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Economic Commentary

The US economy continues to “muddle” along in the low 2% range. The fifty indicators that we monitor regularly suggest continued incremental gains in nearly all measured components. Consumer confidence surveys completed by the Conference Board reveal a consumer more confident in the forward period than they were a year ago. Fittingly, the small business confidence index has increased 14% year over year as well. The last two months reduction in initial jobless claims (first time applicants), may play a large part in the confidence portrayed within the surveys.

Auto sales continued to soften off of the record sales figures of 2017 and are now at a 16.58 million unit annual run rate, producing a 13.2% year over year decline. Recent tightening of lease and finance standards across the financial industry are providing some headwind for sales, but the decline is not greater than the forecasts produced by the auto industry late in 2017.

Home sales rose for the reporting period by 1.1% as inventory declined and days on market followed suit. The most recent Case - Shilar report indicated that year over year housing price growth more than doubled inflation at + 4.9%. While it took over ten years to accomplish, the housing market as measured by price, has fully returned to the record levels seen in the fall of 2006.

Wages have grown by 2.5%, while personal income increased by 4.0% and savings held steady at 5.5%. Not surprising, given reduced unemployment and wage growth, consumer spending also grew by 4%. From the consumer's side of the equation the economy is sound yet certainly not robust. Nearly all of the components of production continue to be flat year over year with durable goods orders registering only incremental dollar gains. Productivity has diminished and job gains have been largely in professional services and health care.

On a more macro economic perspective, emerging economies have bottomed and are now in recovery. The Baltic Dry Index, which measures shipping capacity and movement, has increased 33% year over year, indicating greater movement of goods globally. The US dollar has fallen 5.6% since January 1, 2017. Normally, a country's currency will rise when

Commentary, continued

“This modest devaluation in the dollar is the first that we have seen in nearly eight years and, while welcomed by some industries, it is not likely to grow significantly from this level.”

the economy of that country gains strength and fall when it weakens. All currencies, however, react in a relative, not isolated, relationship with other currencies, and thus the decline in the US dollar is not so much about our economy but rather about the renewed strength of other economies. The current decline in the dollar is welcomed by companies that export and also compete against imports, as it makes US exported goods cheaper abroad and imported goods more expensive in the US. For publicly traded companies, this dual advantage flows through as a potential boost to quarterly earnings. This modest devaluation in the dollar is the first that we have seen in nearly eight years and, while welcomed by some industries, it is not likely to grow significantly from this level.

In general the incremental progress of the economy continues intact. More people are employed, their wages are growing slightly, inflation remains benign, interest rates have increased only slightly and confidence levels are increasing. If we were assigning a grade, we would give the current economy a C+.

Threats or enhancements to the grade being earned by the economy remain as they have been for the past nearly nine years. Geopolitical fractures remain as the largest potential threat to sustained economic growth. It is accurate to say that there is a new European order being negotiated and structured that includes some form of Brexit and a new, as of yet unclear, US–Europe order as well. These are not the type of changes that cause immediate impacts to economic growth, but need to be sorted well so as not to cause impairments. The anticipated G20 summit may provide more solid clues as to elements of the new order and, to be certain, many assessments will be given to even the most minor elements of posturing. In the end, these are mature economies being represented at the summit and none are in a relative position of strength that allows for big movements in the established order that currently exists.

ISIS or ISIL is running out of leaders, financial assets and fighters. This is not to suggest that they or any other group won't re-emerge if there is a future vacuum created by political instability within the region. What is currently in transition is a battlefield war being badly lost by ISIS, that will be replaced by an increase in terrorist-attempted actions in many countries. While the actions will be horrific examples of man's continued inhumanity to man and gruesome to see and experience, the actions will be more interruptive rather than impairing to economies of the world. As we have written before, the fight in this region is within Islam. The centuries old battle between the Shiite and Sunni is both financed and manipulated by many governments within the region. The

solution to this fight can only be solved by those who fight the battle and those that allow it to be fought. We have been covertly and or overtly involved in this conflict for over thirty years but that is only a few short years compared to a battle in Islam that originated 1,386 years ago.

North Korea is more than problematic and is a real defined threat to several major economies of the world. The strongest political powers if the world have attempted to either ignore or contain North Korea over the past sixty five years, to little avail and only limited and then temporary effectiveness. Global sanctions are only effective if there is global adherence and discipline of the global partners. North Korea is the best example of limited adherence and discipline. Getting the outcome wrong with North Korea would be far more than interruptive, and getting it right could be the most significant benefit to global economic stability in the past six decades. Not having made progress in this arena is universally the most common regret of every US President, both living and dead, since Harry Truman. Hopefully, this global issue has the highest priority for a lasting solution within the current administration.

Speaking of the current administration, we are now approaching mid summer of 2017 and healthcare, tax reform and immigration remain on the yet-to-do list of President Trump and the Republican-led House and Senate. Without a bipartisan plan on healthcare the Republicans will be forced to deliver sixty affirmative votes in the Senate and are, at this writing, unable to do so. Financial markets during the last two weeks began to believe that the Republicans would not be able to deliver on the promise of repealing the regulatory side of the Affordable Healthcare Act. Of importance to the healthcare industry, and therefore healthcare sectors in the stock market, was the repeal of the device industry and pharmaceutical industry tax on sales. Also important to investors was the 3.8% tax on investment income inclusive of capital gains that would be eliminated if the regulatory parts of the Affordable Healthcare Act were repealed. Word in the halls of the senate just prior to the July 4th break was that a growing number of Republican Senators were moving in the direction of not repealing the device tax or the 3.8% surcharge, so that they could get some support from across the aisle. While the chance of bipartisan support remains very limited, the markets voted with a five percent drop in the health care sector, suggesting that the repeal portion of the campaign promise is in doubt. There is much demagoguery on both sides of the aisle, and little clarity in what is to be crafted in any of the campaign promise-focused legislation yet to be delivered. The first 100 days has now morphed into over 200. As always we will continue to look for clarity and assess its impact on the economy when anything is delivered. ☑

“Speaking of the current administration, we are now approaching mid summer of 2017 and healthcare, tax reform and immigration remain on the yet-to-do list of President Trump and the Republican-led House and Senate.”

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We’re looking forward to discussing mywealth with you in your next review meeting. In the meantime, reach out to any member of your client centric team for more information.

Three Cultural Building Blocks

I recently had the opportunity to speak at Southwest Michigan First's First Leaders breakfast. The First Leaders breakfast is a networking event for developing leaders in our community and involves a question and answer session with a community leader facilitated by Southwest Michigan First's CEO, Ron Kitchens. I was honored and humbled to be the community leader chosen to be interviewed. During the open question and answer portion of the breakfast I was asked a question that, upon further reflection, I think my answer could have been better than what it was on the spot. Has that ever happened to you? I'm thankful I have a monthly newsletter article to clarify.

The question was after hearing me talk about the importance of our culture what did I think the three most important parts of creating a strong culture were? I often struggle answering questions involving "most important" in them. In this case in particular, there are a lot of components that go into creating a strong culture. But with a little more time I think I could have grouped the components under the following banners: foundation of trust, belief in the mission, and relentless commitment.

Our culture is built upon a foundation of trust. That foundation starts with finding the right talent to join our team. The right talent is honest and honorable, a self-starter,

inspired by continuous improvement, collaborative, empathetic, and likes working with others. With these talent themes, new teammates feel comforted and energized sooner by being around "like minded" teammates. Their managers engage them in career development and do what they said they were going to do. Work-life balance also becomes more than just a human resources buzz word to them. The foundation of trust is complete when they realize there is a safe space for dialogue, debate, and problem-solving.

Belief in the mission is the next most important component of a strong culture. In our case it's simple; we are client-focused first and foremost. "How does this benefit the client?" provides the starting point for all of our actions and strategic initiatives. In addition to hiring talented teammates that derive intrinsic satisfaction from helping others, we involve everyone in the company in the strategic planning process and hold ourselves accountable for successful strategic initiative results. Open and effective communication plays a role here as well.

Finally, we are relentless in our commitment to a strong culture. As you can surmise, nurturing a strong culture is a big part of my responsibility and I take it seriously. I am not alone. In fact, 13 years ago we formed a workgroup who meets monthly to focus on strengthening



*Michael F. Odar, CFA
President*

“Our culture is built upon a foundation of trust. That foundation starts with finding the right talent to join our team.”

the way we communicate and our workplace culture. The Communication and Culture Workgroup's mission is to cultivate a caring workplace culture that inspires employee connectivity, fosters teamwork, and embodies the core values established by our founder. In 2016, they organized 37 opportunities for teammates to do just this.

The benefit of putting these three most important components together is that we have a diversely talented 112-member team that is highly engaged in what they do and focused on the individual needs of each of our clients. ☑



*N. Dean MacVicar, CTFA
Executive Vice President
Director of Institutional Relations*

“... the number of foundations operating in southwest Michigan would surprise most of us.”

Foundations Come in Several Flavors, and They're All Good

Charitable organizations and foundations are a very large and diverse group of not-for-profit institutions that play a key role in bettering society and the quality of life in communities across the country.

Although I have not researched the number of foundations in operation throughout the state of Michigan and nationally, suffice it to say that it is a rather staggering number. Even the number of foundations operating in southwest Michigan would surprise most of us.

On a national scale, there are obviously the “biggies” that we hear in the news from time-to-time, such as the Bill and Melinda Gates Foundation (at in excess of \$40 billion), the Ford Foundation, and the W.K. Kellogg Foundation, which is the 12th largest foundation in the US. Here in Kalamazoo, there are a number of well-known and well-established foundations, the most recognizable probably being the Kalamazoo Community Foundation.

Community Foundations.

Community foundations, such as the Kalamazoo Community Foundation, are just one type of foundation. Generally, community foundations are public charities that make grants intended to improve the lives of people in their geographical area. Grants are made to individuals, such as for scholarships and other educational endeavors, as well as to other non-profit organizations, economic development initiatives, etc. Community foundations bring together the financial resources of a wide array of small and large donors, be they individuals, families, or businesses, to support a variety of initiatives and activities. The Council on Foundations cites that more than 750 community foundations, covering every state, operate in the United States. It has been estimated that in excess of \$4 billion per year is paid out to support activities in fields of education, the arts, health and human services, the environment, and disaster relief. Although much can be written on this, we'll leave that undertaking to the community foundations themselves.

A community foundation is but one type of “public charity.” In addition to the spectrum of public charities, there exist various types of private foundations, as well as irrevocable trusts that operate like a private foundation.

I'll step back to some basics for a moment, before touching further on private foundations. Organizations that only operate charitable activities are classified under Section 501(c)(3) of the Internal Revenue Code.

Many types of organizations are tax-exempt, but not all qualify for 501(c)(3) status. Preferential tax treatment is provided to public charities as well as to their donors. Private foundations also have tax benefits, but they are subject to more complex and restrictive rules.

Private Foundations.

Generally, private foundations are established by, and typically funded by, an individual or small group of individuals, a family or a corporation. Private foundations must pay out at least 5 percent of their assets each year in the form of grants and operating charitable activities. A private operating foundation is a somewhat different type of foundation and will operate under similar rules, but there is not the same 5% payout requirement. Rather, it must carry out its own charitable purposes.

There are several types of private foundations, with differing elements of governance and operation applying to each, but these matters go beyond the scope of this article.

Supporting Organizations.

Whereas it is common that many foundations that are public charities operate with a purpose of making grants to unrelated organizations, institutions and individuals, there are also foundations that exist to support related non-profit organizations. Consider, for example, the Western Michigan University Foundation, which is an independent, tax-exempt 501(c)(3) not-for-profit corporation that operates to raise funds for Western Michigan University. There are numerous other examples of these types of foundations both locally and across the country. As with private foundations, there are different types of supporting organizations, with differing rules and tax considerations.

Although I only scratched the surface on a few types of foundations, and did not delve into operational elements of foundations, one take-away is that there are numerous types of foundations, different rules for the various types, and various overarching reasons for existence. What is most important is that, regardless of the specific rules and reasons for existence, a common thread is that, collectively, the foundations that exist locally, state-wide, nationally, and internationally have a huge impact on bettering our society through their grant-making activities. We are honored to be a small part of this betterment by providing administrative and fiduciary services to a number of foundations within our marketplace. ☑

“...the foundations that exist locally, state-wide, nationally, and internationally have a huge impact on bettering our society through their grant-making activities.”



Gabrielle D. Contesti
Participant Services Coordinator

“While Millennials are set to inherit \$30 trillion in wealth transfer from aging baby boomers, they are also less trusting of financial advisors than earlier generations”

Millennial Investors Require a New Approach from Financial Advisors

We tend to think of money as simple — dollars and cents. It’s math. It should be black and white. But it isn’t. There are psychological and emotional components to it. This fact is deeply understood by the members of the Millennial generation who are saddled with debt, have experienced two extreme market drops during their short careers, and have delayed “adulthood” simply because they can’t afford it. While Millennials are set to inherit \$30 trillion in wealth transfer from aging baby boomers, they are also less trusting of financial advisors than earlier generations. Millennials are in need of the education and resources to properly manage and invest those dollars. So, how can this generation be helped?

These circumstances present a unique challenge for financial advisors. The first hurdle to overcome is building trust — Millennials are more comfortable seeking advice from their parents, or the internet, than they are from a wealth manager. An advisor who is real and relatable, preferably a person

who has experienced the same financial climate as Millennials, and who forges a heart felt connection with young investors will be the most successful. They prefer more casual forms of communication, such as email or text, and would prefer to meet in a more casual setting.

Wealth managers will need to employ a multi-faceted approach when serving Millennials by teaching them how to manage a daily budget while paying down debt and saving. Because of this, teaching fundamentals is key — basic cash management, identifying opportunities to save and goal prioritization. The first place to prioritize would be the establishment of long-term goals. If an employer offers a retirement plan, it’s important to contribute to that plan as soon as possible. Retirement will require the most savings, and it’s imperative that Millennials start as soon as they can, even while paying down debt. With traditional pensions disappearing, Millennials will be required to save more through 401(k)s and other retirement plans than any generation before them.

The goals of this generation

differ only slightly from the generations before them; they want to own a home and start a family, but only after they have paid down their student loan debt. Typically, Millennials are not interested in wealth accumulation, but rather achieving smaller, more immediate goals, such as travel.

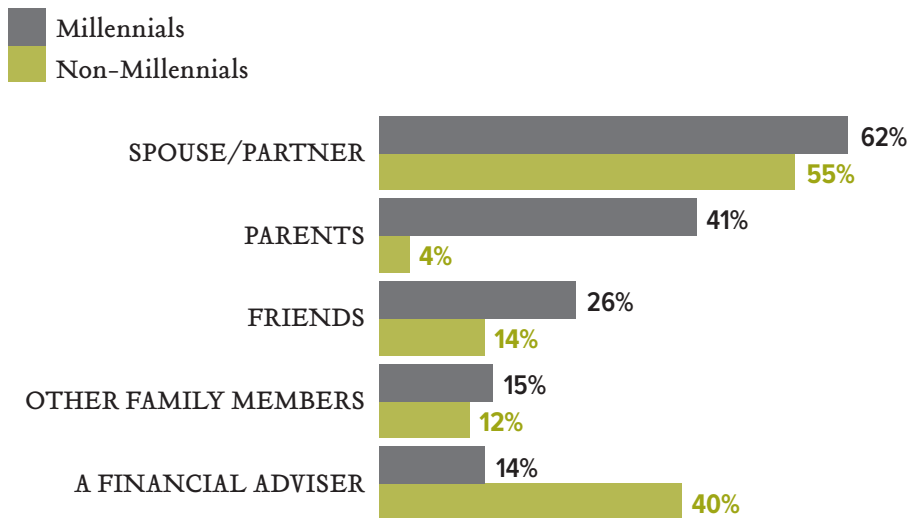
Critical advice for Millennials should be to save regardless of debt or how small their income is. If you're waiting until you are

completely out of debt to start saving and investing, you may never get started. You also waste one of the biggest elements of successful saving — time!

Getting sound advice early on is critical to building wealth over time and, more importantly for Millennials, managing their financial well being. That means young investors need financial advice now, not just once they have finally accumulated that wealth. ☑

“Critical advice for Millennials should be to save regardless of debt or how small their income is.”

WHO TO ASK — Sources of financial advice



UBS Investor Watch's *Think you know the Next Gen investor? Think again.*, first quarter 2014. THE WALL STREET JOURNAL



Charles P. Knoll
Manager Selection Analyst

The Impact of the Inclusion of China A-Shares in MSCI Indices

In mid-June, there was some big news in the index world. MSCI, a leading index provider, announced that it would be adding China's domestic equity shares to its major emerging-market indices. Changes such as this can have significant real world implications for investors and firms across the globe. In this article I will summarize MSCI's decision and discuss potential implications for Greenleaf portfolios and financial markets going forward.

What happened?

On Tuesday June 20th, MSCI voted to include a portion of China's A-shares in the MSCI Emerging Markets Index and the MSCI All Country World Index.¹ A-shares are domestically listed and domestically traded Chinese stocks only accessible to foreign investors with a Qualified Foreign Institutional Investor (QFII) license or more recently through "Stock Connect" programs. China's A-share market opened in 1992 and is currently dominated by retail investors.² Due to the market's youth, trading has been volatile and government intervention has been heavy-handed as regulators work to understand the appropriate level of control and oversight.

MSCI has considered adding A-shares to emerging market indices for years, but has been reluctant to do so because of the restricted access and an unproven implementation of new trading suspension controls.³ The most recent report from MSCI specifically cited both the new Shenzhen Connect program, which offers investors access to over 1,400 Shanghai and Shenzhen stocks, and the successful implementation of new trading suspension policies as justification for moving forward with the change.⁴

The inclusion of the Chinese market will occur as a two-phase process with the first group of stocks being added in May 2018, followed by a second group in August 2018. In total the addition will include 222 large-cap stocks, the majority of which are financial and industrial, state-owned companies.⁵

What are the implications for investors?

In the near-term, the effects will be quite minimal as the additional securities will represent just 0.73% of the Emerging Markets Index. Capital flows into the relevant A-shares are expected to total \$17-\$18 billion initially as investors seeking to replicate the index make incremental purchases.⁵ Importantly, the MSCI Emerging Markets Index already has significant exposure to Chinese stocks today, with Chinese companies listed

“On Tuesday June 20th, MSCI voted to include a portion of China's A-shares in the MSCI Emerging Markets Index and the MSCI All Country World Index.”

in Hong Kong already accounting for six of the 10 largest companies by weighting as of the end of last month.¹

While the short-term impact will likely be limited, the long-term impact could be more meaningful as the move reflects confidence from global investors and regulators in the strong prospects for China's economic development and stability of their financial markets. MSCI is the world's largest index provider, with nearly \$11 trillion in assets estimated to be benchmarked to its products.³ The inclusion of domestic Chinese A-shares is just the first step in a likely steady increase in capital flows which will drive further growth in one of the world's fastest going economies.

Conclusion

In our opinion, it was an appropriate time to include the world's second largest equity market into global emerging market indices. While the initial impact is limited, this could help drive foreign capital flows over the long-term. We believe the change will allow our emerging market fund managers better access to local Chinese stocks, while index-based strategies will adjust exposures modestly to align with the change, an effect that will be muted at the portfolio level. ☑

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“...it was an appropriate time to include the world's second largest equity market into global emerging market indices.”

Stock Market Pulse

Index	Total Return		P/E Multiples	6/30/17
	6/30/17	Since 12/31/2016		
S&P 1500	561.75	8.87%	S&P 1500	21.8x
Dow Jones Industrials.....	21,349.63	9.35%	Dow Jones Industrials.....	18.8x
NASDAQ.....	6,140.42	14.76%	NASDAQ.....	23.4x
S&P 500.....	2,423.41	9.34%	S&P 500.....	21.5x
S&P 400	1,746.65	5.99%	S&P 400	24.2x
S&P 600	855.85	2.78%	S&P 600	26.3x
NYSE Composite	11,761.70	7.82%		
Dow Jones Utilities.....	706.91	9.04%		
Barclays Aggregate Bond.....	109.51	2.40%		

Key Rates

Fed Funds Rate	1.00% to 1.25%
T Bill 90 Days.....	0.98%
T Bond 30 Yr.....	2.84%
Prime Rate	4.25%

Current Valuations

Index	Aggregate	P/E	Div. Yield
S&P 1500	561.75	21.8x	1.97%
S&P 500.....	2,423.41	21.5x	2.03%
Dow Jones Industrials....	21,349.63	18.8x	2.45%
Dow Jones Utilities.....	706.91	NA	3.45%

Spread Between 30 Year Government Yields and Market Dividend Yields: 0.87%

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