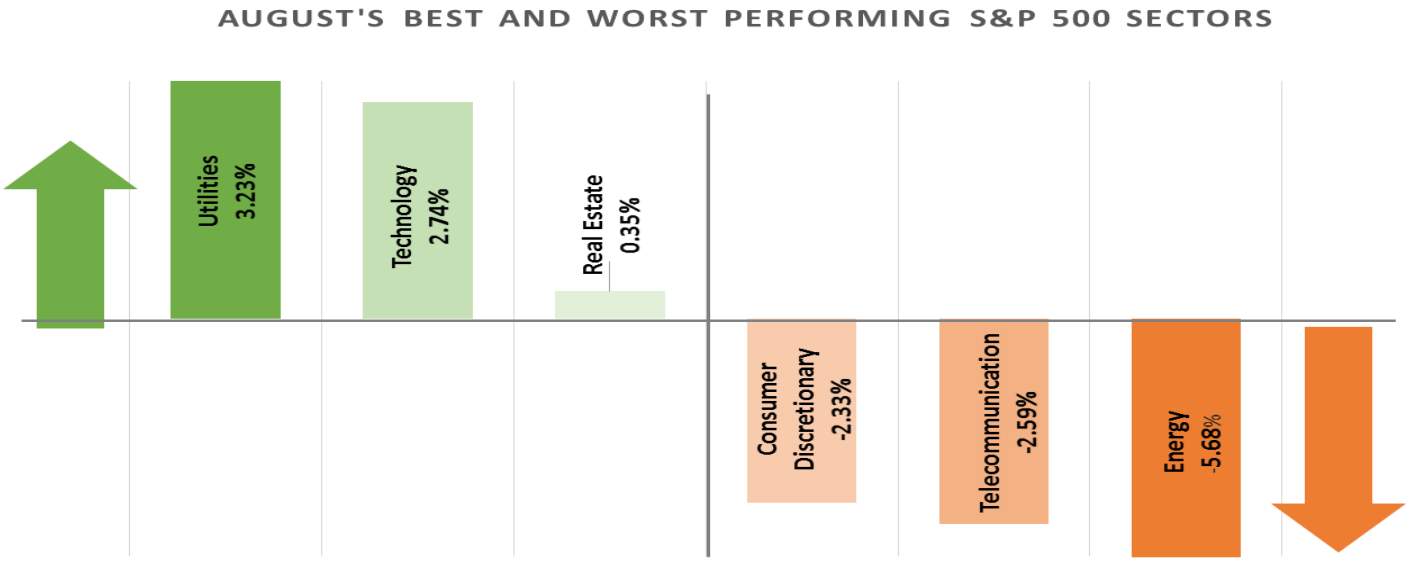
INNOVEST MONTHLY MARKET COMMENTARY

August 2017

Harvey's Devastation

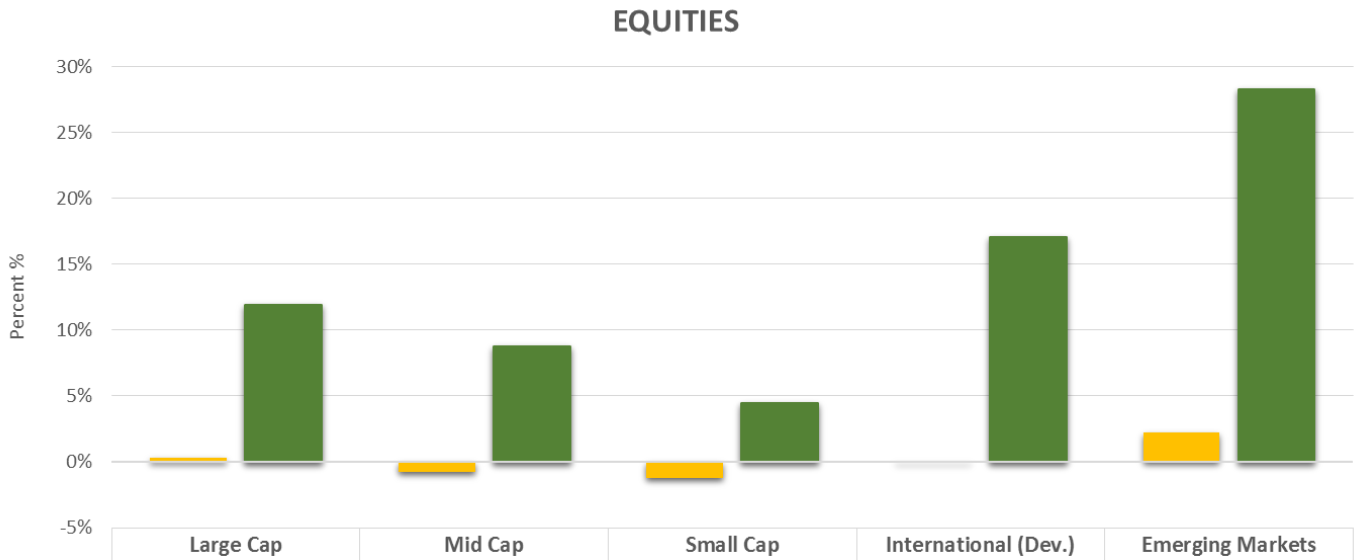
As the floodwaters subside in Houston and surrounding areas following tropical storm Harvey, devastation and ruin lay in its wake. According to the analytics firm CoreLogic, Harvey could have caused as much as $40 billion in damage when taking into account the numerous cars, homes, and businesses that have been destroyed. This impact has already affected the energy stocks, which finished the month down 5.68%.



Houston is a major source for oil imports and exports, as well as storage for oil and refined products. The two largest oil refineries in the US are in the Houston area, and nearly a fifth of US oil production has been shut down. Nearly 3.6 million barrels of oil per day are now out of commission, which represents about 20 percent of the US's total capacity based on estimates from Reuters. The refineries in the Houston area will unfortunately be bogged down with transportation, maintenance, and personnel issues as employees sort through personal issues resulting from the flooding. It is possible that these factors will have a major impact on the nation's energy prices, at least over the short term.

Other equity underperformers for the month included consumer discretionary, which has been hit especially hard since May, down another 2.33%, followed by telecommunication services (down 2.59%), despite being a top performer in July. Conversely, utilities finished atop an overall

underwhelming month, up 3.23%. Utilities have attracted investors seeking less volatile equities and dependable dividend yields. It is important to note, however, that utilities are highly sensitive to interest rates and may remain in favor as long as interest rates continue to trudge along near historic lows.



	Large Cap	Mid Cap	Small Cap	International (Dev.)	Emerging Markets
August	0.31%	-0.78%	-1.27%	-0.04%	2.23%
YTD	11.93%	8.73%	4.42%	17.05%	28.29%

Benchmark Indexes: Large Cap = S&P 500; Mid Cap = Russell Mid Cap; Small Cap = Russell 2000; International Developed = MSCI EAFE; Emerging Markets = MSCI EM.

While S&P 500 finished August with a small gain of 0.31%, it is up 11.93% for the first eight months of the year. US stocks rose at the end of August, as markets mostly shrugged off uncertainties regarding North Korea, led by 2.74% gains in the technology sector. Mid cap companies dipped slightly for the month, down 0.78%. Small cap stocks continued their 2017 trend of underperforming large caps, down 1.27% for the month and up a modest 4.42% year to date. Weak earnings coupled with economic proposals that have been put on hold following the "Trump bump" have led to underwhelming 2017 returns for the small caps.

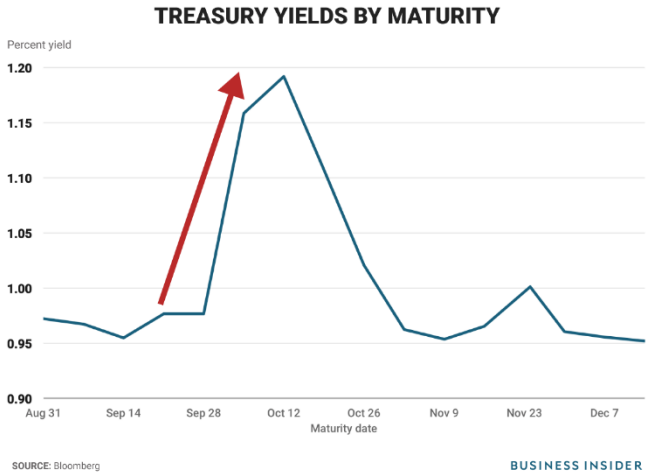
Globally, emerging markets bounced back in August after a pullback at the beginning of the month, returning a positive 2.23%. Strong fundamentals, such as corporate earnings and modest valuations, continue to support the outperformance of emerging markets versus the increasingly expensive US markets. Developed international markets lost -0.04% in August.

	Core Fixed Income	Munis	High Yield	Floating Rate	Commodities	MLPs
August	0.90%	0.64%	-0.04%	-0.14%	0.40%	-5.61%
YTD	3.64%	4.60%	6.05%	2.62%	-2.72%	-7.69%

Benchmark Indexes: Domestic Fixed Income - Barclays US Agg; Municipal Bonds - Barclays 4-6 Yr Muni; High Yield - Barclays US Corp. HY; Floating Rate – CSFB Leveraged Loan Index; Commodities - Bloomberg Commodity; MLPs - Alerian MLP Infrastructure.

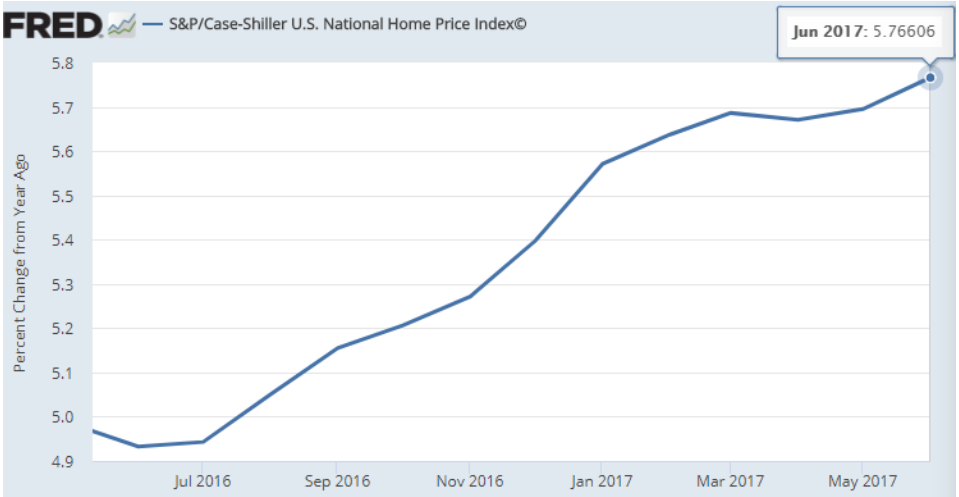
In the fixed income markets, the 10-year Treasury yield slipped lower since last month, finishing at 2.12% as Fed policymakers seem to have become less concerned about inflation. Last month, the Fed released dovish notes from the FOMC meeting, which conveyed a sentiment that "inflation might remain below 2 percent for longer than they currently expected."

U(S) Have a Debt to Pay



The uncertainty of another debt ceiling debacle has been seen in the yield spike of Treasury bill maturing this October. The US Treasury Department auctions bills that mature within a year to borrow from the public, and the yield indicates investors' demand for lending to the government. Unless President Trump and Congress pass measures to raise the US debt limit once again, the US government's ability to pay its obligations will be seriously threated. Legislators face a September 29 deadline to raise the debt ceiling or risk another government shutdown and a potentially catastrophic default on the government's debt.

Changes in the Value of U.S. Residential Real Estate Prices



Source: S&P Dow Jones Indices LLC, Federal Reserve Bank of St. Louis.

Location, Location… Inflation?

The rise over time in the prices for goods and services, better known as inflation, is natural in a healthy economy. Home values have increasingly outpaced inflation in recent years, making it especially difficult for younger and first-time home buyers to move into the housing market. According to data from the US Census Bureau, the average US home price in 2000 was $207,000. In July 2017 the average price had jumped to $371,200.

The S&P/Case-Shiller US National Home Price Index tracks the changes in the value of residential real estate and is considered the leading measure of US residential real estate prices. The most recent report from S&P/Case-Shiller indicated that home prices increased 5.8% in the last 12 months. Major cities leading the trend of rising home prices were Seattle, Portland, and Denver, where prices from a year ago were up 13.4%, 8.2%, and 7.6%, respectively. Tight supplies of homes for sale has led to bidding wars has contributed to home prices outpacing gains in wages.

These factors help to explain that the current typical home buyer is 44 years old, compared to the 1980s, when the range was around 25 to 34 years old. Typically, an individual buys a house in the hope that it will be a good investment. A renter will theoretically spend hundreds of thousands of dollars on rent over a 30 year time period, while the same individual could start out by buying a house and hopefully end up owning it over the same period after paying off a mortgage. Future gains in home prices might be more subdued as demand for housing may fall from people being priced out of the market.

The Bull Market Continues

From Hurricane Harvey to historically low interest rates, there are a number of factors that continue to affect the economy, both over the short and long term. As uncertainty in the markets continues,

it remains critical that clients maintain a well-diversified portfolio of asset classes to mitigate risk. It would be highly presumptuous to assume the stock market will continue posting annualized gains of more than 10%. However, as long as you have a sound financial plan in place, you should be prepared to weather any volatility ahead. As always, please do not hesitate to reach out to us with any questions regarding your portfolio.