Friends,

BOND VALUATIONS

Sometime in January 2016 I wrote in this newsletter that I felt high yield bonds offered an attractive risk-return tradeoff considering the recent declines connected to stock market volatility. Since then, the asset class has done quite well. Attached is a quick snapshot of average bond prices by major index as of 5/2/2017 and a year ago. Most categories of bonds have actually declined in value from a year ago, theoretically making them more of a bargain today. However the chart shows two categories that have done very well: high yield and leveraged loans (which is really just a short duration version of high yield). Generally speaking, I really like high yield bonds as an asset class; historically they have generated near-stock market returns with less volatility. However, there have always been points in time when they don't really have the same upside potential. And in my opinion, we're currently in one of those moments; I think they're expensive. These "moments" can last months or years, but I feel it's likely (if history is any guide) that we'll have the opportunity to purchase this asset class in the future at more attractive prices.

FRENCH ELECTION

Homer Simpson once described the French as "a bunch of low-producing, cheese-eating surrender monkeys." While we can debate the political correctness of such a comment, we can't argue with the accuracy of the "low-producing" part. According to Trading Economics, France's GDP has averaged a paltry 0.78% from 1949 – 2017 Q1. This now coincides with an unemployment rate of 9.6%. It seems that a lot of French citizens have had enough, electing a new president over the weekend. Emmanuel Macron is promising economic reform that would move France from a model of social democracy towards free-market capitalism. Among the initiatives on his platform are reducing the wealth tax, reducing the corporate tax rate, reduce government jobs, and eliminate the 35-hour work week. Considering how low expectations seem to be for developed Europe, and the relatively low base of growth, France might be a country with some upside surprise in the future.

CAUTION WITH NEW MONEY

One of the most common decisions an investor faces is how to invest new money. If the stock market is down, investment in stocks usually feels uncomfortable, because of the fear a decline might continue. However, if the stock market is up, adding money to a rising market seems easy, as the expectation is that good times will continue. MFS strategist James Swanson, CFA, weighs in on the question in his weekly newsletter, and argues that the current moment is not ideal for new money investment in US stocks. Not only are valuations on the expensive side, but chief among his concerns is the low level of business investment in plant and equipment. Without an increase in private sector capex, he doesn't expect the current business cycle to continue much further; thus his recommendation to remain cautious with new money. Please see the attached for more detail.

Have a great week!

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Investments in fixed-income securities are subject to market, interest rate, credit and other risks. Bond prices fluctuate inversely to changes in interest rates. Therefore, a general rise in interest rates can result in the decline in the bond's price. Credit risk is the risk that an issuer will default on payments of interest and/or principal. This risk is heightened in lower rated bonds. If sold prior to maturity, fixed income securities are subject to market risk. All fixed income investments may be worth less than their original cost upon redemption or maturity

High-yield bonds, also known as junk bonds, are subject to greater risk of loss of principal and interest, including default risk, than higher-rated bonds. Investors should not place undue reliance on yield as a factor to be considered in selecting a high yield investment.

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