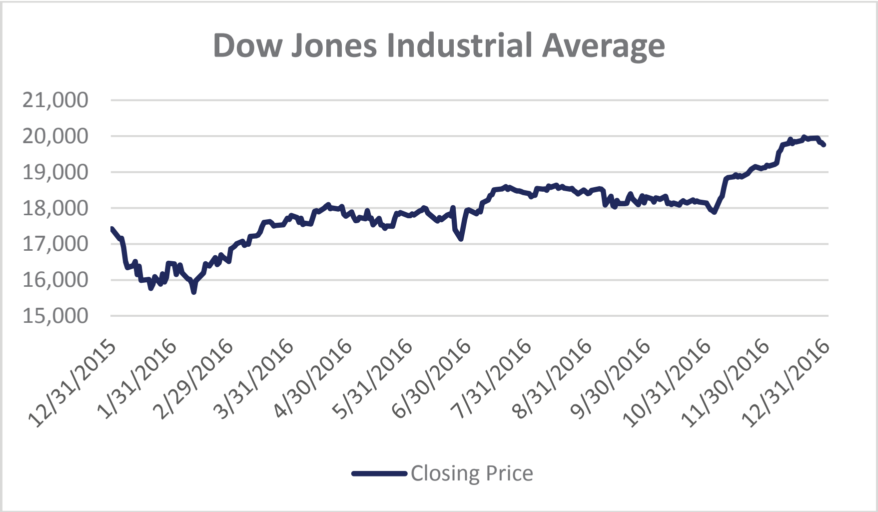
JANUARY 2017 COMMENTARY

2016 was an eventful year for the markets! The Dow Jones Industrial Average ("Dow") opened 2016 at 17,405.48, declined to 15,660.18 on February 11th, only to rally 26.2% from there, to close the year at 19,762.60. The global markets dealt with large swings in the price of Crude Oil (which bottomed out at $26.21 per barrel in February but more than doubled to $53.77 by year-end). The markets also faced Brexit, a surprising U.S. election result and the U.S. Federal Reserve ("Fed") finally hiking interest rates in December. Despite these perceived headwinds U.S. market indices closed 2016 near all-time highs.



The economy performed quite well in 2016. Auto sales set another record and unemployment fell from 4.9% to 4.7%. Further, retail sales were healthy and all signs point to this trend continuing in 2017. Wage growth is finally showing signs of accelerating.

Moving past 2016 and looking towards 2017, we expect the U.S. economy to gain strength even without an overly accommodative Fed. With the Trump presidency and Republican control of both the House and Senate, it is likely that we will see a significant amount of legislation designed to increase economic growth. While there is still much uncertainty regarding the specific framework for this legislation, we expect these policies to be a net positive to U.S. economic growth. Specifically, we believe there is a very high probability that we will see the most significant revamp of the tax code since the

Reagan presidency. While the actual details of the various legislation will be of critical importance, Consumer Confidence and Small Business Optimism readings have reached levels not seen since before the Financial Crisis of 2008-2009.
Our biggest concern has more to do with the current valuation of the stock market than the state of the overall economy. Looking at trailing earnings over the last year, the S&P 500 is trading at a level most would historically consider expensive. Analysts predict above average earnings growth for 2017, and if their expectations are correct, then the current valuation of the market is much more reasonable. We are optimistic that earnings growth will accelerate, but are a little concerned that it will not be at the rate currently anticipated by the analysts.

We fully expect the Fed to hike rates again in 2017. How many times remains to be seen, as the 2017 voting members of the Fed are considered dovish. The Fed will likely continue to exercise patience and be "data dependent", but all else being equal, rate hikes are generally done to manage inflation in response to strong economic growth.

Even though we expect the Fed to raise interest rates, we do not see a bear market in bonds. In other developed markets, such as Japan and Europe, we anticipate that central banks will remain very accommodative. 30-year German and Japanese Government Bonds were yielding 0.94% and 0.72% respectively on December 30, 2016. Those yields make a 30-year U.S. Treasury Bond yielding 3.07% (as of December 30, 2016) look very attractive.

No matter whether you were happy or disappointed with the results of the 2016 election, we expect many legislative and regulatory changes to take place in 2017. We will closely monitor the changes as they are proposed and make their way through the political process, paying special attention to how they may impact your investments.

Sincerely,

Robert Dan Rachael

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Data Source: Bloomberg LP