Dear Clients & Friends of Patriot Investment Management

2017 turned out to be a banner year, thanks to a near-perfect alignment of three key economic factors – low inflation, low volatility and ample liquidity. Global expansion synchronized and gained momentum in the third and fourth quarters, as nearly all major asset classes and markets, including the US, and many developed and emerging economies posted positive returns for the year. The Dow climbed upwards into new territory, setting 71 separate record highs, corporate earnings grew, and unemployment has remained low. In December, Congress passed sweeping tax reform legislation on a scale not seen since the Reagan era.

US Economy:

Inflation increased to 2.1% as oil prices have temporarily spiked in the aftermath of numerous natural disasters, such as Hurricanes Harvey, Irma & Maria, and the California wildfires, as the long process of rebuilding begins. Even after accounting for these events, inflation has remained low, despite very low unemployment numbers. This is likely due to productivity gains from technology and automation offsetting current wage pressure. The Fed raised the Federal funds rate 0.25% once more in December 2017, and plans to continue gradually raising rates in 2018. The Fed will also continue unwinding its balance sheet, shedding a portion of assets from their quantitative easing (QE) programs, thereby reducing some of the liquidity in the markets.

Consumer confidence is at a 17-year high, and corporate earnings remain healthy, supported by low inflation, sustained global growth and an increase in manufacturing orders. The new tax legislation is projected to add a modest boost to GDP growth over the next couple of years, as lower corporate tax rates should encourage business investment. Bond yields are expected to gradually rise, but will likely stay below their historical averages as structural factors will keep the economy in a low interest rate environment for the foreseeable future.

Global Markets:

Fourth quarter saw a synchronization in global expansion, particularly in emerging markets and Europe. Emerging markets outperformed US markets for the first time in five years, boosted by a weaker dollar and stronger economic growth.

Europe's economy has been helped by the European Central Bank's (ECB's) accommodative policies this past year, which they will begin gradually reducing over the next nine months as the major economies in the Eurozone are entering a mid-cycle expansion. The UK, on the other hand, will likely face continued challenges and more volatility as they negotiate Brexit trade agreements with the EU, and the Bank of England (BOE) plans to keep their balance sheet steady.

In Asia, Japan's prospects continue to improve, as they may finally be seeing a rise in core inflation as their labor markets tighten. China has had some success in reigning in the excess leverage in their financial system, effectively slowing non-bank lending, but could run the risk of losing growth momentum if they reduce their stimulus too quickly. Given China's influence on global trade and manufacturing, this will be an area to watch in 2018. Geo-politically, North Korea is an ongoing concern as a potentially destabilizing factor in the region.

In Summary:

The US markets enjoyed a near-perfect year, bolstered by low inflation and low unemployment. Despite several setbacks to their agenda, the new administration successfully passed sweeping tax reform legislation in December. Global expansion synchronized and gained momentum as markets moved into the growth phase of the economic cycle. Barring a major geo-political event, the US economy is poised to continue on a steady pace of modest growth, but is unlikely to repeat its double-digit performance in 2018.

2017 Year End Returns:

S&P 500 + dividends	21.83%
Dow Jones Industrial	25.08%
Russell 2000	14.65%
Emerging Markets	34.35%
EAFE	25.03%
Barclays Aggregate Bond Index	3.54%

Returns are price-only unless otherwise noted

10-year Bond yield as of 12/29/17	2.40%

Inflation	2.1% thru December 2017
Unemployment	4.1% in December 2017

Thank You!

We value the confidence and trust you have placed with us, and we welcome your questions and comments. Our goal is to be our clients' trusted resource for all things financial.

Do you know someone who could benefit from our expertise? We appreciate your introductions and the opportunity to help your family, friends and colleagues meet their financial goals.