C&N Vantage Point

Annual Market Recap & Outlook

Fourth Quarter, 2017

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This Quarter's Content

Key Interest Rates	2017			
	3/31/17	6/30/17	9/29/17	12/29/17
2-yr Treasury Note	1.27	1.38	1.47	1.89
10-yr Treasury Note	2.4	2.31	2.33	2.4
30-yr Treasury Note	3.02	2.84	2.86	2.74
30-yr Fixed Mortgage	4.33	4.13	4.11	4.16
Corp. Bond Index	3.33	3.2	3.17	3.26
High-Yield Bond Index	6.18	6.06	5.98	6.16

Sources: Northern Trust/JP Morgan
Past performance does not guarantee future results, which may vary.

Key Equity Indexes - As of Quarter End	%YTD Return	NTM P/E	P/B	Dividend Yield
S&P 500	21.83	18.21	3.30	1.88
Russell 2000	14.65	24.30	2.19	1.51
Russell 1000 Growth	30.21	21.15	6.68	1.60
Russell 1000 Value	13.66	16.23	2.12	2.65
MSCI EAFE	25.62	14.95	1.74	2.94
MSCI EM	37.75	12.51	1.75	2.21

Sources: Northern Trust/JP Morgan
Past performance does not guarantee future results, which may vary.

2017 Style Performances	US Equity Style			MSCI World Style			US Fixed Income Maturity			
Equity Size	Value	Core	Growth	Value	Core	Growth	Short	Intermed.	Long	Quality
Large	13.66%	21.69%	30.21%	16.53%	22.21%	28.64%	0.68%	1.14%	8.53%	Government
Medium	13.34%	18.52%	25.27%	20.31%	23.31%	25.61%	2.56%	3.92%	12.09%	Corporate
Small	7.84%	14.65%	22.17%	17.80%	22.66%	27.74%	6.42%	7.03%	15.03%	High Yield

Source: Goldman Sachs Asset Management Market Monitor Week Ending December 29, 2017.
Past performance does not guarantee future results, which may vary.

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AS GOOD AS IT GETS

With robust economies and strong financial markets heading into 2018, this may be as good as it gets. But that can be taken in two ways — either things *have never been* better or things *will never be* better. It is a subtle but important distinction. The first carries an optimistic tone; the other assumes a more pessimistic connotation. Investors are lining up on both sides as they assess the prospects for 2018. Let's review from a variety of angles.

Growth. Synchronized global growth was the catch phrase among investors in 2017 — growth across all major developed economies showed acceleration. Meanwhile, China continued to significantly support global demand. Can this continue? The optimists believe that an object (or economy) in motion will stay in motion — and that "animal spirits" are just now making their presence felt. The pessimists will point out that the two largest economies in the world, the U.S. and China, may have difficulty living up to expectations in 2018. They note that China has started to slow from a debt-fueled growth spurt while the U.S. is growing faster than can be supported by underlying population growth and productivity gains (its economic potential).

Inflation. If the U.S. was truly growing faster than its economic potential, the optimists push back, it should show up in the inflation data. Year-over-year core inflation is at 1.5%, well below the stated 2% target. Other developed economies have even lower inflation levels: Europe at 0.9% and Japan at 0.2%. All this can change quickly, claim the pessimists, especially if wage growth accelerates due to increasingly tight labor markets.

Monetary Policy. With inflation pressures still low, central bankers are constantly being forced to defend any removal of monetary policy accommodation. In this sense, the major central banks are starting to take the pessimists' side — the "things will never be better" side — arguing inflation can only go up from here and must be curtailed before it presents a problem. This is most evident with the Federal Reserve but nascent signs of a move towards reduced accommodation are also percolating at the European Central Bank (ECB) and the Bank of Japan (BoJ) through recent actions and/or rhetoric (see details on next page). The optimists point out that even the worst case expectations call for still-easy monetary policy by all historical standards. And, with inflation so low, the best case scenario may still entail overly accommodative monetary policy well into 2018 and beyond.

Capital Markets. As interest rates remained low around the world in 2017, equity valuations pushed higher. The pessimists will note that current global equity valuations at 21.6 times earnings are materially above the long-term historical average of 17.8. The optimists will counter that, relative to low bond yields, global equities remain very attractive especially in a low volatility world (a premise, pessimists quickly retort, will soon end given rising interest rates and elevated political tensions).

In summary, heading into 2018, the focus will be on the current global growth momentum, whether inflation awakens and how central bankers react to it all. These factors will determine whether this is as good as it gets — or as good as it *will* get.

FOURTH QUARTER AND 2017 TOTAL RETURNS

All asset classes were positive for the year, with equities well into double digits.

	FIXED INCOME						EQUITIES			REAL ASSETS		
	Cash	Muni	Inv. Grade	TIPS	High Yield	EM Debt	U.S.	Dev. Ex-U.S.	EM	NR	GRE	GLI
■ 2017	0.8	5.4	3.5	3.0	7.5	15.2	21.3	25.8	37.3	22.7	15.0	20.1
4Q17	0.3	0.7	0.4	1.3	0.5	0.8	6.3	4.5	7.7	8.6	3.8	1.9

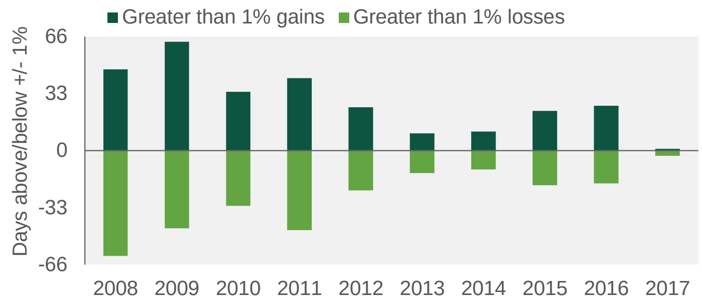
Source: Northern Trust Investment Strategy, Bloomberg. NR = Natural Resources; GRE = Global Real Estate; GLI = Global Listed Infrastructure. EM = Emerging Markets. Indexes are gross of fees and disclosed on last page. **Past performance is no guarantee of future results.**

KEY THEMES

Global Equities: A Year for the Record Books

Global equities returned 25% in 2017. But it's how they did it that's so impressive. Global equities only suffered two days of greater than 1% losses (one prompted by the announcement of the Mueller investigation; the other related to North Korean tensions) and only experienced one day of a greater than 1% gain (the day after Emmanuel Macron won the first round of the French elections). In most years, this metric is well into double-digits on both sides (see chart). The standard deviation of global equities in 2017 was just below 3%, a risk level normally reserved for investment-grade bonds. Further, global equities had positive returns in every single month of 2017 — the first time ever, based on the available data.

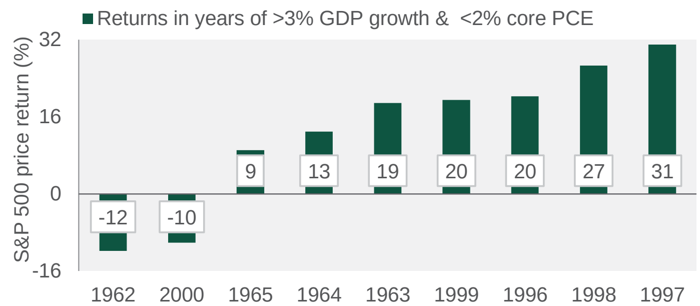
NUMBER OF 1% DAYS ON THE GLOBAL STOCK MARKET



The Powerful Duo of Global Growth and Stuckflation

Global growth was strong all year and accelerated into year's end, allowing for double-digit earnings growth across all major equity markets. Meanwhile, core inflation levels remained stuck below 2% on a global basis, keeping central bank policy easy and equity valuations elevated. U.S. real gross domestic product (GDP) has surpassed 3% in recent quarters while personal consumption expenditure core price index (PCE) remains below the Fed's 2% target at 1.5%. The U.S. has experienced this "goldilocks" (just right) environment in nine prior years (all in the early 60s or late 90s). Returns have been generally good; but with two exceptions: 1962 (the "Kennedy slide") and 2000 (the start of the dot-com bust).

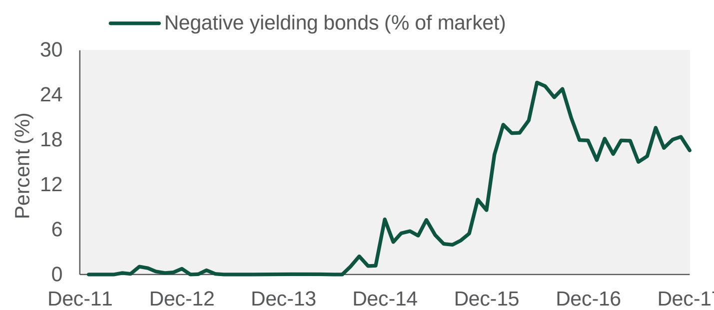
U.S. EQUITY RETURNS IN "GOLDILOCKS" ENVIRONMENTS



Still Accommodative After All These Years

Major central banks, including the Fed, the ECB and the BoJ, have now spent nearly a decade in ultra-easy money mode. There are signs that this is slowly changing. The Fed raised policy rates three times (now targeting a range of 1.25-1.50%) and began to reduce the size of its balance sheet by not reinvesting maturing assets (subject to a cap). The ECB announced that its quantitative easing purchases will be cut in half (from €60 to €30 billion/month) starting in 2018. Even the BoJ hinted at reducing accommodation sometime in the not too distant future (though unlikely in 2018). However, monetary policy remains very easy by historical standards, with 17% of the global bond market carrying negative yields.

NEGATIVE YIELDING DEBT



A Note on Bitcoin

Bitcoin was no doubt a popular discussion topic at holiday dinner tables given its 1,500% price increase in 2017. Bitcoin followers generally fall into one of three camps. The first views bitcoin as the gold of the 21st century. Just like gold, bitcoin has no real intrinsic value but has limited supply and provides an alternative to currencies controlled by printing press-happy central banks. The second groups bitcoin with the long list of asset bubbles — a modern day tulip mania that will end in ruin as demand wanes or dissipates across the hundreds of bitcoin substitutes. The third sees the true value in the blockchain technology that underpins bitcoin, which could materially reduce transactional frictions across multiple markets by eliminating the need for a trusted central clearing agent.

BITCOIN IN 2017

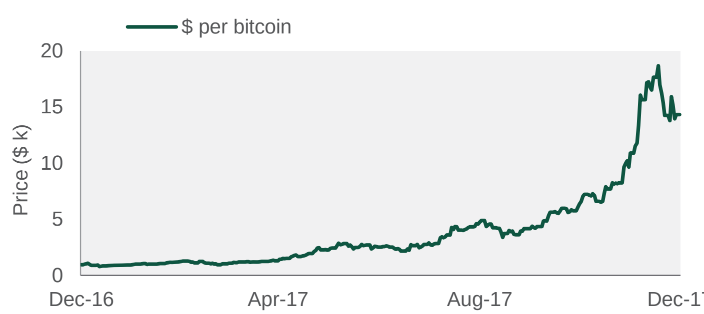


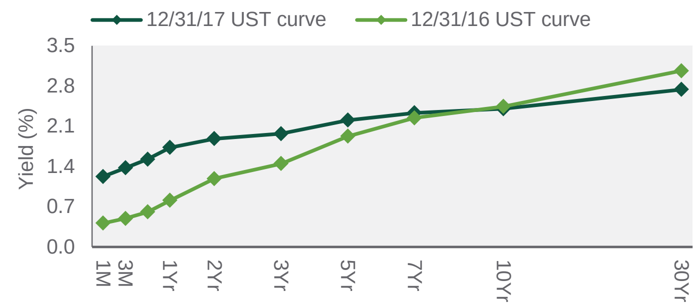
Chart Sources: Northern Trust Investment Strategy, Bloomberg. Indexes are gross of fees. **Past returns are no guarantee of future results.** Charts are as of December 31, 2017.

MARKET REVIEW

Interest Rates

The U.S. yield curve materially flattened in 2017. The Fed managed to push through three rate hikes, lifting the short-end of the yield curve throughout the year. However, low inflation and low/negative interest rates outside the U.S. left the 10-year Treasury yield mostly flat and the 30-year Treasury yield 0.3% lower during 2017. Close attention is paid to the shape of the yield curve as an inverted yield curve (where long-end rates are lower than short-end rates) has historically foreshadowed economic recession. During 2017, the 10-year minus the 2-year yield spread (a common measure of yield curve steepness) fell from 1.3% to 0.5%. This is below the long-term average of 0.9% but still some ways from inversion.

YIELD CURVE



Credit Markets

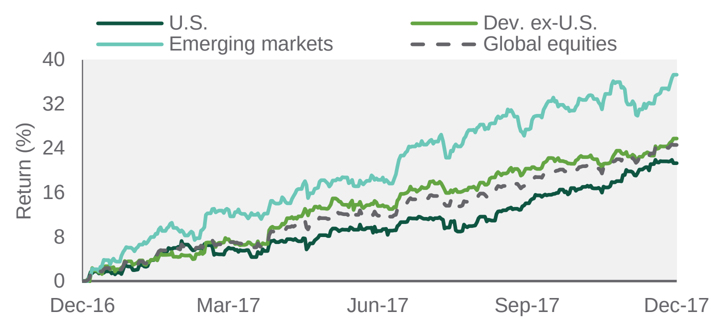
Credit spreads generally moved lower throughout 2017, driven by the combination of solid fundamentals, low interest rates and healthy investor demand. Investment-grade spreads started the year at 118 basis points (bps) and finished at 89 bps, a 29 bps improvement and a level not seen since mid-2007 (the all-time low of ~50 bps was hit in 1997). High-yield spreads started the year at 409 bps and also ended the year lower (by 66 bps to 343 bps) but took a choppier path. On three separate occasions high yield spreads jumped by ~50 bps, driven by temporary technical issues (abnormal supply) and short-lived investor jitters heightened by rich valuations (though spreads still remain ~20 bps above mid-2014 levels).

CREDIT SPREADS

Equities

Global equities had an excellent year. All major equity regions — U.S., developed ex-U.S. and emerging markets — saw greater-than 20% returns. The 21% U.S. equity return was driven by ~14% earnings growth, ~5% valuation expansion and a ~2% yield from dividend payments. Developed ex-U.S. equities returned 26%. Compared with the U.S., earnings were stronger (up ~21%) and dividend income was higher (~4%). The weak dollar provided a currency boost (~9%) but that benefit was entirely offset by valuation contraction. Emerging market equities fired on all cylinders, a 37% return driven by: ~22% earnings growth; ~5% valuation expansion; ~7% currency appreciation and a ~3% dividend yield.

REGIONAL EQUITY INDICES



Real Assets

Real assets performed admirably in 2017 (all with double-digit returns) but failed to match the performance of global equities. Global listed infrastructure (GLI) gained 20% by exploiting 2017's mix of steady interest rates, higher equity markets and somewhat jittery investors (with GLI serving as a lower-risk alternative to listed real estate). Global real estate (GRE), returning 15%, received some of the same benefits from low rates but faced offsetting headwinds in the form of poor investor sentiment, with increased concerns over the technology-induced impacts on retail (Amazon), commercial (shrinking offices) and other rents. Natural resources (NR) overcame first-half commodity supply worries to return 23%.

REAL ASSET INDICES

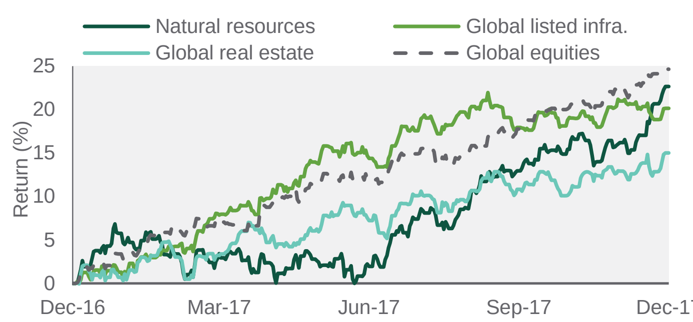
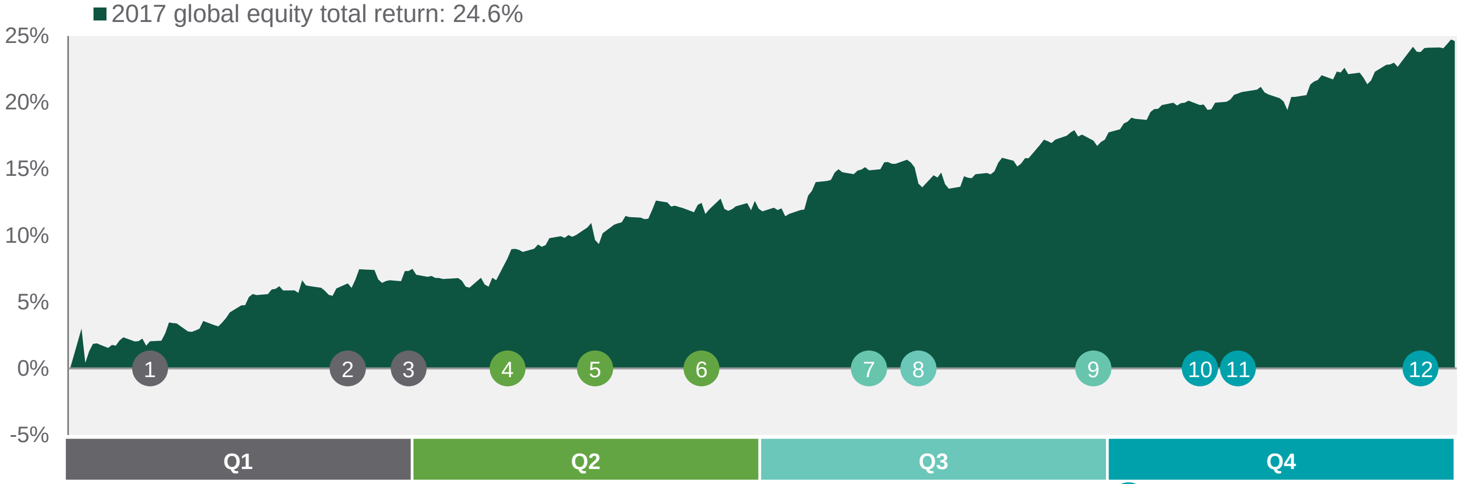


Chart Sources: Northern Trust Investment Strategy, Bloomberg. UST = U.S. Treasury. Indexes are gross of fees. **Past returns are no guarantee of future results.** Charts are as of December 31, 2017.

MARKET EVENTS



Q1

1 Donald Trump becomes the 45th U.S. president, ushering in one-party control of government policy after six years of split power in Washington D.C.

2 Pro-reform Prime Minister Narendra Modi's BJP party scores big election win in India's largest state; emerging market equities jump 1.3%.

3 The U.K. invokes Article 50 of the Lisbon Treaty, formally triggering the start of Brexit negotiations with Europe.

Q2

4 European stocks up 2.2% after French voters support Emmanuel Macron for French president in first round of voting; Macron beats Marine Le Pen in runoff two weeks later.

5 U.S. equities suffer a nearly-2% drop as Robert Mueller is named special counsel to oversee investigation into potential Trump-Russian collusion.

6 Federal Reserve unveils plan for slowly shrinking $4.5 trillion balance sheet accumulated from years of quantitative easing; plan put into action in October.

Q3

7 John Kelly replaces Reince Preibus as White House chief of staff; White House Comm. Director Anthony Scaramucci fired soon thereafter (just 10 days on the job).

8 The volatility index (VIX) reaches its highest level since the U.S. election as military threats are ex-changed with North Korea over nuclear ambitions.

9 German Chancellor Angela Merkel is re-elected for fourth term but overall results disappoint; right wing AfD party takes 13% of Bundestag seats.

Q4

10 Japan Prime Minister Shinzo Abe wins snap election, giving him another four years in office. An improving economy (six straight quarters of growth) helped secure victory.

11 Trump nominates Jerome Powell, a current Federal Reserve governor, for Fed chair. He will replace Janet Yellen on February 3, 2018.

12 Republican-driven tax reform is signed into law. The bill cuts taxes by about $1.5 trillion over 10 years, the biggest change to the tax code since 1986.

Indexes used: Bloomberg Barclays (BBC) 1-3 Month UST (Cash); BBC Municipal (Muni); BBC Aggregate (Inv. Grade); BBC TIPS (TIPS); BBC High Yield 2% Capped (High Yield); JP Morgan GBI-EM Global Diversified (Em. Markets Fixed Income); MSCI U.S. Equities IMI (U.S. Equities); MSCI World ex-U.S. IMI (Dev. ex-U.S. Equities); MSCI Emerging Market Equities (Em. Markets Equities); Morningstar Upstream Natural Resources (Natural Res.); FTSE EPRA/NAREIT Global (Global Real Estate); S&P Global Infrastructure (Global Listed Infra.)

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What You Should Know: Tax Cuts and Jobs Act of 2017

By Mike Charles, CPA, VP/Trust Officer

On December 22, 2017, the Tax Cuts and Jobs Act (H.R. 1) ("the Act") was signed into law. Designed to reduce taxes for individuals and businesses, stimulate the economy and create jobs, many commentators have described it as the most comprehensive tax overhaul since the Tax Reform Act of 1986. In addition to its significant changes to the Internal Revenue Code, the Act also impacts the Affordable Care Act (ACA) by repealing the individual shared responsibility requirement, otherwise known as the "individual mandate."

Fast Facts

- Most provisions of the Act took effect as of January 1, 2018
- In general, the individual changes are scheduled to be phased out after 2025.
- The Internal Revenue Service will issue revised withholding tables in January 2018
- Employees will begin seeing changes in their payroll withholdings as early as February 1, 2018
- Few notable changes during the upcoming 2017 tax return preparation season
- Many planning opportunities for 2018 and beyond
- The following information is intended to provide a brief summary of the Act and its changes to relevant law, and to alert the reader to opportunities and risks.

Significant Changes

- While there are many changes associated with the Act, the list below is a summary of the most significant changes that will likely affect most taxpayers.

Individuals:

- Reduces individual income tax rates 0%-4%, depending on the bracket:

Previous Rates	New Rates
10%	10%
15%	12%
25%	22%
28%	24%
33%	32%
35%	35%
39.60%	37%

- Increases in standard deductions:

Married filing jointly	$24,000
Heads of household	$18,000
Singles, married filing separately	$12,000

- Elimination of personal exemptions.
- Doubling of the child tax credit to $2,000 and allowance of the credit against payroll (Social Security and Medicare) taxes for certain lower income taxpayers.
- Left unchanged is the 3.8% Net Investment Income tax provided for by the Affordable Care Act.
- Reduction of the adjusted gross income (AGI) threshold for the medical expense deduction to 7.5% for regular and AMT purposes for 2017 and 2018 only.
- New $10,000 ($5,000 for married filing separately) limit on the deduction for state and local taxes.
- Reduction of the mortgage debt limit for the home mortgage interest deduction to $750,000 ($375,000 for married filing separately) and limited to acquisition debt only.
- Elimination of the deduction for interest on home equity debt.
- Elimination of miscellaneous itemized deductions subject to the 2% floor (for example, investment expenses, legal and accounting fees and unreimbursed employee business expenses).
- Changes to the rules for tax-free Section 529 plan distributions to allow distributions used to pay qualifying elementary and secondary school expenses, up to $10,000 per student per tax year.
- Repeals the deduction for alimony payments and their inclusion in taxable income of the recipient, applicable only to divorce or separation instruments executed after December 31, 2018.
- The "Kiddie Tax" rules on taxation of unearned income of children under age 23 remain; however, the portion not taxed at the child's rate now will be taxed at fiduciary income tax rates instead of the parents' individual income tax rate.
- Significant increases to the gift and estate tax exemptions, to $10 million for 2017 and indexed annually for inflation.

Businesses:

- Graduated C corporation tax rates ranging from 15% to 35% are replaced with a flat corporate rate of 21%, with certain lower rates available for repatriation of corporate earnings held overseas.
- While the individual and fiduciary AMTs remain, the 20% corporate AMT is repealed.
- New 20% qualified business income deduction for owners of flow-through entities. Entities affected will be sole proprietorships, partnerships, limited liability companies and S corporations. Limits apply to earnings from specified service businesses.
- Doubling of bonus depreciation to 100% and expansion of qualified assets to include used assets, effective for assets acquired and placed in service after September 27, 2017, and before January 1, 2023.
- Doubling of the Section 179 expensing limit to $1 million and an increase of the expensing phaseout threshold to $2.5 million.
- Disallowance of deductions for net interest expense in excess of 30% of adjusted taxable income, defined generally as earnings before interest, depreciation, taxes and amortization (EBITDA). Significant exceptions to this change are available for real estate businesses and businesses with gross receipts of less than $25 million per year.
- Addition of new limitations on deductions for employee fringe benefits, entertainment and meals and transportation.

Conclusion

Certain provisions have received more attention than others, but all taxpayers will be impacted. Although charitable contributions remain deductible, the significant increases in standard deduction amounts will greatly curtail the ability of many taxpayers to take advantage of these deductions. The large increases in federal estate and gift tax exemption amounts may discourage charitable giving as a component of estate planning. Other charitable giving vehicles, such as qualified charitable distributions (QCD) from Individual Retirement Accounts for those age 70 ½ and older, will become even more useful. Every individual, business and charity should be careful to consider the provisions of the Act and to consult with his or her or its tax advisor promptly.

C&N PORTFOLIO POSITIONING: MODEST OVERWEIGHT TO RISK

C&N Vantage Points - January 2018

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Market Views:
Domestic Equity Valuations Will Remain Stretched. International Equity Remain Appealing
Diversification Remains Paramount. Remaining Invested Is Important
A Market Correction Would Be An Opportunity

Market Risks:
Tax Reform Proves To Have Little Economic EffectFed
Fed Rate Hikes Lead To A Flat Or Inverted Yield Curve
Geopolitical Risks & Trade War Risks Increase

Risk Type	Asset Class	Sector Category	Under Weight	Neutral	Over Weight	Viewpoints
Risk Control	Cash/Cash Alternatives	Ultrashort Bonds		●		These sectors give us cash in the event of a market correction. With the Fed hiking rates, we are opportunistic in redeploying these monies. Adding to Small Cap Value in 3Q is one example.
	Alternatives (Fixed Based)	Absolute Return			●	In a low-rate environment, we maintain our increased exposure to these sectors to provide better-than-money market returns while decreasing our overall risk profile.
		Inflation-Linked Bonds			●	TIPS appear fairly valued. Inflation expectations have begun to rise so we continue to monitor its impact. We decreased duration in 4Q17 to offset Fed rate hike impact.
	Fixed Income	US Investment Grade Bonds	●			We have a slight overweight to IG Corps and remain underweight to U.S. Govt bonds due to a tightening Fed and inflationary forces building. Overall, the category remains underweight.
		International Bonds	●			Foreign central banks are beginning to talk down their continuation of extraordinary policies which may leave this category stretched in its valuation.
		Emerging Markets Bonds		●		Spreads tightened throughout 2017 but EM fundamentals are solidifying and valuations improving. Trade war risks appear to be abating. We'll monitor EM bonds for a possible shift to overweight.
Risk Assets		High Yield Bonds			●	The sector benefits from the "risk-on" trade. High-Yield's coupon remains attractive in a flat yield curve environment. Tax reform will help marginally profitable companies. Overweight maintained.
	Equities	US Large Cap			●	Although fairly valued, we believe growth continues. The bias is to the upside for at least the next quarter. We retain a slight overweight in LCV and LCG and look to buy on market pullbacks.
		Developed Ex-US		●		Monetary policies are expected to remain supportive. Valuations are reasonable compared to the U.S. As political headwinds subside, this category's weighting may be re-assessed.
		US Mid & Small Cap		●		Mid Caps remain fairly valued. SCG has outperformed. With tax reform & rate hikes likely in 2018, we're biased toward value for both Small & Large Caps, where financials and energy tend to reside.
		Emerging Markets		●		Even after its 2017 outperformance, EM valuations and opportunities remain fair. Fundamentals are improving. Trade war risks may be abating. We'll monitor for a possible move to overweight.
	Alternatives (Equity Based) & Real Assets	Real Estate		●		Fundamentals remain solid for the REIT category, but a tightening Fed and retail shopping center challenges create headwinds. The risk/reward scenario leads us to maintain our allocation.
		Commodities/Natural Resource		●		Oil finding a base, a tightening Fed, building inflationary forces and a positive demand/supply story expected in metals in the coming years leads us to maintain our position and monitor it.

Note: Views are subject to change based on market conditions and other factors. These views should not be construed as a recommendation for any specific security or sector.
Client portfolios may or may not be at the recommended weightings above due to, but not limited to: distributions, tax management limitations, systematic purchases, etc.

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Fourth Quarter, 2017

Meet Our Experts

Mike Charles

Vice President & Trust Officer

A C&N employee since October 2001, Mr. Charles holds his BA degree in financial accounting, graduating from Lycoming College in 1996. In August of 2003, Mr. Charles earned the designation of Certified Public Accountant (CPA). He is a member of the Pennsylvania Institute of Certified Public Accountants (PICPA) and is past president of its North Central chapter, is a member of the Pennsylvania Bankers Association Government Relations Policy Committee and was a member of its predecessor Tax, Trust and Estates Advisory Committee, and has served as an instructor with Pennsylvania Bankers Association Professional Development Network. Active in his community, Charles is a board member and past president of the Wellsboro Area Chamber of Commerce and is a member of its Enhancement, Finance and Laurel Festival committees.