ECONOMIC HIGHLIGHTS

The PMI Composite Flash Index for February appears nicely expansionary, at 55.9 versus 54.0 consensus. There were no real surprises from the FOMC's January meeting minutes, with exception to the fact that committee members were more positive about the U.S. economic outlook than before. The Index of Leading Indicators would agree, having been up 1.0% in January versus +0.6% consensus.

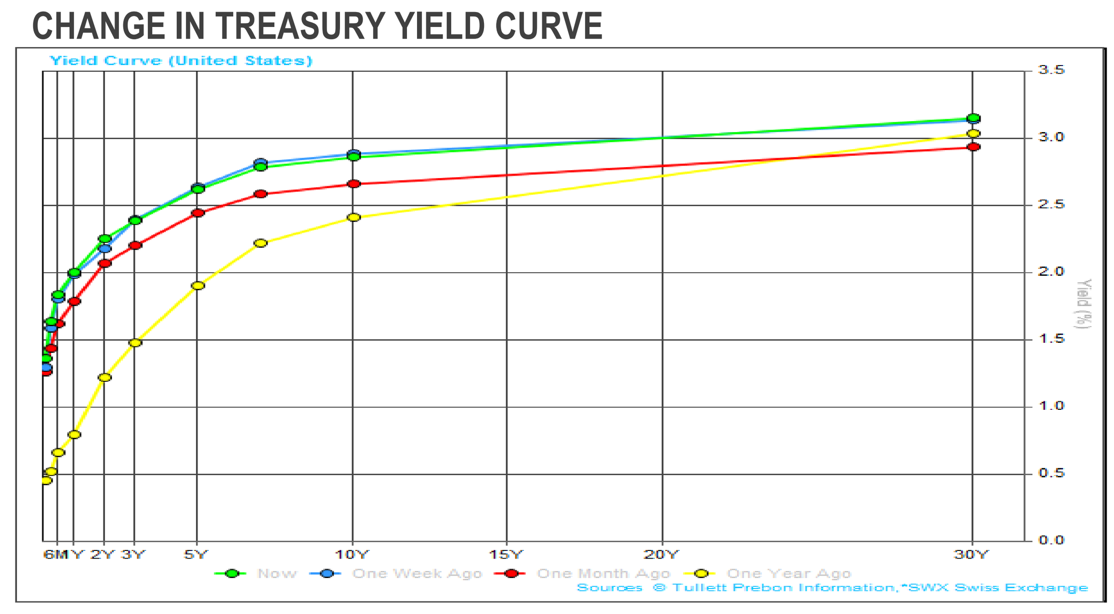
FIXED INCOME

Federal Reserve Bank of San Francisco President John Williams said he favors three or four interest-rate increases this year and policymakers should make a move soon. "It makes sense to think about three or four rate increases in 2018," Williams told reporters following a speech last Friday in Los Angeles. When asked if he would want to move at the Fed's next meeting, which is a two-day meeting starting on March 20, he declined to comment directly but said that "we should be moving ahead with a rate increase relatively soon, in the near future." Williams, who votes on monetary policy this year and has been interviewed by the White House for the post of Federal Reserve Vice Chairman, painted an upbeat picture of the U.S. economy, echoing recent remarks from other U.S. central bankers. Investors have essentially fully priced in a rate hike at the Fed's March meeting. Officials penciled in three rate moves this year in projections they submitted in December which will be updated next month. Investors will get a chance for a fuller description of the outlook when Jerome Powell delivers his first testimony to Congress as Fed chairman on Tuesday. Williams said the labor market could continue to pull some people from the sidelines and he expected productivity growth to pick up as investments rebound, while inflation should move up as temporary factors that weighed it down last year recede. Inflation, according to the Fed's preferred gauge, was 1.7% in the 12 months through December and has been below the central bank's 2% target for most of the last six years. Williams also said he's watching to see whether the neutral rate--a theoretical level that neither stokes nor slows growth--may head higher on the back of recent tax-cuts passed by Congress. Williams has made the case that the rate is much lower now than it's been historically. "Right now it's conjecture," he said, but "my view is that other fundamentals haven't changed in any way," so while the neutral rate may have moved higher in response to tax cuts, it would be by a relatively small amount.

CURRENT GENERIC BONDS YIELDS

TREAURIES		AGENCIES		CORPORATES		MUNICIPALS	
3 mo	1.64%	3 mo	1.66%	3 mo	2.05%	3 mo	1.20%
6 mo	1.84%	6 mo	1.74%	6 mo	2.14%	6 mo	1.27%
1 yr	2.00%	1 yr	2.00%	1 yr	2.26%	1 yr	1.34%
2 yr	2.24%	2 yr	2.21%	2 yr	2.54%	2 yr	1.53%
5 yr	2.62%	5 yr	2.51%	5 yr	3.05%	5 yr	2.04%
10 yr	2.87%	10 yr	3.20%	10 yr	3.65%	10 yr	2.70%
30 yr	3.16%	30 yr		30 yr	4.08%	30 yr	3.70%

CHANGE IN TREASURY YIELD CURVE



EQUITY

INDEX RETURNS	LAST WEEK	YTD
Dow Jones Industrials	0.36%	2.74%
S&P 500 (Large Cap)	0.58%	3.04%
S&P 400 (Mid Cap)	0.18%	0.37%
Russell 2000 (Small Cap)	0.38%	1.02%
NASDAQ Composite	1.36%	6.46%
MSCI EAFE (International)	-0.11%	1.46%
iShares Real Estate	-0.32%	-7.63%

Stocks continued their rally following the quick, early-February pullback – ending the week higher and booking back-to-back weekly gains. Most of last week's gain came on Friday when equity market rallied sharply as bond yields fell.

Last week was a decisively risk-on week for sector performance with cyclicals such as Materials, Technology, and Consumer Discretionary leading advancers. Defensive sectors such as Consumer Staples and Telecom fell the most. On the whole, 7 of the 11 major sector groups rose.

Wal-Mart was a drag on the Consumer Staples sector – falling over -10% on Tuesday after the company released an earnings report that showed slowing e-commerce growth. Revenue beat comps, but earnings and margins missed estimates.

The rebound in stocks from their February 9 lows has been very uneven according to data from Bespoke. They noted that of the eleven major sectors, Technology is just 3% from its prior high. Energy stocks have not recovered as much and are still more than 13% from their prior 52-week high. The only other sector more than 10% from its high is Utilities. Interestingly, the ten largest S&P 500 stocks are down an average of 6.5% from their 52- week highs, while the remaining 490 stocks in the index are down nearly twice as much from their 52-week highs (-11.7%).

The swift bounce off the early February lows was matched by equally swift moves in investor sentiment data. Bullish sentiment in the AAII Investor Sentiment Poll increased last week to 48.5% from its prior reading of 37.0% - that is the largest weekly increase since last September. Bearish sentiment plunged to 21.4% from 35.0% for its largest weekly decline in two years.

As this earnings season winds down, it is shaping up to be one of the strongest of the last 20 years. Bespoke wrote in a report that 69% of companies have beaten consensus earnings per share estimates, while 73.2% have beaten consensus revenue estimates. For EPS, the 69% beat rate is the highest since the third quarter of 2006 and the 6th highest over the past 20 years. For revenues, the 73.2% beat rate is the highest since the fourth quarter of 2004 and the fourth highest over the last 20 years.

For the week ahead, fourth quarter earnings are expected to be released from several retailers including Macy's, Lowe's, Foot Locker, and JCPenny's among others. On the economic front we will see new home sales on Monday and a second look at Q4 GDP and Chicago PMI on Wednesday. Core PCE index – one of the ways the Federal Reserve monitors inflation – will be released on Thursday.

Last week's rally was not enough to move the support and resistance levels we are watching for the S&P 500. For support, we are watching the following levels – 2700, 2645, 2600, and 2560. Resistance levels stand at 2790 and 2872 (all-time highs). The index finished last week at 2747.

ASSET ALLOCATION

CURRENT SENTIMENT	
Cash	Neutral
Short Fixed Income	Neutral
Intermediate Fixed Income	Neutral
Inflation-Adjusted Fixed Income	Unfavorable
High Yield Fixed Income	Neutral
International Fixed Income	Neutral
Equity Income	Favorable
Large Cap Equity	Favorable
Mid Cap Equity	Favorable
Small Cap Equity	Neutral
International Equity	Neutral
Emerging Markets Equity	Favorable
Real Estate	Favorable
Commodities	Unfavorable

Below is a summery of our current stance on most asset classes:

Cash - Holding as little as possible given the miniscule yields in money market instruments. Any exposure is for defensive positioning.
Short Term Bonds - Relative to Intermediate Bonds, the reduced duration is preferable given the outlook for higher interest rates.
Intermediate Term Bonds - The current trading range of intermediate bonds warrants a neutral position with limited upside potential. Some opportunities still remain present in spread products.
Inflation-Adjusted Bonds - Low inflation expected in near-term providing zero real return.
High Yield Bonds - Spreads have tightened; however, still remain attractive versus Treasuries.
International Bonds - Emerging market bonds offer good diversification qualities while providing higher yield opportunities relative to domestic fixed income.
Equity Income - High quality and higher-dividend-paying companies remain attractive for long-term investors given their favorable risk-adjusted profile and current yield curves.
Large Cap Stocks - A favorable weighting is recommended. Growth has reemerged as a more favorable style and should be overweighed versus Value.
Mid Cap Stocks - Mid cap exposure along with a value tilt is preferred. Mid cap stocks continue to provide the "sweet spot" of market capitalization - large enough to provide stability, but small enough to be more nimble.
Small Cap Stocks - In broad market corrections, small cap stocks will suffer most with increased volatility. However, a recent divergence of relative strength between small caps and large caps warrants a neutral exposure.
International Stocks - Given most foreign investment is in developed markets and European countries, until sovereign debt concerns are alleviated, an underweight to neutral weight is recommended.
Emerging Market Stocks - Stronger balance sheets, less debt, and better growth potential make emerging markets more fundamentally attractive than developed countries longer-term. Recent relative performance versus developed markets support the stronger fundamental backdrop and positions have been added.
Real Estate - Pricing has stabilized and long-term valuations appear attractive. Real Estate has performed well of late and should continue to be a strong alternative to other asset classes.
Commodities - Global demand should support higher prices if the global recovery remains on track. Although, volatility will be higher and commodities will be susceptible to short-term price shocks, if used in conjunction with other asset classes, risk can be reduced substantially to a diversified portfolio. However, used alone is not recommended as the short-term outlook is not favorable.