Financial & Economic Review

The dominant story in the United Stated at the start of 2017 was the beginning of the Trump Administration. With that came expectations of lower personal and corporate tax rates, rolling back of corporate regulations, increased interest rates, increases in military spending and an emphasis on U.S. infrastructure spending. These prospects have largely led to an increase in the broader U.S. markets throughout the quarter. With markets pricing in this optimism, any major retracement in expectation may lead to a short-term market pause or pullback. Additional considerations should be given to the fact that inflation and energy price forecasts have possibly peaked early in 2017, resulting in the U.S. consumer having less disposable income. Spending may consequently pause, causing headwinds to the sector and the overall economy. The relatively slow growth environment continued in the first quarter, maintaining the trend towards businesses employing alternative means to grow. M&A activity remained high in all sectors with an increase in stock buybacks also notably elevated. One additional observation was the higher than normal incidence of divestitures, with General Motors spinning off European operations and Johnson Controls splitting up operations, highlighting two.

It should come as no surprise that after eight years into a bull market rally, rich stock valuations have left far more companies overvalued than undervalued, continuing along the path of getting further rich by the end of the quarter. Technology and Health Care were the best performing equity sectors in Q1, returning 12.4% and 10.8%. The worst performing equity sector return was in Equity Energy dropping -5.9% respectively. In fixed income, the U.S. Aggregate Bond index rose 0.8%, while the 10-year Treasury bond yield remained close to unchanged, dropping from 2.45% at the start of the year to 2.40% at the quarter's end. The S&P 500, Dow Jones Industrial Average and NASDAQ Composite Index returned 5.5%, 4.6% and 9.8% in the first quarter respectively. The most overvalued sector was again Basic Materials, trading at approximately 1.44 price/fair value of Morningstar's coverage universe. Healthcare also remained the most undervalued at 0.98 respectively with the overall price/fair value of covered stocks being 1.06[1]. We are recommending patience for new and current clients as we navigate fully valued markets. We are currently recommending wide moat companies while we wait for the market to take a breather and possible small step back. They represent companies with sustainable earnings power and the ability to survive market shocks.

We appreciate the trust you have instilled in us as we navigate the financial markets throughout 2017. We look forward to continually earning your business, growing and protecting your investments and earning your referrals in the quarters and years ahead.

Jack A. Kennedy
Chief Investment Officer

[1] Results referenced from Morningstar.com

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