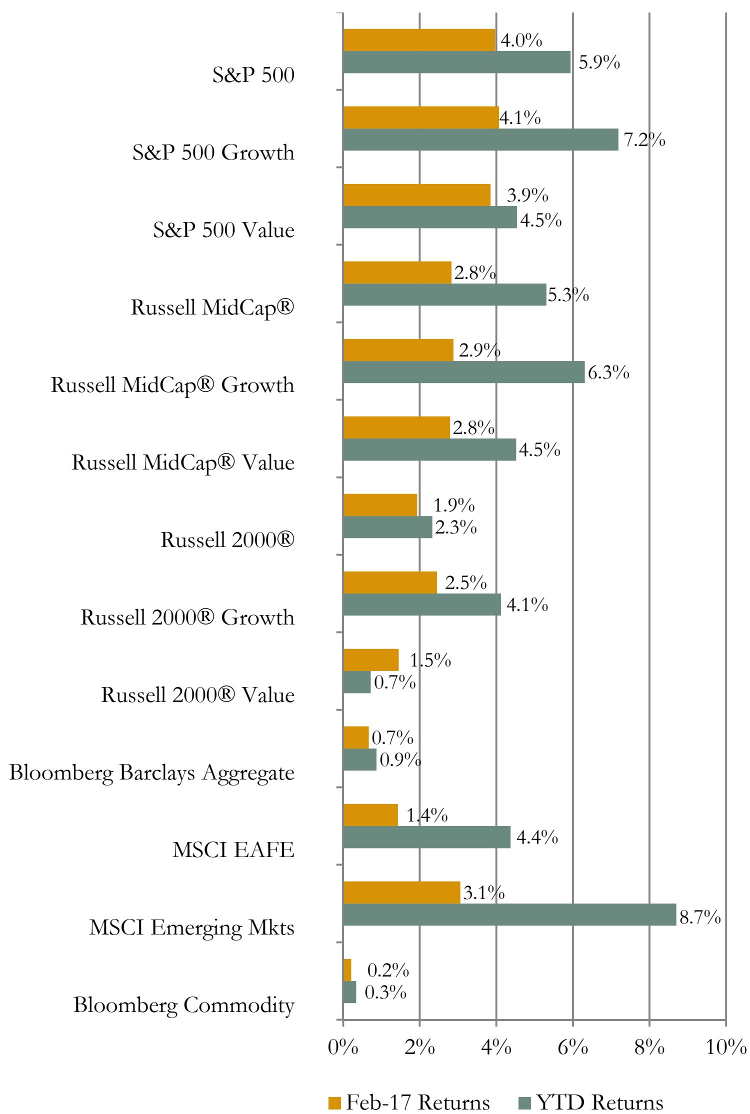
Monthly Market Summary – February 2017

U.S. and global equity markets continued to rally in February. Various indices including the Dow Jones Industrial Average (DJIA) and the S&P 500 hit several new record highs during the month. The DJIA made headlines when it registered a new record closing high for 12 days in a row. That streak broke a 30-year record for consecutive daily new highs. The S&P 500 had nine new closing highs during the month. Tax cut and various business friendly comments by President Trump had a positive impact on sentiment which provided a boost to equity markets. Several better than expected U.S. and global economic data reports, a shift in inflation data, and a solid corporate earnings reporting season also fueled the rally. Given the pro-growth policy comments and improving economic data, it is not surprising that economically sensitive stocks have been among the best performers, with the exception of energy stocks, which appear to be consolidating after posting sizeable gains in 2016. Healthcare has also been a top performing sector as biotechnology stocks have been rebounding from a weak 2016 on good earnings reports. The bond and commodity markets had mostly positive, but more modest, returns for the month as measured by the Bloomberg Barclays Aggregate Bond and the Bloomberg Commodity indices shown in the chart to the left.

Market Indices – February 2017



President Trump's pro-growth policy comments have been capturing the most attention but more importantly the majority of economic data released during February indicates a pick-up in economic activity. For example, the U.S. Institute for Supply Management's manufacturing purchasing managers' index increased to 56.0, which was the fifth consecutive monthly increase and the non-manufacturing index remained well into expansion territory at 56.5. The IHS Markit composite purchasing managers' index for the eurozone surprised analysts with an increase to 56.0, which was the highest level since April 2011. The underlying components of the report were also positive with new orders coming in at the highest level in six years and hiring the strongest since before the financial crisis. The improvement in activity was driven largely by Germany and France which both had significant pick-ups in activity. The U.S. housing market was mostly positive with building permits up 4.6% to a 10-year high. Existing home sales also reached a 10-year high and pending home sales increased 1.6%. Inflation numbers are higher around the world and getting close to central bank targets. The U.S. consumer price index (CPI) was up 0.6% from the prior month bringing the year-over-year change to 2.5%. The producer price index increased a more than expected 0.6%. The eurozone inflation rate moved up to 1.8%. Much of the inflation rate increase was due to higher energy prices. The United Kingdom inflation rate reached the highest level since 2014 on the weakening pound.

The improving economic data is significant not only because it supports higher equity prices, but also because it factors into the Federal Reserve Open Market Committee's (Fed) interest rate policy decisions. In her testimony to Congress during February, Fed chair Yellen signaled that the Fed may be ready to raise the federal funds rate "fairly soon". The firming global economic conditions and the pick-up in inflation close to the Fed's target have increased the probability of a rate hike as soon as at the Fed's March meeting.

Major U.S. equity market index returns were positive for the month of February. The large-capitalization (cap) indices had higher gains than mid and small-cap indices. The stronger gains of the large-cap indices are due in part to the significant amount of money flowing into the U.S. equity market through passively managed exchange traded funds (ETFs). Large-cap index products tend to receive the bulk of flows into ETFs. Growth stocks continued to outperform value stocks in each of the market cap categories. Healthcare, a growth sector, was the top performing sector for the month in each market cap category. Information technology stocks, which are also mostly growth stocks, were also among the top performing for the month. Financial stocks had strong gains boosted by the prospect of a reduction in regulations affecting the industry along with increasing expectations for higher interest rates with the Fed raising rates possibly as soon as March. The energy sector, which sold-off in January, continued to decline in February despite oil trading in a tight range. The energy sector had a negative return and was the weakest performing sector in each market cap category.

International equity market returns were mostly positive for February. The MSCI EAFE index of developed international market equities and the MSCI Emerging Markets (EM) index had returns for February of 1.4% and 3.1% respectively on a U.S. dollar basis. Currency moves had a mixed impact on the returns for U.S. investors as the dollar strengthened against the euro, pound, and franc but weakened against emerging market currencies. On a local currency basis, the EAFE index had a return of 2.2% and the EM index had a return of 1.7%. Sector results in developed international markets were similar to results in the U.S. equity market. Growth stocks outperformed value stocks and healthcare was the top performing sector while energy had a negative return and was the weakest sector. In emerging markets, value outperformed growth since industrials, financials, and consumer discretionary stocks were the best performing. Just as in the U.S. and developed international markets, energy had the lowest return in emerging markets. On a geographic basis, among developed international countries, the Pacific ex Japan region had the highest return due a strong gain in Australia. Many European country indices had modest returns since stock prices were pressured late in the month by concerns about the upcoming French election. Among the emerging economies, the BRIC (Brazil, Russia, India, and China) index was a top performer. Strong returns for Brazil and India - due to central bank actions seen as positive - offset the negative return for Russia.

All sectors of the U.S. bond market posted positive returns for February leading the Bloomberg Barclays U.S. Aggregate Bond index to post a return of 0.7%. The benchmark 10-year Treasury bond traded in a tight range of 2.30% to 2.60% during the month. The 10-year Treasury yield closed the month at 2.36%, which was little changed from the prior month-end closing yield of 2.46%. Corporate bonds generally outperformed government bonds on strong capital inflows, low new supply of bonds, and improving credit conditions. The corporate high yield sector was the strongest performer with that index gaining 1.5% for the period. An interesting development occurred in the international bond market. German government bonds are considered to be safe haven assets by many market participants and demand for German bonds often rises when investor concerns increase. During February the yield on the two-year German bond fell to a record low of -0.96% as fears swelled about the stability of the European Union and the French election.

The Bloomberg Commodity index had a return for February of 0.2%. Precious metals, industrial metals, and some agriculture sub-indices posted gains while the energy index declined. Metals prices have been driven higher in part due to policies implemented in China intended to boost economic activity. Silver had the largest gain of over 5% for the month. Natural gas drove the energy sector lower with a decline of about 12%. Oil traded in a tight range of $50-$55 as production cuts by the Organization for Petroleum Exporting Countries (OPEC) and others have been offset by increasing U.S. production. Oil ended the month at $54.15 per barrel, up slightly from $52.80 at the end of January.

Vogel Consulting, LLC (Vogel) Tactical Recommendations

No changes were made to our tactical asset allocation recommendations during February. Our tactical asset class recommendations include an equal weight position in U.S. large-cap, mid-cap, and small-cap stocks. Economic data is showing improvement. In addition, expectations continue to be high that business-friendly economic policies such as tax cuts and infrastructure spending favored by President Trump will lead to higher economic growth in the U.S. even though the details and timing of policy changes are uncertain. We also recommend an equal weight position in emerging market equities due to improving economic conditions and country fundamentals. We recommend an underweight to developed international equities even though there are some signs of improving economic conditions because uncertainty remains high in Europe due to several upcoming elections in addition to Brexit (the United Kingdom leaving the European Union) issues. Also, the U.S. dollar is likely to strengthen due to higher interest rates relative to other developed countries. A stronger dollar could dampen international equity returns for U.S. investors. We continue to recommend an equal weight to hedge fund strategies and an underweight to fixed income. We favor hedge fund strategies over fixed income for the lower expected volatility portion of portfolios since bond yields are near historically low levels and are likely to rise and bond prices fall as central bank polices are adjusted. Recent Fed comments point to a rate increase possibly as soon as in March. Within fixed income we continue to recommend a focus on short to intermediate term bonds. We also continue to favor non-Treasury bonds for the yield advantage they provide compared to Treasury bonds. Since our expectation is for a moderate rate of inflation to continue, we recommend an equal weight to real assets. We would not be surprised if financial markets experience bouts of volatility as more details emerge about any fiscal, monetary, or political policy changes or if there are delays in implementing these actions. Therefore, we continue to recommend using periods of market strength to raise any cash needed to support spending needs over the coming 12-24 months.