of Viewpointe, we provide our thoughts on these topics and provide our outlook for the remainder of the year. We also highlight some recent changes that were made to our model portfolios. We conclude with a brief discussion regarding credit scores.

Economic Review - Growth Cycle at Risk?

While the U.S. economy appears to be on track to experience the strongest calendar year growth in over a decade, many clients are preoccupied with the many risks they fear could derail the current growth cycle. While we actively monitor a multitude of economic and market risks on an ongoing basis, four have come to the forefront in recent client meetings. These include recent emerging market turmoil, growing trade tensions, the upcoming mid-term election and the risk of overly aggressive monetary policy. We will discuss the first three risks in this section and will discuss monetary policy in the fixed income section of the newsletter.

The equity, bond and currency markets of several emerging market countries faced significant downward pressure during the third quarter. This market turmoil was largely spurred by a strengthening U.S. Dollar. A strengthening U.S. dollar simply means it takes more of a foreign currency to purchase one U.S. Dollar. This is significant due to the fact many emerging market countries owe a significant amount of debt that is denominated in U.S. Dollars. In short, as the U.S. Dollar strengthens paying down this debt becomes more expensive for these countries.

Perhaps the situation that received the most attention was what transpired in Turkey. While Turkish debt had been downgraded earlier in the year, their economic crisis kicked into high gear in August in reaction to the Trump administration’s doubling of tariffs on Turkish imports. The combination of a strengthening U.S. Dollar combined with these tariffs increased the likelihood that Turkey could default on upcoming debt payments. This led to fears of default contagion and talk of a potential debt crisis. Contagion fears revolved around the fact that financially vulnerable countries, such as Italy, have material exposure to Turkish debt. Many feared that a Turkish default could in-turn trigger defaults in these countries, which in turn could lead countries that held their debt to default and so on.

Fortunately, thus far it appears contagion fears have been contained within emerging market economies. Developed market junk bond debt has held up rather well. In addition, most emerging markets have significantly recovered from their August lows following offers from the World Bank and various countries to offer financial assistance. At the present time we are of the opinion this situation is under control for the time being. We, however, do not rule out the possibility of a future flare up some time in 2019 or later.

Another topic that clients routinely bring up revolves around growing trade tensions. While the Trump administration appears to have made some progress on the trade front, many hurdles still lie ahead. In July, they appear to have concluded the U.S. could not fight a trade war on three fronts (China, European Union and NAFTA). As a result, the current strategy appears to take more of a one at a time approach with the first focus being on NAFTA. The strategy regarding NAFTA was to first negotiate with Mexico and reach a tentative deal. The idea behind this strategy is that a U.S./Mexico deal would force Canada to make more concessions. Thus far, the strategy appears to be working. Since a tentative deal has been struck with Mexico it appears the Canadians are

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more willing to negotiate on some of the prior sticking points. Our research sources are of the opinion that a NAFTA agreement will be finalized sometime during the first quarter of 2019.

The general consensus is that a deal with the European Union and China will be harder to come by. While some recent progress has been made with the European Union, negotiations with China appear to have hit a road block. It appears that China is focused on not seriously sitting down until after the mid-term elections. This strategy is based upon their presumption that Trump will be weakened by the mid-term election results. Ultimately, we believe trade negotiations will drag into 2019 and perhaps beyond. With that said it is important to note that fiscal policy stimulus in the form of tax reform and increased federal spending has dwarfed the extent of the tariff drag thus far. As trade talks drag on and fiscal policy begins to fade, we see trade issues becoming a larger threat to the current growth cycle. We, however, view this as more of a late 2019 or 2020 issue.

Last but not least are concerns regarding the upcoming mid-term election. The general issue here is the belief that if Trump has a tense relationship with his fellow Republicans, how is he expected to get along with Democrats? While Republicans are currently expected to hold onto the Senate, betting odds currently place a 70 percent probability of the Democrats taking over the House. If this comes to fruition, it will mark the 6th time in seven elections that U.S. voters removed the party in power.

Assuming the Democrats take the House we believe they will be able to find some common ground with the Trump administration on some major issues. Two key issues that come to mind are trade and infrastructure. Let's face it, Trump is not your stereotypical Republican. Historically it has been the Democrats who have taken issue with unfair trade. We see this as a key point where the Democrats and Trump could potentially work together. In addition, on the infrastructure front the Democrats have plans to introduce a major infrastructure bill. Trump has already stated that he supports many of the projects covered in the proposed bill. In short, a divided government does not necessarily mean the end to positive fiscal policy.

In conclusion, the above mentioned concerns do not alter our growth forecast for 2018. We still expect to see a growth rate of 3% or higher for the current calendar year. With that said we continue to monitor a multitude of risks to determine their possible impact on future years. We become more concerned when we look out to 2020 where we believe economic momentum is more vulnerable in the event capital expenditures do not materially pick up.

Fixed Income Commentary - Full Steam Ahead?

A strong August jobs report kept the Fed in the mood for hiking interest rates. With the August U.S. unemployment rate registering a mere 3.9% and wage growth up 2.9% it was pretty much a given that the Fed was going to raise the Fed Funds rate in September. September marks the third rate hike of the year and at the present moment markets are pricing in roughly a 70% probability of another rate hike in December.

Thus far, pro-growth fiscal policy has given the Fed ample cover to normalize interest rates without any noticeable negative domestic economic impact. Unfortunately, the same can't be said for emerging markets who were the direct casualty of a strengthening U.S. dollar fueled by higher interest rates here at home. Regardless, thus far the Fed's attention has been focused on the domestic impact of higher interest rates. With the U.S. in a strong patch the Fed is of the opinion the economy can withstand higher rates and thus far conditions have not indicated otherwise. The Fed is taking advantage of this opportunity to normalize the U.S. rate environment.

While we are of the opinion the U.S. economy can absorb a December hike, we are concerned with the Fed's outlook of three rate hikes in 2019. We believe if the Fed moves forward with such a strategy we will be at risk of an inverted yield curve scenario. This concerns us since such a scenario has a historical high probability of leading to a significant economic downturn. We are especially vigilant since much of the Fed's success with hiking rates is based on the fact the drag of higher rates has been overcome by increased government spending and favorable tax policy. In the event the Democrats obtain a majority in the House, we see an increased probability of a debt-ceiling fight. In such an environment it will be difficult to implement new policy on a scale large enough to replace that which rolls off. In the event this accommodative policy goes away or is greatly reduced, we are of the opinion the remaining growth drivers will be insufficient to overcome the drag of three rate hikes in 2019. In addition, it is important to note that absent a material uptick in capital expenditures we expect economic growth in 2019 to drift back down to the 2% level. This also indicates that three rate hikes would be excessive.

In conclusion, we see an overly aggressive Fed as a key risk next year and view an inversion of the yield curve as a serious threat. We are hopeful the Fed recognizes that additional accommodative fiscal policy is not a done deal and that economic growth will be harder to come by post-election. Assuming that to be the case, we are hopeful the Fed may begin to soften their rhetoric and adjust their 2019 forecast at their December meeting.

Equity Commentary -
Lower Returns on the Horizon?

Equity performance was spotty during the third quarter. While U.S. stocks performed extremely well, international stocks did poorly. For example, while the S&P 500 was up roughly 7% between July 1st and September 14th the MSCI EAFE Index (developed international) and MSCI Emerging Markets index were down -.57% and -2.93 % respectively. A similar story holds true on a year-to-date basis with the S&P 500 coming in at about 10% and both international indices falling well within negative territory.

While as of mid-September, the major U.S. large-cap, mid-cap and small-cap indices were all comfortably in positive territory for the third quarter. Large-cap and small-cap stocks were definitely the standouts, both registering around 7%. Mid-caps however were no slouches coming in just under 5%. All in all domestic equities performed much better than anticipated during the third quarter. This is even more impressive due to the pattern of weak equity market performance that oftentimes occurs during the latter summer months as well as the downward pressure that often takes place during the lead up to a mid-term election.

We identified several factors that we believe led to the large performance deviation between foreign and domestic stocks. First off, and perhaps most importantly, is the simple fact that while the U.S. economy is experiencing an impressive growth spurt, most other world economies are stagnant at best. It is also important to note the recent reduction in the corporate tax rate led to a sizeable increase in earnings growth. This made domestic stock valuations more attractive in comparison to where they stood prior to the tax law change. In addition, thus far U.S. stocks have not reacted to trade war fears anywhere near the level to which foreign stocks have. Lastly, U.S. stocks remain more attractive than bonds for U.S. investors. The combination of these factors led to outperformance versus international markets.

While we do not see the U.S. equity market as overvalued at present levels, we do not view it as cheap either. All in all, we see U.S equity markets as fairly priced. Unfortunately, while we take some comfort in current valuations we do believe they limit the upside. We become more concerned when we look out to 2019 where earnings growth will likely be hard to come by after the lower corporate tax rate has played out. This combined with a lackluster global economic backdrop make us question whether we are entering a phase of lower equity market returns

Asset Allocation -
Staying Active

We rebalanced our Classic model portfolios at the end of June. This rebalance was focused on replacing the Aquila Mid-Cap Growth fund with the Carillon Eagle Mid-Cap Growth fund. The reason for this change was highlighted in the previous edition of Viewpointe. Overall the other trades that took place during this rebalance were relatively insignificant.

We also made some changes to our Political Activism individual stock portfolio in July. As you may recall this portfolio consists of 50 individual stocks selected based upon political contributions as well as several credit related factors. When we ran our third quarter screen one name had fallen off due to its recent acquisition. In addition, two names had dropped off due to the fact they had lobbied hard to defeat the introduction of a Border Adjustment Tax. When the threat passed they significantly decreased their political contributions in the second quarter, resulting in a significant drop in rank. The remaining names removed were simply beat out by companies that were either recently added to the S&P 500 or companies that had been in the S&P, but significantly increased their political contributions. We removed these old names and introduced new names in the early days of July at the same time that we added the Carillon Eagle fund to the Premier portfolios.

We currently have no changes in the works for our Classic or Premier portfolios. On a year-to-date basis we are happy with how we are stacking up versus benchmark. We are especially pleased since once again industry data shows that active managers are having a hard time keeping up with benchmarks this year.

While we had kicked around the idea of increasing our international equity weight we have decided to wait for the time being. This is a strategy that is being widely discussed in the industry as a result of the more favorable valuations offered by international stocks. We, however, have decided to wait until foreign economies demonstrate more favorable prospects. A key factor that we are monitoring is Fed policy here at home. As long as the Fed continues to move forward with their mission for higher rates we expect foreign economies to be pressured by a strengthening U.S. Dollar. In the event the Fed starts to indicate a slowdown in rate hikes we will take a more serious look at increasing our foreign equity exposure.

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Financial Planning -

All About Credit Scores

It is difficult to imagine functioning in today's world without credit. Whether buying a car or purchasing a home, credit has become an integral part of our everyday lives. Having easy access to credit goes hand in hand with having a good credit score, so it is important to know how to maintain a positive credit score and credit history.

The importance of having a good credit score

Your credit score is based on your past and present credit transactions. Having a good credit score is important because most lenders use credit scores to evaluate the creditworthiness of a potential borrower. Borrowers with good credit are presumed to be more trustworthy and may find it easier to obtain a loan, often at a lower interest rate. Credit scores can even be a deciding factor when you rent an apartment or apply for a new job.

How is your credit score determined? The three major credit reporting agencies (Experian, Equifax, and TransUnion) track your credit history and assign you a corresponding credit score, typically using software developed by Fair Isaac Corporation (FICO).

The most common credit score is your FICO score, a three-digit number that ranges from 300-850. What is a good FICO score? For the most part, that depends on the lender and your particular situation. However, individuals with scores of 700 or higher are generally eligible for the most favorable terms from lenders, while those with scores below 700 may have to pay more of a premium for credit. Finally, individuals with scores below 620 may have trouble obtaining any credit at all.

Factors that can negatively impact your credit score

A number of factors could negatively affect your credit score, including:

- A history of late payments.

  Your credit report provides information to lenders regarding your payment history over the previous 12 to 24 months. For the most part, a lender may assume that you can be trusted to make timely monthly debt payments in the future if you have done so in the past. Consequently, if you have a history of late payments and/or unpaid debts, a lender may consider you to be a high risk and turn you down for a loan.

- Not enough good credit.

  You may have good credit, but you may not have a substantial credit history. As a result, you may need to build your credit history before a lender deems you worthy of taking take on additional debt.

- Too many credit inquiries.

  Each time you apply for credit, the lender will request a copy of your credit history. The lender's request then appears as an inquiry on your credit report. Too many inquiries in a short amount of time could be viewed negatively by a potential lender, because it may indicate that you have a history of being turned down for loans or have access to too much credit.

- Uncorrected errors on your credit report.

  Errors on a credit report could make it difficult for a lender to accurately evaluate your creditworthiness and might result in a loan denial. If you have errors on your credit report, it is important to take steps to correct your report, even if it does not contain derogatory information.

Fixing credit report errors

Since a mistake on your credit report can negatively impact your credit score, it is important to monitor your credit report from each credit reporting agency on a regular basis and make sure all versions are accurate.

If you find an error on your credit report, your first step should be to contact the credit reporting agency, either online or by mail, to indicate that you are disputing information on your report. The credit reporting agency usually must investigate the dispute within 30 days of receiving it. Once the investigation is complete, the agency must provide you with written results of its investigation. If the credit reporting agency concludes that your credit report does contain errors, the information on your report must be removed or corrected, and you will receive an updated version of your credit report for free.

If the investigation does not resolve the issue to your satisfaction, you can add a 100-word consumer statement to your credit file. Even though creditors are not required to take consumer statements into consideration when evaluating your creditworthiness, the statement can at least give you a chance to tell your side of the story.

If you believe that your credit report error is the result of identity theft, you may need to take additional steps to resolve the issue, such as placing a fraud alert or security freeze on your credit report. You can visit the Federal Trade Commission (FTC) website at ftc.gov for more information on the various identity theft protections that might be available to you.

Finally, due to the amount of paperwork and steps involved, fixing a credit report error can often be a time-consuming and emotionally draining process. If at any time you believe that your credit reporting rights are being violated, you can file a complaint with the Consumer Financial Protection Bureau (CFPB) at consumerfinance.gov.