June 2016

WealthManagement

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Market Insights

A periodic newsletter from Idaho Trust

Members of the Federal Reserve Bank (Fed) are clearly struggling with how to 'normalize' interest rates following a long period of extremely low rates. Recently, several Fed Governors stated they think it's appropriate to raise interest rates in the coming months. However, the underlying economic data may not warrant such a move, at least in the near-term.

Interest Rates

At its most recent meeting, the Federal Reserve Bank (Fed) made no changes to its interest rate policies. (Recall that the Fed funds' target range was increased to 0.25% – 0.50% in December.) At the recent meeting, the Fed lowered its interest-rate forecasts for this year and next. The Fed projections had been significantly above what most economists projected, so the lower forecasts were thought to be market friendly. Although more recent economic data has shown some sign of improvement, the domestic economy had experienced a slow down over the past six months and several market commentators have argued that the economy was not strong enough to withstand a tighter monetary environment.

In late May, the minutes from the April meeting were released. The minutes presented a much different picture than what had been assumed following the last meeting. The minutes revealed that many members were ready to lift interest

Idaho Trust Bank offers total wealth solutions including its LifeNeeds™ investing process. The LifeNeeds™ investment process utilizes proven strategies and techniques delivered by a highly trained staff of wealth management professionals.

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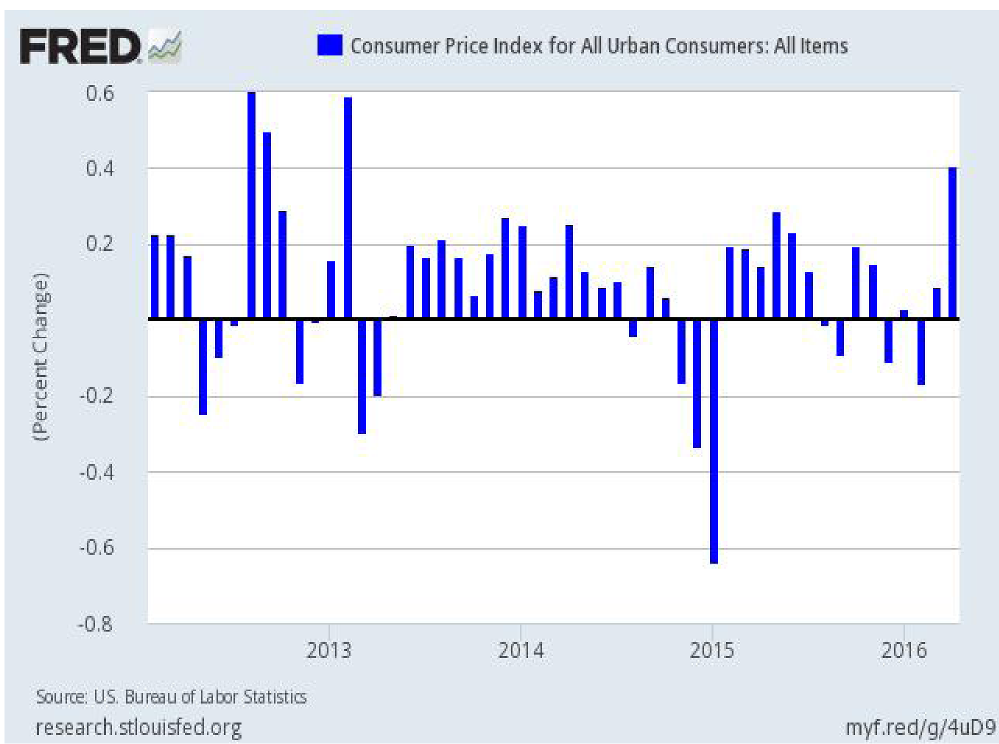
rates during the June meeting, assuming the economy improves. This development is very different from what most market participants had been expecting. In fact, prior to the minutes being released, the odds of a Fed rate hike in June were extremely low (basically implying no increase expected). Those odds moved higher once the minutes revealed a desire of the members to raise rates. The outlook for interest rates became more unclear following the release of the May employment report, which revealed a sharp slowdown job creation. Despite the confusion surrounding the near-term stance on Fed policy, we think tame economic activity levels argue for a slow increase in interest rates.

The yield on the 2 Year U.S. Treasury bond (an excellent barometer for future Fed interest rate changes) has been very volatile over the past two months. Despite this volatility, there has been a modest trend toward higher rates, indicating that the general move in short-term rates will be higher in the coming year.

One area that is contributing to a higher probability of an interest rate increase is higher commodity prices, especially energy prices. Spot oil prices which fell below $35 per barrel in January has since rebounded to about $50. The Chairperson of the Federal Reserve Bank, Janet Yellen, suggested that the Fed wanted to act before there were signs of inflation. The central bank made a big effort to convey the idea that economic activity

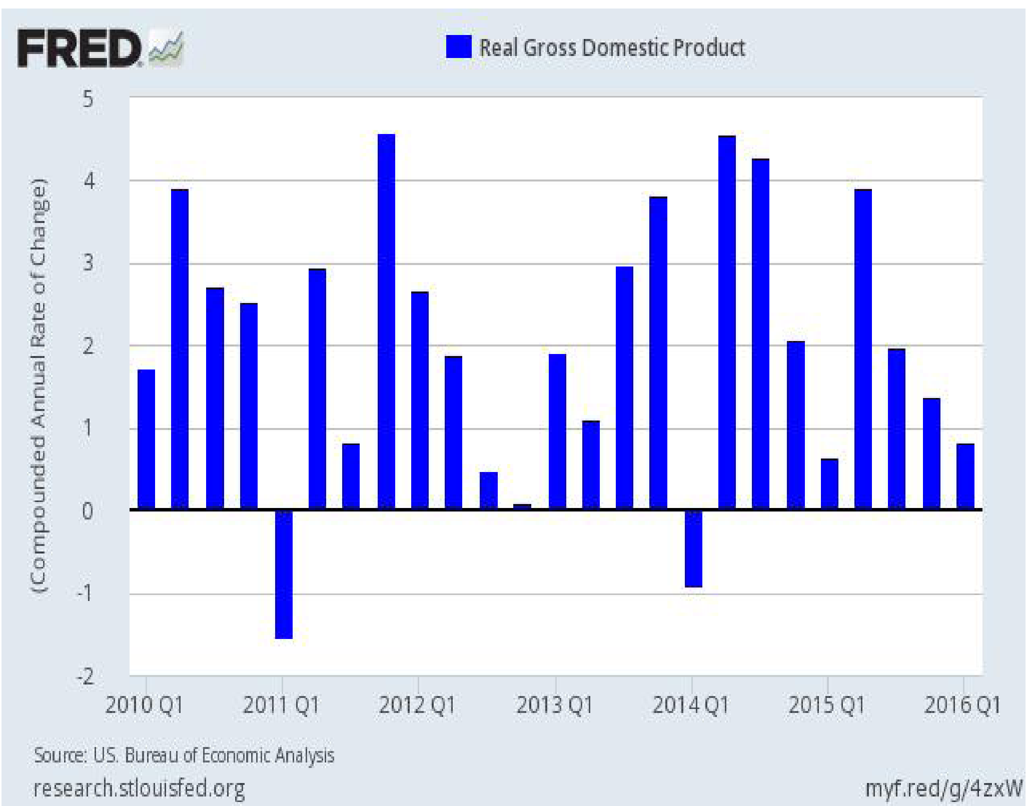


levels will determine the path and timing of future interest rate increases.

The most recent Government report on inflation showed a headline increase that was the strongest reading in about 3 years. The headline CPI (Consumer Price Index) rose by 0.4% in April. The big driver was gasoline prices which rose by 8.1% over the prior month, but remains well below year ago levels. The inflation readings can be volatile and, therefore, we do not put too much weight in a single reading. The core rate of inflation, which excludes food and energy, rose by 0.2% in April. This represents a more subdue inflation picture, but certainly something we will have to continue to monitor.

Gross Domestic Product

The first quarter Gross Domestic Product (GDP) was revised higher to 0.8%, up from 0.5%. The increase was welcome news. Yet, the first quarter was the third quarter in a row that GDP growth decelerated, meaning the rate of growth slowed. The latest figures showed a larger gain for residential investment. During the first three months of the year, U.S. corporate profits rose at a 1.9% rate from the fourth quarter. The modest rebound came after two consecutive quarters of falling profits. Based on incoming economic data, the 2Q GDP reading should experience a solid increase from 1Q. Consumer spending, which accounts for more than two-thirds of the U.S. economy, has expanded supported by a slightly better wages growth and



rising home values.

Conclusion

The current economic environment does not warrant a sharp increase in interest rates. Therefore, we expect that the Fed will monitor activity and inflation levels which will result in an environment of slowly rising interest rates. The pace towards normalization will likely be a long process.

S&P 500 Index

3 Month	6.58%
Year-to-Date	3.57%
1 Year	1.49%
3 Year	11.04%
5 Year	12.16%

MSCI EAFE Net Index

3 Month	7.60%
Year-to-Date	-1.10%
1 Year	-9.31%
3 Year	1.99%
5 Year	2.17%

Barclays Aggregate Bond Index

3 Month	1.71%
Year-to-Date	3.45%
1 Year	3.49%
3 Year	2.91%
5 Year	3.26%

As of 5.31.2016

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