

Economic & Market Review
~ THIRD QUARTER 2016 NEWSLETTER ~
EXECUTIVE SUMMARY

Considering the capital market turbulence ushered in during the first half of 2016, investment returns through the end of the third quarter were nothing short of remarkable. All major asset classes, worldwide, have delivered not only positive returns, but in some cases results in excess of even the most positive prognosticators. Moreover, investments previously shunned, questioned, or doubted by investors, such as commodities, emerging markets, and international bonds, delivered the strongest returns to those investors with well diversified portfolios.

If the first and second quarters were distinguished by their volatility, the third quarter was notable for just the opposite. In July, bonds rallied on falling interest rates, and equity markets climbed a "wall of worry." Yields on U.S. government 10-year and 30-year debt plumbed historic lows and U.S. stocks hit new all-time highs during the month. International gains were even more substantial.

August presented the lowest investment market volatility many investors have experienced in their lifetimes. The S&P 500 index traded within its tightest 30-day range since December 1965, and the yield on the 10-year U.S. Treasury note moved in its narrowest range in over a decade. Low volatility levels such as these have only been seen a handful of times over the past half century.

Central banks stirred calm waters in September, but most investments fared well.

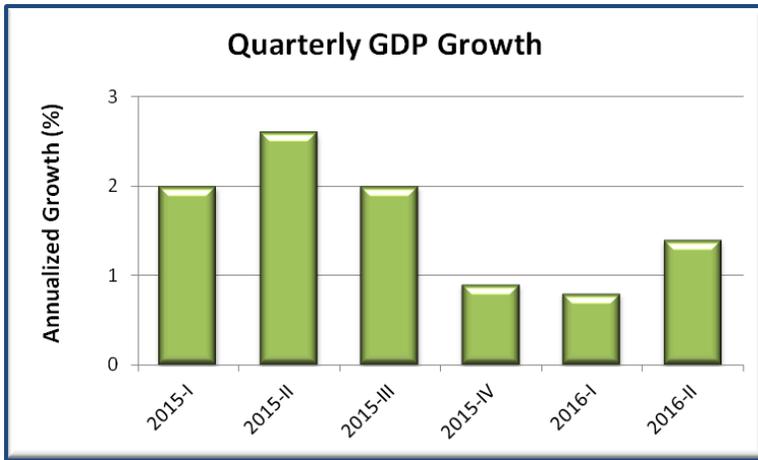
The exceptions were higher yielding investments such as longer dated bonds, real estate, and some dividend focused strategies. Though even these lagging strategies experienced only modest declines.

Looking forward, U.S. economic fundamentals look reasonable. Labor markets continue to improve and the consumer appears healthy. The housing market hit an air pocket in the second quarter and price gains have slowed, yet interest rates are supportive and sentiment remains positive. Most believe data for the third quarter will show a nice acceleration in GDP growth and expectations call for an overall reading of accelerated economic growth in the second half of 2016. Analysts also expect the fourth quarter to show corporate earnings growth following six consecutive quarters of year-over-year declines.

Aside from the upcoming election, which will likely drive some market volatility, policymakers will be front and center for some time to come. The Federal Reserve has telegraphed a rate hike prior to year-end. Most investors expect this to take place at the group's December meeting. Eyes will also be on the European Central Bank and the Bank of Japan. Recent actions by both organizations have underwhelmed investors, leaving many to wonder if they are running out of either the will, or the capacity, to do more. Meanwhile, as austerity falls by the wayside, it appears increasingly likely that the role of monetary policy will begin to diminish while nations increasingly turn to fiscal tools to coax progress out of growth challenged economies.

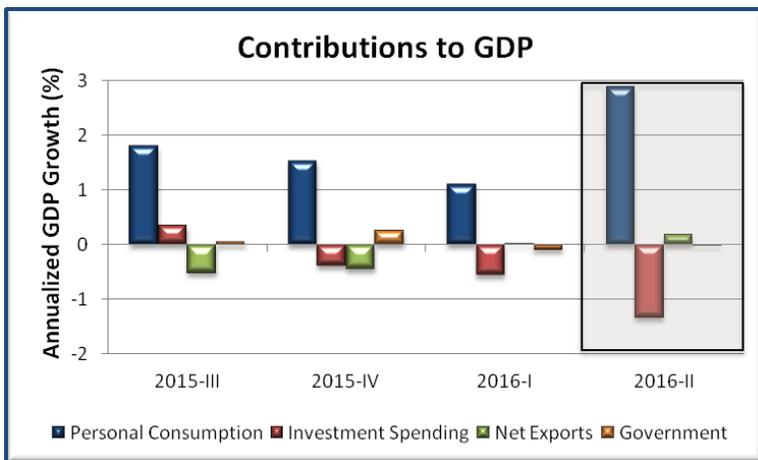
ECONOMIC REVIEW AND OUTLOOK

Key Economic Fundamentals



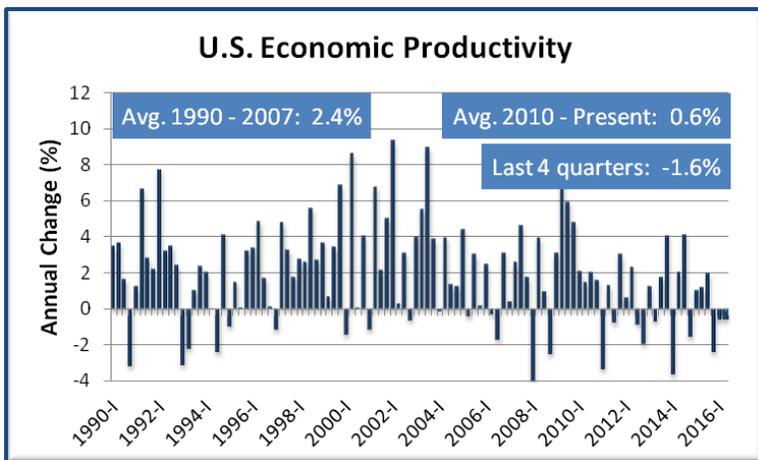
Data Source: U.S. Department of Commerce

Annualized second quarter U.S. GDP growth of 1.4% proved surprisingly tepid against original expectations of 2.6%. Married with an even weaker first quarter, it was the nation's slowest start to a year since 2011. Expectations call for faster growth in the second half of 2016, starting with a forecast of 3% in the third quarter.



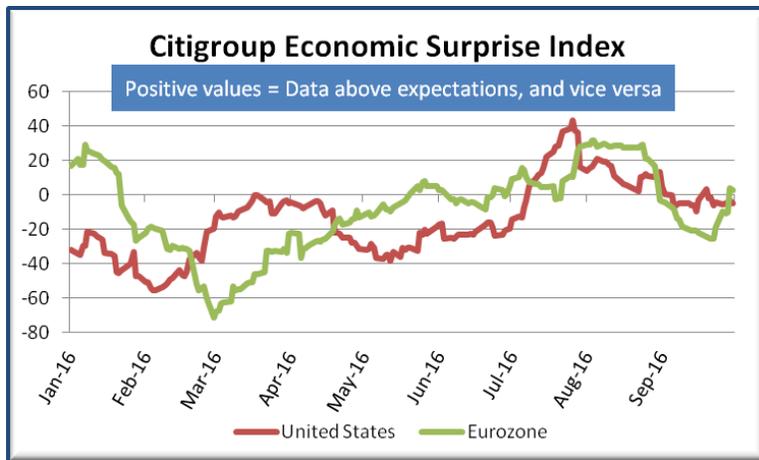
Data Source: U.S. Department of Commerce

Growing at its second fastest quarterly pace since the recession, personal consumption accounted for over 200% of Q2 growth! Government and investment spending were weak, housing investment declined for the first time since early 2014, and inventories outright contracted for only the second time dating back to 2010.



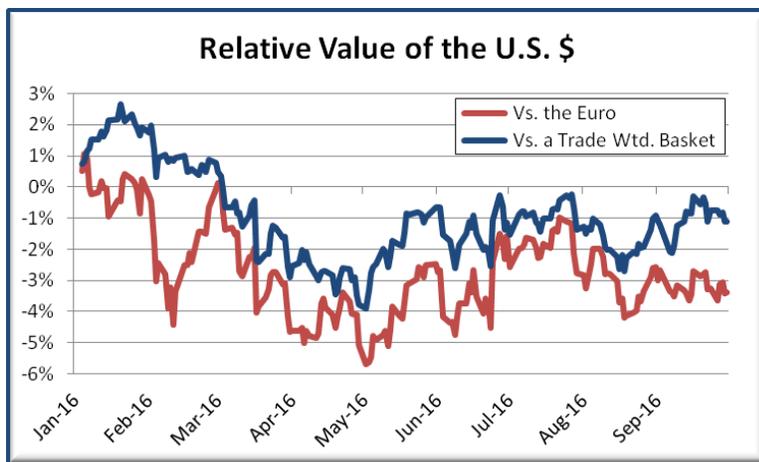
Data Source: U.S. Bureau of Labor Statistics

Long-term economic growth is a function of labor force growth and worker productivity. In addition to unfavorable demographic trends in the U.S., tepid post-crisis growth stems from the stunning decline in productivity shown to the left. Government policies, regulation, and business investment all impact productivity significantly.



Data Source: Citigroup

Relative to previous periods, forecasts of economic results proved fairly accurate in the third quarter. If anything, actual results for both the U.S. and Europe generally exceeded expectations for the first time this year. Favorable investment outcomes and lower market volatility resulted.



Data Source: U.S. Federal Reserve

The dollar's strengthening in recent years has given way to stabilization, if not weakness, in 2016. The change in trend has been a welcome respite for manufacturers, multinational companies, U.S. policymakers, and globally diversified investors.

Global Growth Rates¹ (%)

	Q2 2016	Q3 2016	Q4 2016	2015	2016	2017
Advanced	1.6	1.6	1.7	2.0	1.6	1.8
Euro²	1.1	1.1	1.2	1.6	1.5	1.3
U.S.²	1.3	1.5	1.8	2.6	1.5	2.1
Japan²	0.7	0.5	0.5	0.5	0.6	1.0
U.K.²	2.1	1.9	1.2	2.2	1.8	0.9
Canada²	2.3	2.1	2.2	1.2	2.0	1.8
Emerging	4.3	4.5	4.8	4.2	4.5	5.2
China	6.7	6.6	6.6	6.9	6.6	6.4
India	7.1	7.9	7.9	7.5	7.8	8.0
Russia	-0.6	0.2	1.8	-3.7	0.0	2.6
Brazil	-3.8	-2.4	-1.1	-3.8	-3.2	1.1
World	3.0	3.1	3.3	3.1	3.1	3.5

Data Source: Goldman Sachs, Central Intelligence Agency

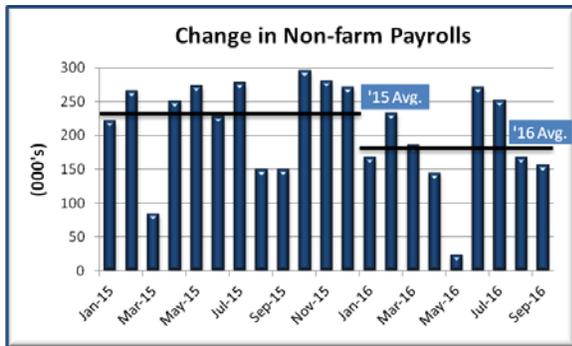
¹Q2 2016 and 2015 are actual, all others are forecasts

²Quarterly numbers are sequential annualized, others are year-over-year

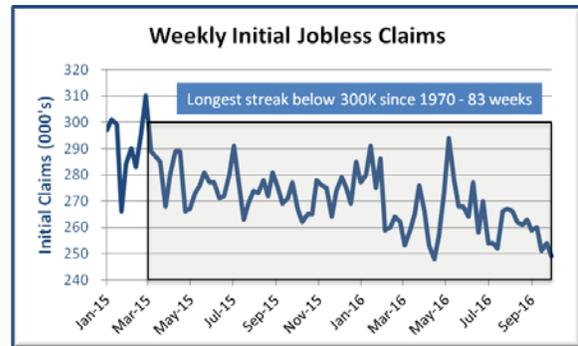
Economic growth in the three largest economies (Euro zone, U.S., and China) has slowed this year, as expected. Forecasts of a net deceleration in advanced economies has generally been offset by emerging nations. Strong and accelerating growth in India, as well as "less bad" results out of Russia and Brazil, have been key drivers.

Employment

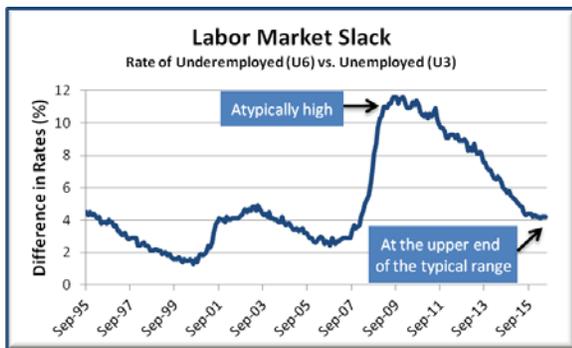
Aside from an aberrant result in May, the U.S. labor market continues to improve. Net payroll growth, while somewhat slower than last year, continues to exceed the pace of population expansion. Workers are more mobile, willing to leave jobs for better opportunities, while employers are reluctant to let workers go. Labor market slack has diminished and the percentage of individuals participating in the labor force has bounced off of the low set at this time last year. A stable unemployment rate, at the Federal Reserve's target, has resulted. Importantly, wage gains have accelerated as well. The growth rate of nominal wage gains has accelerated over the past year, and inflation adjusted wage contraction from years ago has reversed to expansion in recent periods. Considering these improvements, and the increasing potential for wage related inflationary pressures, the Federal Reserve is expected to raise interest rates before year end.



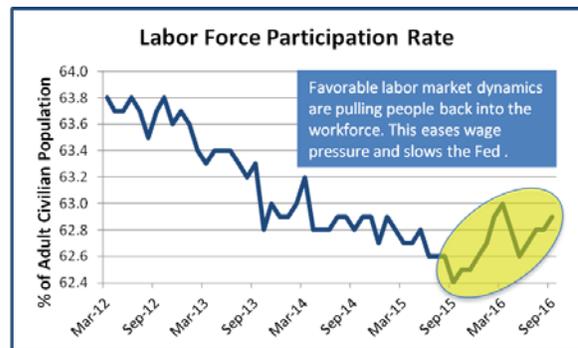
Data Source: U.S. Department of Labor



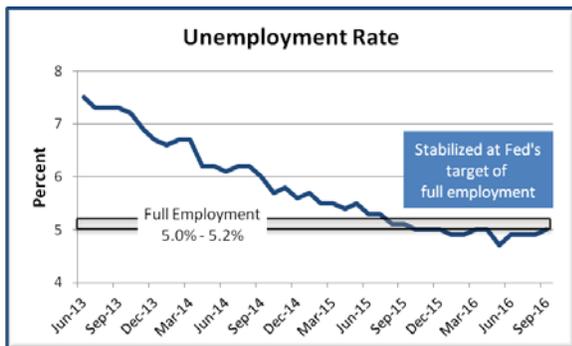
Data Source: U.S. Department of Labor



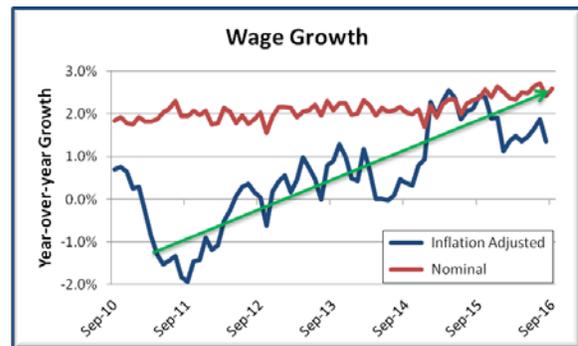
Data Source: U.S. Department of Labor



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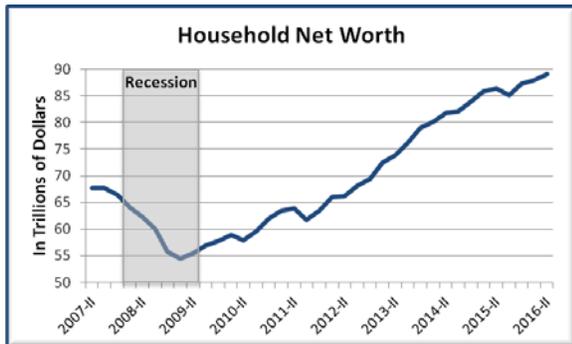
Data Source: U.S. Department of Labor



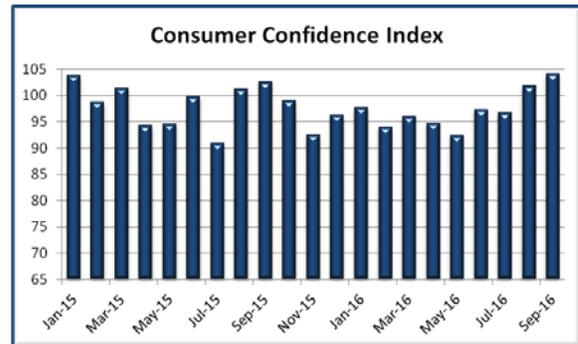
Data Source: U.S. Department of Labor

Consumer

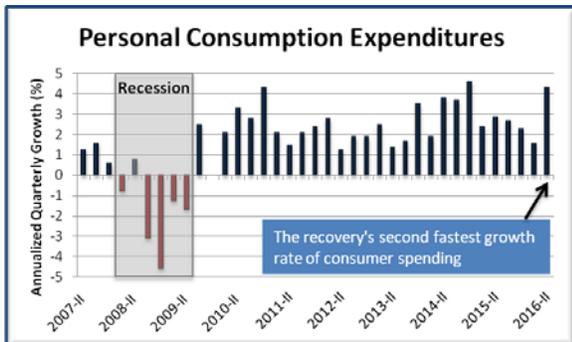
Low interest rates, more jobs, higher wages, cheap gasoline, and a new all-time high in household wealth have all contributed to the U.S. consumer remaining relatively resilient and confident. September marked the highest post-recession level of consumer confidence, and second quarter personal consumption expenditures grew at nearly the fastest pace of this recovery. Despite the positives, it is notable that consumer spending and retail sales have been soft in recent months. In particular, auto sales have posted year-over-year declines in five of the past seven months. It remains to be seen whether these trends are simply election year jitters or something more ominous.



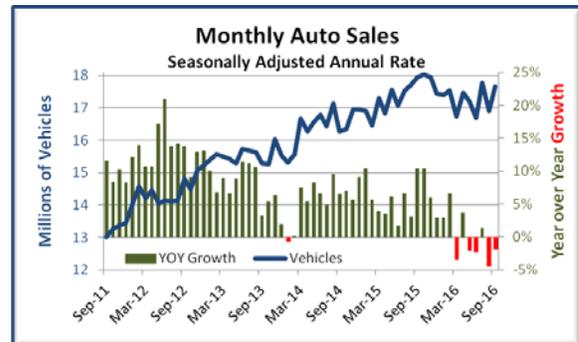
Data Source: U.S. Federal Reserve



Data Source: The Conference Board



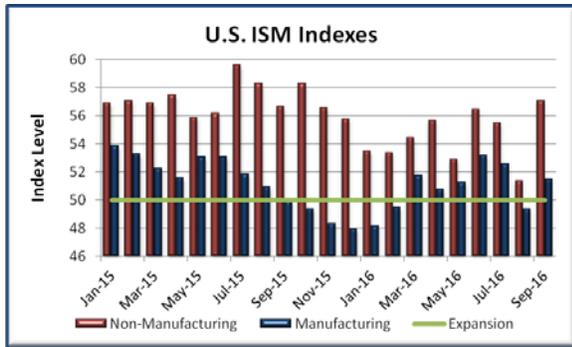
Data Source: U.S. Bureau of Economic Analysis



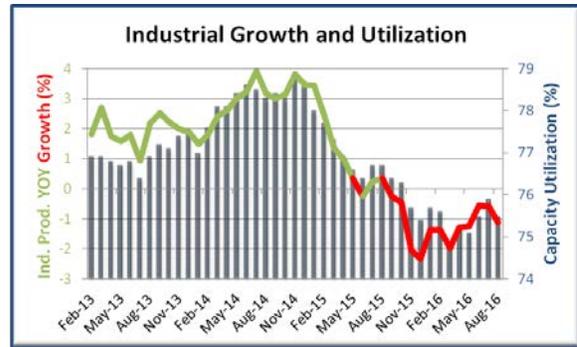
Data Source: Bloomberg

Business Activity

As shown by the ISM graph on the following page, business activity has slowed and become somewhat more erratic. Over the past year, manufacturing has vacillated between expansion and contraction, and the service sector is less vibrant this year than last. Industrial production has been in decline for nearly two years and capacity utilization, while possibly stabilizing, shows no signs yet of improvement.



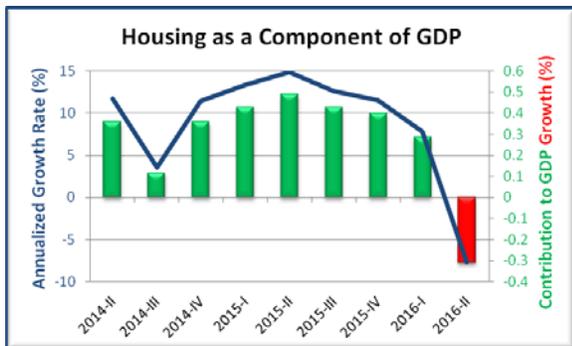
Data Source: Institute for Supply Management



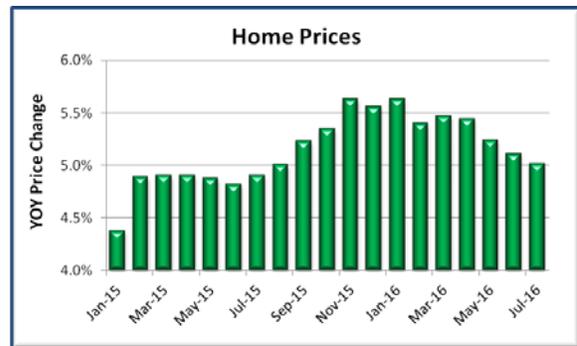
Data Source: U.S. Federal Reserve

Real Estate

Along with the consumer, housing has been a pillar of U.S. economic strength in recent years. That said, recent data suggests a somewhat murkier outlook for housing. Investment in residential housing cratered in the second quarter, becoming an actual drag on GDP growth for the first time in over two years. Housing price gains are slowing as well. Half of the nation's real estate markets have experienced falling prices since May, and year-over-year price gains have been trending lower throughout 2016. Despite the negatives, home builder sentiment — a reliable leading indicator — hit another new post-crisis high in September. Likewise, mortgage rates have fallen throughout 2016 to the lowest level since May 2013. In short, the jury is still out on housing. Considering the segment's economic importance, developments deserve our attention.



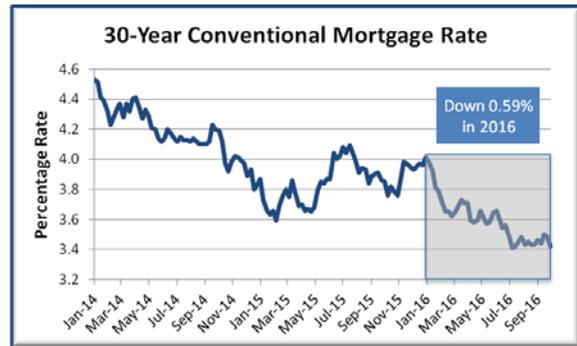
Data Source: U.S. Census Bureau



Data Source: S&P/Case-Shiller



Data Source: National Association of Home Builders



Data Source: U.S. Federal Reserve

CAPITAL MARKETS REVIEW

Returns

	3 rd Qtr 2016	YTD 2016
Cash and Fixed Income		
U.S. Treasury Bills	0.1%	0.2%
Barclays U.S. Aggregate Bond	0.5%	5.8%
Barclays Municipal Bond	-0.3%	4.0%
Barclays Global Agg. ex. U.S.	1.0%	13.1%
Hedge Funds and Alts.		
Bloomberg Commodity	-3.9%	8.9%
DJ US Real Estate	-1.1%	11.0%
HFR1 FOF Composite	2.5%	-0.1%

Data Sources: Morningstar & Hedge Fund Research, Inc.

	3 rd Qtr 2016	YTD 2016
Domestic Equities		
Wilshire 5000	4.3%	8.4%
S&P 500	3.9%	7.8%
Russell 2000	9.0%	11.5%
International Equities		
MSCI ACWI ex. U.S.	7.1%	6.1%
MSCI EAFE (Developed)	6.4%	1.7%
MSCI EM (Emerging)	9.0%	16.0%

Equity Markets

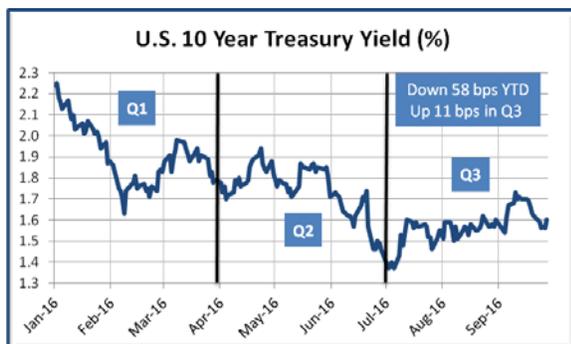


Data Source: S&P Dow Jones Indices LLC

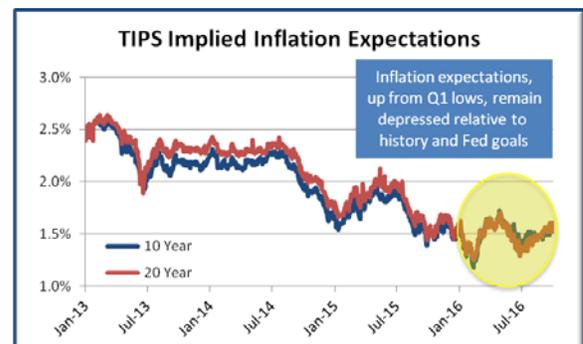


Data Source: Morningstar

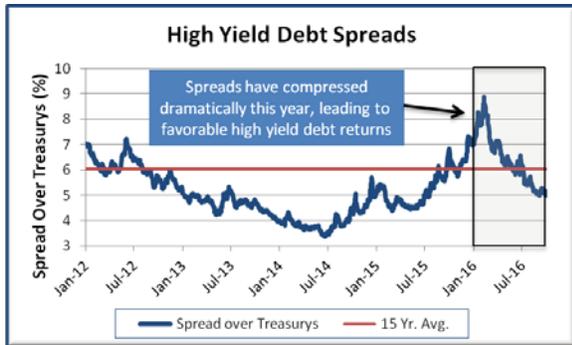
Fixed Income Markets



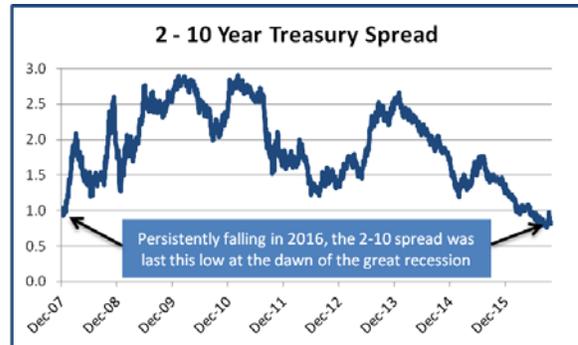
Data Source: U.S. Department of the Treasury



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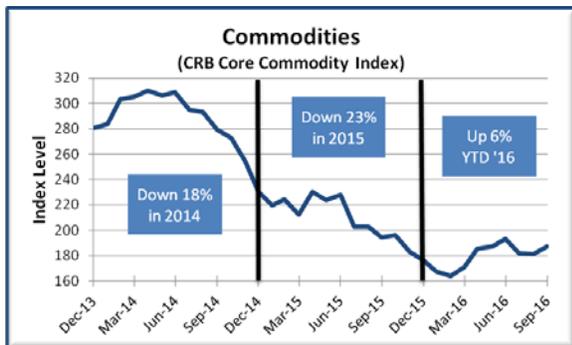


Data Source: BofA Merrill Lynch

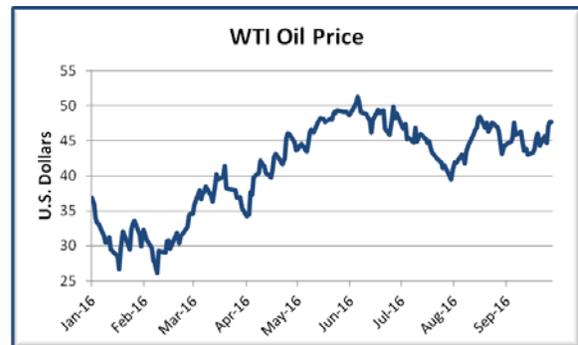


Data Sources: U.S. Department of the Treasury

Alternatives



Data Source: Thomson Reuters



Data Source: US. Energy Information Administration

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