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ECONOMIC UPDATE - - THE FED PAUSE

The Federal Reserve's dual mandate is to promote the goals of maximum employment and stable prices. Its quarter point rate increase last week followed a year-long pause during which the economy experienced two quarters of tepid growth, well below the 2.0% trend of recent years. Incoming data now shows the economy, in the absence of stimulative fiscal policy, is probably better off for that pause, having grown at an annualized rate of 3.5% in the third quarter. Unemployment has fallen to 4.6% of the labor force, the lowest since August 2007. The labor force participation rate for 25 to 54 year-olds, which fell sharply after the recession and is still low by historical standards, has recovered about a third of its decline, after its fastest growth spurt since 1985. Inflation is also picking-up. Core CPI prices, which exclude food and energy, are up 1.7% from a year ago, still below the Fed's 2.0% target, but higher than the 1.4% since the Fed raised rates in December 2015. And, recently released forward looking data we monitor forecast a continuation of the stronger GDP growth. Both our firm's propriety Economic Model and the Leading Economic Indicators (LEI) confirm the improved trend. Based upon this outlook, all else being equal, we would expect the Fed to continue its rate normalization process next year with two or three additional 0.25% rate hikes.

Now, following Donald Trump's election, the Fed's job may have changed. Equity markets in the US have rallied to new highs, the dollar has surged and US Treasury yields have jumped in the anticipation of the large fiscal stimulus, tax reform, deregulation and repatriation promised by the new administration. Should Trump's fiscal stimulus cause the Fed to raise rates more quickly? Fed officials know they face risks in doing so. If they raise rates too rapidly there would be little room to significantly reduce them in the event the economy sours. It would, in our view, be unwise for the Fed to react too hastily to the mere prospect of fiscal easing. So, we believe they will remain cautious and data-dependent as, at this

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point, it is far too early to gauge how much and to what effect Mr. Trump's fiscal policy will impact the economy.

The Fed's caution in raising rates this year was well founded. Over the past year a strong dollar, fragile emerging markets and the risk of over-tightening have held the Fed back from more aggressively raising rates. Today the economy is on solid ground and the labor market tighter, so the rationale for further normalization is in place.

INVESTMENT POLICY

There is no change in investment policy. Portfolios remain fully-invested with the equity portion having significant concentrations in energy, financials, industrials and technology shares totaling well over 50% of the value of the investments. We have largely avoided shares of utilities, consumer staples, REITS and higher yielding stocks with limited organic growth prospects which have been hit hard by higher interest rates. We target up to15% of the equity portfolio in companies domiciled abroad in developed and emerging markets.

Fixed income portfolios, which have been invested with preservation of principal as the central theme, have shown positive returns during the recent sharp bond market down-turn. Bond portfolio durations remain highly defensive and are likely to remain so for the foreseeable future as we see rates continuing to rise.

Happy Holidays!!

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