August 2017

MEEDER INVESTMENT MANAGEMENT

Monthly Market Commentary

Discussion Points

- » Hurricane Harvey Blows Through Gulf Coast
- » Tensions with North Korea Heighten
- » Markets Continue to Climb A "Wall of Worry"

As of August 31, 2017

While it is still too soon to get specifics for the level of damage to all areas impacted by Hurricane Harvey, initial estimates from AccuWeather are looking at an economic impact of $160 billion. If accurate, this would be near the monetary equivalent of Hurricanes Katrina and Sandy combined, and would rank as the single most expensive natural disaster in U.S. history. This would represent an approximate hit of 0.8% GDP to the U.S. economy.

With respect to the physical enormity of Hurricane Harvey, according to the Washington Post, an estimated 19 trillion gallons of water have been dumped on the city of Houston and the surrounding Texas area. This compares to 6.5 trillion gallons that were produced throughout Hurricane Katrina. Trying to put 19 trillion gallons of water in relevant terms is not easy, but an Olympic-sized swimming pool holds over 660,000 gallons of water. That means the water produced by Hurricane Harvey, just in Texas alone, could fill the equivalent of over 28 million Olympic-sized swimming pools. A meteorologist with the Harris County Flood Control district tweeted that "1 trillion gallons of rainfall …. would run Niagara Falls for 15 days."

While the search and rescue efforts continue in the near term, the economic impact will likely be felt for the foreseeable future. According to CNNMoney, there are currently 10 oil refineries that have been temporarily closed due to Harvey. The ports that receive oil in Houston and Corpus Christi have also closed due to the storm and are expected to not receive shipments for at least a week. The Interior Department's Bureau of Safety and Environmental Enforcement estimates that the disruption in the refining process is equivalent to 25% of the total refining capacity of the United States. With fewer refineries and some shipping ports being closed, it was expected that the prices of oil and gasoline would spike dramatically higher. Actually, it hasn't. At the time of this writing, the national average price for a gallon of gasoline, according to GasBuddy.com, has increased 7% from just one month ago. The demand for oil producing products from Houston residents, which is the fourth largest city in the U.S., has dropped drastically. U.S. oil production over the past year has been elevated due to more hydraulic fracking rigs coming back online and has been able to subsidize a substantial portion of the drop in the normal supply lines. Therefore, a decrease in total demand along with oil productivity remaining somewhat near normalized levels are the likely reasons oil prices have not risen considerably during this unusual time.

Capital Markets Update

The month of August saw volatility awaken from its deep slumber only to roll over and practically begin snoring again. In the wake of North Korea testing an intercontinental ballistic missile that was shown to have the capability of reaching the United States, the North Koreans also made it known that they were analyzing potential strikes on U.S. military bases in Guam. President Trump issued a statement warning that North Korea will "face fire and fury like the world has never seen," unless they stopped making threats against the United States. Investors ran for cover after

the aggressive tone and the VIX spiked up nearly 40% in a single day. Just days after the event, volatility returned to its benign state. At the end of the month, North Korea tested a missile that flew directly over Japan and ultimately landed in the Pacific Ocean. This along with the severe weather and flooding in the Gulf Coast from Hurricane Harvey, caused volatility to increase again for a short time at the end of August.

On the economic front, the ISM Manufacturing Index exceeded estimates with a result of 58.8 compared to a consensus estimate of 56.3. Index results over 50 are a sign of expansion in the industry, which according to the Bureau of Economic Analysis represents nearly 12% of the country's productivity. GDP for the second quarter was revised upward from 2.6% to 3.0% and lifted markets. August nonfarm payroll numbers of 156,000 fell short of the 180,000 consensus estimates. Unemployment rose from 4.3% to 4.4%. Consumer sentiment echoed this same theme as it continued to remain high from a historical perspective at 96.8, but it did incur a noticeable drop from the prior month's level of 97.4. Economic data as a whole continues to remain strong, but data from August has tempered what was reported in July.

Emerging markets represented by the MSCI EM Index rose 2.23% and continue to lead all major markets year-to-date by rising 28.29% through the end of August. Performance for the MSCI EAFE Index has slowed over the past few months, but still maintains an impressive 17.05% return so far in 2017. Domestically, the S&P 500 Index finished the month 0.31% higher, increasing the year-to-date returns to 11.93%. Small-cap stocks gave back some of their gains over August, yet have contributed 4.42% for the year. When looking at domestic equities year-to-date, large-cap stocks have fared the best from a performance perspective, followed by mid- and small-caps. Growth stocks continue to dramatically outpace value stocks.

The U.S. Barclay's Aggregate Index continued its steady climb this year to gain 3.49%. The 10-Year Treasury began the month with a yield of 2.29% and finished at 2.14%. The brief increases in volatility helped to push yields down as investors flocked to the safety of U.S. Treasuries. Earlier this summer, the Fed provided details of a plan to unwind their $4.5 trillion balance sheet, but the implementation date has yet to be determined. The balance sheet reduction will likely begin later this year, and according to Bloomberg at the time of this writing, the likelihood of a Federal Funds rate hike for September is now at 0%, and only 8% for November. This aligns with many investors as they have expressed concern over a Federal Funds rate hike and a reduction in the Fed's balance sheet occurring simultaneously. The potential impact this could have on fixed income markets remains unknown.

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