

Q1 2017 – Market Overview Newsletter

Economic Update

U.S. stock markets swelled to record levels in the 1st quarter of 2017 on a wave of investor optimism from last November's presidential election. The bull market continued through President Trump's inauguration and his first month in office, as investors brightened to the prospects for tax cuts, infrastructure spending, deregulation and more to help spark U.S. economic growth and lift equity prices. For the quarter, the benchmark S&P 500 Index gained 6%, rising on the strength of growth stocks and technology shares. Large-caps outpaced small-caps in Q1, although small company stocks remain the better performer since Election Day. International markets performed better than the U.S. during the quarter, especially broad European stock indexes, Asian markets excluding Japan, and emerging markets in general.

Improving reports on the U.S. economy, including employment and wage growth, prompted the Federal Reserve to raise its target rate by a quarter-point in March. Specifically, a strong jump in the annual inflation rate for February—to the highest point in nearly five years—made the Fed's decision all but certain by the time it was announced. Interest rates on government and corporate bonds rose on these expectations. But more significantly, the Fed cooled some of the

market speculation that they would raise rates at a faster pace going forward. Their stated goal is two additional rate hikes for the remainder of 2017, but as of this writing, the market sees just one rate increase as likely in the next nine months.

After flat performance for equities in March, talk of "animal spirits" lifting the stock higher seems to have run its course. That does not mean the outlook for stocks is altogether negative. In fact, there are strong economic fundamentals to support the case for stocks, from upward revisions to GDP, to improvement in housing starts, durable goods orders and corporate earnings. The failure of the Republican-led House of Representatives to hold a vote on dramatically changing the Affordable Care Act ("Obamacare") deflated some of the lofty expectations around possible tax and regulatory reform. Bringing change to Washington is not an easy task. In an environment where seemingly anything can happen; with U.S. stock markets reaching expensive levels, rising interest rates and changes around the globe, now may be an especially important time to stay diversified.

For more market details, see the "Capital Analysts Q1 2017 Market Review" in the commentaries page on our website at www.langdonshaw.com/commentaries. -LS

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