



**“For our society to get better, we need people who succeed. We shouldn’t be jealous of them, we should say ‘fantastic’.”**

French President Emmanuel Macron

2017 was a remarkable year in many ways. From a market perspective, perhaps the most surprising was the emergence of a 39-year old former investment banker rising from political obscurity to claim the French Presidency. The year opened with a cloud of malaise hanging over Europe and an anti-European Union (EU), populist candidate (Marine LePen) high in the French polls. This was on the heels of Britain voting to leave the EU. Many thought Frexit the logical successor to Brexit. Instead, the year ended with Macron pushing through labor reforms.

After consecutive earnings declines in 2015 and 2016, Europe’s top 600 companies are expected to exit 2017 with 13% growth with views of 7-10% growth in 2018<sup>a</sup>. Even Greece, seen as the basket case of Europe, has rebounded and has seen the yield on its 2-year bonds drop to below that of U.S. 2-year Treasuries at 1.9%<sup>b</sup>.

Across the globe, much more went right than not:

**China** – Housing development has underpinned growth in recent years and many are concerned about overbuilding and the resulting vacant commercial housing. Fears of a Chinese slowdown spiked in early 2016 when vacant housing peaked at 450 million square meters. Government support has helped bring down inventories to their lowest level since 2013 at 300 million square meters<sup>a</sup>.

**U.S. Dollar** – A year ago, expectations were that the dollar would strengthen as the Federal Reserve was the only central bank embarking on rate hikes. Instead, the dollar weakened nearly 10% against a basket of foreign currencies as global growth was surprisingly strong<sup>b</sup>. For U.S. investors, the weaker dollar helped propel non-U.S. financial assets higher and U.S. multi-national companies earned fatter profits on their overseas earnings.

**Inflation** – Despite low U.S. unemployment, worker’s wage increases were mild. Energy prices rose but not by much. Overall, interest rates stayed low and range bound throughout the year.

a. Wall Street Journal Year-End Review & Outlook, January 2, 2018.

b. Bloomberg

c. Reuters “U.S. tax cut to deliver corporate earnings gift” 12/19/2017.

d. BusinessInsider “A record year for the S&P 500” 12/29/2017

e. National Institute of Statistics, Italy Hourly Wage Inflation. Since 2012, wage inflation has been below 2%.

**Tax Cuts** – After several legislative impasses, Congress struck a business friendly bill that makes the tax code more competitive on the world stage. Companies primarily doing business in the U.S. gain from lower rates while larger multi-national firms can now repatriate overseas earnings with less tax impact. The market has likely priced in what many believe is a 7-10% bump in 2018 earnings as a result<sup>c</sup>.

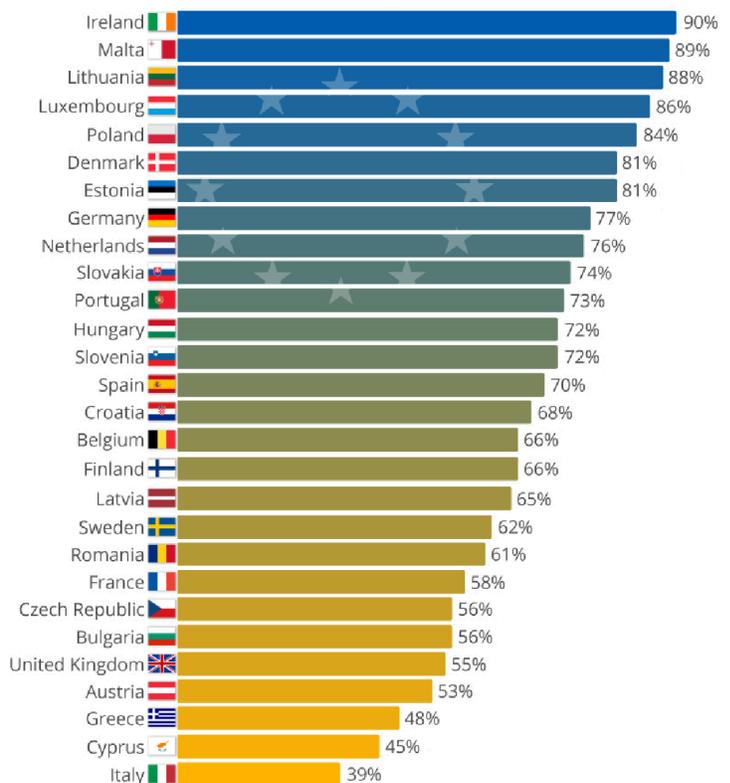
The upshot was the first global synchronous economic expansion since 2009 and strong equity returns world-wide. Volatility was at its lowest point in at least a decade<sup>a</sup> as the S&P 500 posted gains during each month of 2017. That has never happened before<sup>d</sup>.

**2018 – Don’t expect an encore**

The strong global economic expansion and business momentum suggests strong underlying support for the equity markets as we enter 2018. Whereas developments broke in a market friendly way in 2017, what are areas to consider in 2018?

**Italy** – Whereas the French election took European concerns off the table in 2017, Italy could bring long-term EU stability concerns back into question. Italians have the lowest public opinion of the EU. Wages have been static in recent years<sup>e</sup> and many voters may want change. Their chance to vote comes March 4.

**Who Feels EU Membership has Paid Off?**  
Share agreeing their country has benefited from being in the EU



As of 2017. Sources: Statista, European Parliament.  
www.statista.com/chart/11574/who-feels-eu-membership-has-paid-off

**Middle East** – While attention has been focused on the Korean peninsula, long-simmering tensions are flaring between Saudi Arabia and Iran. Recent protests in Iran and a new leader in Saudi Arabia suggests instability could roil the oil markets if the conflict escalates.

**Central Banks** – Due to their role in setting the price of money, markets always pay attention to the central banks. Stronger economic growth may allow Europe and Japan to curtail and perhaps even end their quantitative easing programs. In the U.S., a new Federal Reserve (Fed) chairman (Jerome Powell) and other newly elected voting members are expected to continue raising rates. If wage growth percolates higher, the Fed may move more aggressively than anticipated. Overall, global central bankers have been accommodative since the Great Recession and this boost is dissipating as we enter 2018.

We expect 2018 to be a ‘normal’ year with more muted returns and at least one bout of market volatility. Longer term, we still believe that bond yields will stay low and that equities will outperform. In our Global Asset Allocation strategies, we continue to hold a neutral position towards stocks and have kept the average maturity for bonds on the shorter side. Longer term, we would prefer to be overweight equities. One key reason for this view is that we believe in human ingenuity and progress. Equities, over the long term, is the asset class that best captures these collective advancements.

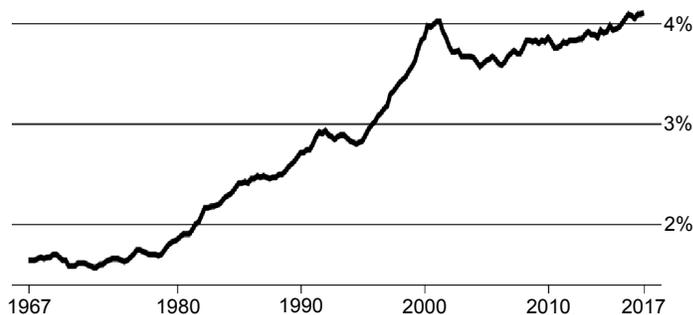
One small example can be seen in a \$14,000 sushi-making robot. Autec USA, a small company in California, makes a machine which churns out precisely calibrated beds of sticky rice onto a bed of seaweed. It helps a sushi chef make 200 rolls an hour, a great improvement from the 50 or so if made entirely by hand. This machine reduces the tedious part of sushi-making and makes life easier and more efficient for the chef.

U.S. Department of Commerce data shows investments like this in service-related equipment surpassed 4% of GDP last year, the first time since 2000<sup>f</sup>. Multiplied across an economy, these improvements will continue to incrementally drive productivity growth.

f. Bloomberg Businessweek “Robots are Making your Sushi, and That’s Good for the Economy” 12/19/2017.

g. RIA Channel ranked those firms with \$100M-\$500M in total Assets Under Management (AUM) that have grown by at least 30% over the past five years. Firms which met these criteria were ranked by their total AUM as of their most current assets reported to the SEC as of 10/31/2017. Of the 100 firms included on this list, Wellesley Investment Partners (WIP) was ranked #64. WIP did not pay a fee to participate in this survey. Ranking is not indicative of WIP’s potential future growth.

## U.S. Investment in Intellectual Property Products as a Share of GDP



Sources: Bloomberg Businessweek, U.S. Department of Commerce

Wellesley Investment Partners was recently named a Top 100 Emerging Wealth Manager by RIA Channel<sup>g</sup>. We feel this is a tangible result of the trust you have placed in us and we will continue to work hard every day to continue to earn that trust.

From everyone here, we wish you a healthy and prosperous 2018.

Regards,

Richard Siple, CFA  
Chief Investment Officer

Performance of Notable Indices	Q4	YTD
	2017	(1/1/17 – 12/31/17)
S&P 500 Index	6.6%	21.8%
U.S. Midcap Equities	6.3%	16.2%
U.S. Small Cap Equities	3.3%	14.7%
International Developed Market Equities	4.2%	25.0%
Emerging Market Equities	7.4%	37.3%
U.S. Core Bonds	0.4%	3.5%
Global Bonds	1.0%	7.1%
Gold, \$/troy oz	1.8%	13.1%

Total return indices unless otherwise stated.

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- This report is for the quarter ending December 31, 2017.