Investor Insights & Outlook

April 2017 1st Quarter Concorde Investment Management

Domestic Economic Overview

A Message from Concorde Investment Management

We are pleased to provide the following overview of the domestic and international economic backdrop and the financial markets that impacted our investment policy and strategy during the First Quarter of 2017, as well as other articles of interest.

The Concorde Team

Most forecasters began the quarter estimating that GDP growth during the quarter would be somewhere around 3%. As the quarter progressed, forecasters continued to trim with most recent numbers coming in below 1%. Actual GDP for the quarter was .7% (subject to 2 further reviews) which was the weakest Q1 GDP number in three years. This is following a Q4 number of 1.9% (which missed estimates). What is going on? The expectations of a Trump presidency, tax cuts, reduced regulation, and a new health care law had the Consumer Confidence Index hit 125.6 in March which is the highest since December 2000! This bodes well for the 2nd quarter given the optimism is centered around business, jobs, and personal income prospects but consumer spending was one of the main drags in Q1. Expect consumers to open their wallets and give the consumer spending portion of GDP an increase during Q2. The problem, though, is nothing from a policy standpoint has been enacted yet. Improvements in commerce, trade, regulatory, and tax policy have not been put into motion yet and details have been scarce.

We have an interesting dichotomy in the bond and equity markets on expectations around the improvements in the above stated policies and economic growth. As mentioned in the equity and fixed income sections, equity markets increased in the first quarter while bond rates remained flat. Even as we went into April, the 10-year treasury

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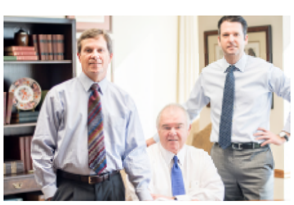

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Domestic Economic Overview (continued)

dipped back to just below 2.2%, the same level it was when Trump was elected. Equity markets remain optimistic that the new administration can get things done that will improve the economy and economic growth rates while the bond market is taking a 'show me first' stance. We will find out if our Real GDP numbers will increase with reduced regulatory burden and increased wage growth. The new administration is working on reducing regulations through executive orders and given the tight labor supply, wage growth continues to accelerate. We wrote in our Q4 letter that all of the ideas this administration has to boost the economy would be difficult to get through Congress and so far the only thing we've seen is an 'almost' vote on a health care bill. Other than that, just generalities have been discussed. We remain optimistic that the GOP will figure out a way to work together and get some legislative accomplishments done to assist the economy in getting out of the slow growth trend it's been stuck in for some time.

International Economic Overview

Activity in the Euro zone dominated the headlines during the first quarter. The UK Prime Minister, Theresa May, invoked Article 50 in March which triggers the Brexit process and then she followed that up with calling for a snap election on June 8th. The goal, it seems, is to give her some guidance and political capital during the Brexit negotiations. The French held the first part of their Presidential Elections in April and the two top vote receivers will have a run off in May. Marine Le Pen of the National Front will be going against Emmanuel Macron of En Marche. Regardless, this election is a referendum on the Euro as Le Pen would want to leave the union whereas Macron would strengthen ties. The Dutch held an election on March 15th and the populist, euro exit Party of Freedom was soundly defeated.

Despite the political activity threatening global economic growth, Global GDP is expected to expand 2.8% year over year which would match Q4's growth. Developed economies lead the way, however, major emerging economies are growing again in part due to increased commodity prices. China grew at 6.9% during Q1 which was faster than expected and should help stabilized economic relationships in Asia.

We are monitoring the Trump administration's stance to international trade policy daily. The most recent news prior to this letter being mailed out was that both the Canadian Prime Minister and President of Mexico have agreed to renegotiate NAFTA after Trump threatened to pull out of the agreement prior to his 100 day on the job deadline. We spoke of the trade deficit mechanism for increasing domestic GDP growth and Trump has already held meetings with the President of China and he's getting ready to renegotiate with Canada and Mexico. Those are three of the top four largest trade deficit partners of the U.S. The fourth, Japan, began having economic talks with the U.S. in April. The Trump administration wants a bilateral trade agreement and Commerce Secretary Ross will be visiting Tokyo to hold talks with the Japanese trade minister. We mentioned those four countries in our Q4 letter as the countries to watch for immediate negotiations to take place.

Equity Markets

The domestic equity markets recorded very good total returns for the quarter after surging through late February and trending sideways in March and early into the second quarter. Growth and cyclical sectors outperformed as individual company and economic reports continue to reflect better trends that began in mid-2016. Some hiring and corporate project decisions may be reflecting optimism for potential policy changes being pushed by the new administration, but actual improvements in recent conditions are likely the primary driver of performance. Reflective of the sectors described above, growth indices outperformed value significantly. International markets also generally rose with most emerging markets rising more than developed markets.

Within the domestic sectors, financials, energy, and telecoms lagged at +2.5%, -6.7%, and -4.0% respectively, reflecting their defensive nature and for energy, a pullback from a very strong 2016. Information technology and consumer discretionary led sector performances at +12.6% and +8.4%, reflecting good results and some optimism for improved corporate and consumer activity. Assuming interest rates only move modestly higher during the next year or two, equities in general are fairly valued, forcing individual stock investors to dig deeper to find good values. It will likely take at least some success in proposed policy changes and different fiscal spending priorities to spur the U.S. economy to grow at greater than the recent 1.5% - 2.0% real rate trend. If additional growth above this level does not evolve it is likely that equity markets will struggle to maintain the recent uptrend. With this backdrop, we recommend conservative equity policy allocations in order to take advantage of corrections but with enough exposure to continue to participate if current trends persist.

Q1 - 2017	
S&P 500	6.1%
S&P 500 Growth	8.5%
S&P 500 Value	3.3%
MSCI EAFE (Developed)	7.4%
MSCI EM (Emerging)	11.5%
	Source: Morgan Stanley; Bloomberg; FactSet

WEB PRESENCE AND CLIENT LOGIN

Last year we launched our website www.concordeco.com. If you have not already done so, please take a few minutes to explore the website. On the site you will find information about our firm, services, certain literature, and access to client portals. Notice that our "Client Access" tab has a pathway to a "Concorde Login". To obtain your personal login information, please contact Greg Wood at gregwood@concordeco.com or 972-701-5412 and he will work with you to get your account set up.

Fixed Income

After surging higher during the last quarter of 2016, most government and corporate bond yields remained flat in early 2017. The resulting performance of these trends were gains that largely reflected the coupon income of individual issues. Yields on shorter term bonds (< 3 years) trended higher as the Fed increased their target rate for the third time in this cycle with expectations that further hikes are likely. Spreads between higher risk corporate bonds and Treasuries increased slightly after shrinking considerably over the prior six quarters. Municipal bonds became slightly less attractive in the quarter as demand remained firm. Looking toward future investment prospects, after a likely consolidation in Treasury bond yields in the recent surge, rates should move higher over the next year or two, suggesting strategies that emphasize short to medium term maturities.

Although corporate bond yield spreads have narrowed considerably as noted above, they remain attractive in the current environment. Our recommendation for corporates is to maintain holdings in select companies utilizing short and medium maturities as with Treasuries. Investment demand for corporates, which has increased considerably from private foreign investors since early 2015, should remain strong as U.S. policy remains more hawkish and the domestic economy stays attractive versus most other central banks and economies. Municipal bond investment should remain very selective as we have emphasized in recent years as many large cities and some states face significant liability issues.

Experts Forecast Long-Term Stock and Bond Returns

by Alina Lamy

Even the most basic financial plan calls upon you to make your best guess about a few key facts: how much you can kick in on an ongoing basis; how much time you have to invest; what combination of stocks and bonds you employ; and finally, the rate of return you can expect to earn on your investments.

The first three fall into the realm of 'somewhat knowable,' and you exert at least some control over them. But forecasting returns is a trickier business.

Many investors turn to long-term market averages--dating to the late 1920s, for example--to help shape their return projections, but they're not perfect gauges. For one, most investors don't have 90 years to invest, they have more realistically 40 or 50 years; the shorter the time period (and the better or worse the starting and ending points), the more returns over that period are apt to vary from historic norms.

So, what's a well-meaning investor to do? It's reasonable to use the long-run averages as a starting point--8% to 10% for stocks and 5% for bonds--then tweak up or down based on experts' opinions about current valuations and the investor's own time horizon. Given today's low yields on both stocks and bonds and not-cheap equity prices following U.S. stocks' extended run, it's only reasonable for U.S. investors to adjust their return assumptions downward from those long-term averages. But how far? Morningstar compiled insights from a range of market experts to help you draw meaningful conclusions. Note that these expert forecasts vary in their time horizons as well as in whether they factor in inflation and currency effects.

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Experts Forecast Long-Term Stock and Bond Returns (continued)

John C. Bogle, founder of Vanguard Group
Highlights: 4%-5% equity returns, 2.5% bond returns (September 2016)

In an interview in late September 2016, the Vanguard founder said he was expecting muted returns for both stocks and bonds. Bogle's intuitive formula starts with the equity market's dividend yield, then factors in expected earnings growth and the potential for P/E multiple expansion or contraction. Based on his inputs--a 2% dividend yield, a 5% earnings-growth rate, and a 3% haircut for P/E contraction due to high starting price multiples--Bogle said it was likely stocks would return 4% or 5% over the next decade, and that figure would shrivel further once inflation, taxes, and investment fees are taken into account. Like most market experts, Bogle isn't expecting robust returns from bonds, either. He said in the September interview that he thinks a 2.5% return is reasonable for investors who are willing to venture beyond Treasuries, as starting bond yields have historically been a good predictor of what bonds will earn over the subsequent decade.

Grantham, Mayo, Van Otterloo (GMO)
Highlights: negative 3% real (inflation-adjusted) returns for U.S. large caps over the next seven years; negative 0.8% real (inflation-adjusted) returns for U.S. bonds (Nov. 30, 2016).

The valuation-conscious team at GMO is frequently pessimistic in its seven-year forecasts, and its latest dispatch is no exception. Owing to low yields and high valuations, the firm is forecasting negative real returns from the U.S. stock and bond markets over the next seven years. (The subset of high-quality U.S. companies should break into the black, on an inflation-adjusted basis, in GMO's view.) Meanwhile, the firm is more sanguine about non-U.S. equities. It's forecasting mildly positive real returns from international equities and the strongest gains (a 4.4% real return) from emerging-markets equities. It's worth noting that the firm's pessimism on the U.S. market has cost it on the return front over the past several years: some funds managed by the same team that formulates the seven-year asset-class forecasts have recently struggled. As Morningstar analyst Leo Acheson points in his most recent review of the fund, GMO has recently experienced some changes in its management ranks, too, as Sam Wilderman, co-head of asset allocation for the firm, departed at year-end 2016.

Morningstar Investment Management
Highlights: 3.1% 10-year nominal returns for U.S. stocks; 2.7% 10-year nominal returns for U.S. bonds (Dec. 31, 2016).

Like GMO and Research Affiliates (below), Morningstar Investment Management's return expectations for U.S. stocks and bonds are low, if not downright discouraging, especially when you factor in inflation. But the outlook is more optimistic for foreign equities: MIM expects U.S. holders of international developed equities to earn 6% on a nominal basis, and U.S. holders of emerging-markets equities to earn 9% nominally. MIM's forecasts are lower once inflation and currency effects are factored in; for example, the return on international developed-markets equities drops to 2.8% and emerging-markets equities to 4.8%.

Research Affiliates
Highlights: 0.8% real returns for U.S. large caps (the S&P 500) during the next 10 years; 0.8% real returns for the Bloomberg Barclays U.S. Aggregate Bond Index (Dec. 31, 2016).

The graph depicting Research Affiliates' return expectations for various asset classes is fun and easy to use. While the firm is even more downbeat about the prospect for U.S. stock and bond market returns over the next decade than it was a year ago, it's still

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Experts Forecast Long-Term Stock and Bond Returns (continued)

optimistic about investing overseas. At year-end, the firm was expecting a nearly 6% real return from developed-markets equities and a 7.5% real return from developing-markets stocks. Like GMO, the firm is also relatively positive on the prospects for emerging-markets bonds, especially those denominated in local currencies; it's forecasting a 4% real return from such bonds over the next decade.

Vanguard
Highlights: Nominal global equity market returns of 5% to 8% during the next decade; 1.5% to 2.5% expected returns for global fixed-income markets (December 2016).

In its 2017 Economic and Market Outlook, Vanguard's economic team describes its outlook for global equities as 'guarded but not bearish.' Vanguard's Capital Markets Model provides a range of probabilities for returns from various asset classes. For global equities, the firm's model places the highest probability of nominal returns in the 5% to 8% range for the next 10 years. The firm's research also suggests that investors in foreign stocks that are not hedged into the dollar could outperform the U.S. market in the next decade. 'The expected return outlook for non-U.S. equity markets is modestly higher from a U.S. investor's perspective,' the firm's economic experts wrote. However, in contrast with the researchers at Research Affiliates and GMO, the Vanguard team doesn't consider emerging-markets equities to be cheap. 'Emerging-market valuations are low relative to developed markets, but this phenomenon is typical of riskier markets,' the firm's economists wrote.

This is for informational purposes only and should not be considered financial planning advice. Please consult with a financial professional for advice specific to your situation.

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