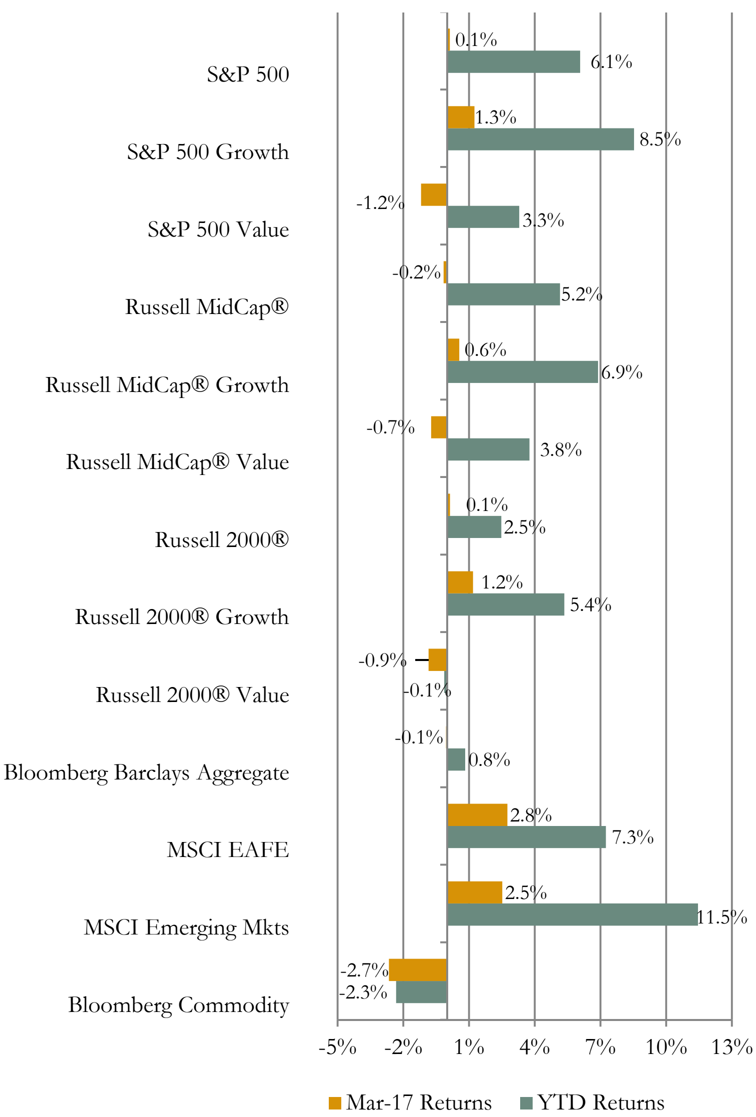
Monthly Market Summary – March 2017

Global financial markets were swayed throughout March by various cross currents resulting from generally positive economic data reports and several political and policy developments. The result was essentially flat returns for major U.S. equity and bond indices, higher returns for international equities, a lower U.S. dollar, and lower commodity prices.

On the economic news front there were indications that economic activity is picking-up in various regions. In the U.S., new jobless claims reached a 44-year low, job openings increased to 5.6 million, and average hourly earnings were up 2.8% over the prior year. The Institute for Supply Management's purchasing managers' index (PMI) manufacturing index increased to 57.7, which was the sixth consecutive monthly increase, and the non-manufacturing index increased again. Reports such as these helped push consumer confidence up to a 16-year high. In Europe, the IHS Markit composite PMI report came in above analyst forecasts as both services and manufacturing moved higher. In the United Kingdom (UK) retail sales surprised on the upside. In emerging markets, the manufacturing PMI for China moved higher on an uptick in exports. Exports were also higher in Mexico helped by a weak peso.

Market Indices – March 2017



On the political and policy front, changing expectations about the outlook for President Trump's pro-growth policies was a key factor in market movements. For example, the S&P 500 index hit a new record high on March 1, the day after Mr. Trump's address to Congress affirmed expectations for more fiscal spending, deregulation, and tax reform. But the index declined during much of the month as House Republicans tangled over the bill to repeal the Affordable Care Act. The failure to reach an agreement on the heath care bill ignited concerns that other stimulus and reform measures on Trump's agenda will also be difficult to pass and so dampened expectations for a boost to economic activity in the near-term. The other key policy event in the U.S. during March was the decision by the Federal Reserve Open Market Committee (FOMC) to raise the federal funds rate target by 0.25% to 0.75%-1.00%. The FOMC also maintained their previous forecast for a gradual pace for additional rate hikes this year. U.S. stocks advanced after the decision was announced while the dollar declined which provided a boost to commodities and emerging markets equities. Outside the U.S., two important events occurred in March. First, in the Dutch election, the pro-Europe party retained the majority which helped calm concerns about the spread of the populist movement and the corresponding threat for a break-up of the European Union (EU). European stocks moved higher on the news. On March 29, the prime minister of the United Kingdom (UK), formally triggered Article 50 setting in motion the withdrawal of the UK from the EU (Brexit). Uncertainty about the impact of Brexit on the UK and other EU countries came to the forefront again.

Major U.S. equity market index returns were mixed for the month of March. The S&P 500, Russell MidCap®, and Russell 2000® growth indices with small positive returns outperformed the value indices which had negative returns. Information technology and consumer discretionary stocks were the top performing sectors for the month as investors favored companies that can grow earnings without a boost from tax cuts or increased infrastructure spending. The financials sector had the lowest return in the large and mid-cap indices and the second lowest return in the small-cap index. Financials declined despite the FOMC decision to raise interest rates at its March meeting. Concerns about delays in passage of tax reform was a factor in the sector's weakness along with a decline in business lending. The energy sector had the lowest return in the small-cap index as the sector was pressured by lower oil prices.

International equity market returns were positive for March and outperformed U.S. returns. The MSCI EAFE index of developed international market equities and the MSCI Emerging Markets (EM) index had returns for March of 2.8% and 2.5% respectively on a U.S. dollar basis. Currency moves had a positive impact on the returns for U.S. investors as the dollar weakened moderately. On a local currency basis, the EAFE index had a return of 2.4% and the EM index had a return of 1.9%. Sector results in developed international and emerging markets were similar to results in the U.S. equity market. Growth stocks outperformed value stocks and information technology was the top performing sector. The weakest sector in developed international markets was materials and in emerging markets was health care. On a geographic basis, among developed international countries, the euro area had the highest return on improving economic data and better sentiment resulting in investors adding to allocations to the region. In emerging markets, Mexico was a top performer with a return of almost 10%. The weak peso along with a strengthening U.S. economy have been positive for Mexican exports. Strong exports reports from Korea provided a boost to stocks there. India was another top performer as the economy appears to have adjusted to the demonetization policy enacted last year.

U.S. bond market returns were mixed for March leading the Bloomberg Barclays U.S. Aggregate Bond index to post a return of -0.1%. The benchmark 10-year Treasury bond yield briefly reached 2.6% in March but dropped again after the FOMC meeting when there was no change to the forecast for future rate hikes and after the healthcare bill failed. The 10-year Treasury yield closed the month at 2.39%, which was little changed from the prior month-end closing yield of 2.36%. Bonds with shorter time to maturity had better returns than longer maturity bonds since yields did move somewhat higher. Corporate and municipal bonds generally outperformed government bonds as demand for the extra yield supported prices.

The Bloomberg Commodity index had a return for March of -2.7%. The livestock sub-index had a small positive return but each of the other sub-indices we track had a negative return for the month. The grains and petroleum sub-indices had the lowest returns. Oil started the month at $54.15 but declined to as low as $48 on reports of high supply levels as U.S. production has been increasing. Oil prices turned higher again late in the month and closed at $50.74 on March 31.

Vogel Consulting, LLC (Vogel) Tactical Recommendations

No changes were made to our tactical asset allocation recommendations during March. Our tactical asset class recommendations include an equal weight position in U.S. large-cap, mid-cap, and small-cap stocks. Even though valuations are above average, economic data and corporate earnings are showing improvement and the FOMC monetary policies are still accommodative. We also recommend an equal weight position in emerging market equities due to improving economic conditions and country fundamentals. We continue to 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 uncertainty. Also, the potential remains for the U.S. dollar to trend higher again as the year goes on despite the recent move lower. The dollar is likely to strengthen due to higher interest rates and a higher economic growth rate in the U.S. relative to other developed countries. Another possible boost to the dollar could come if a tax cut would be passed. A stronger dollar would 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 comments by FOMC members continue to point to two additional rate increases this year. 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.