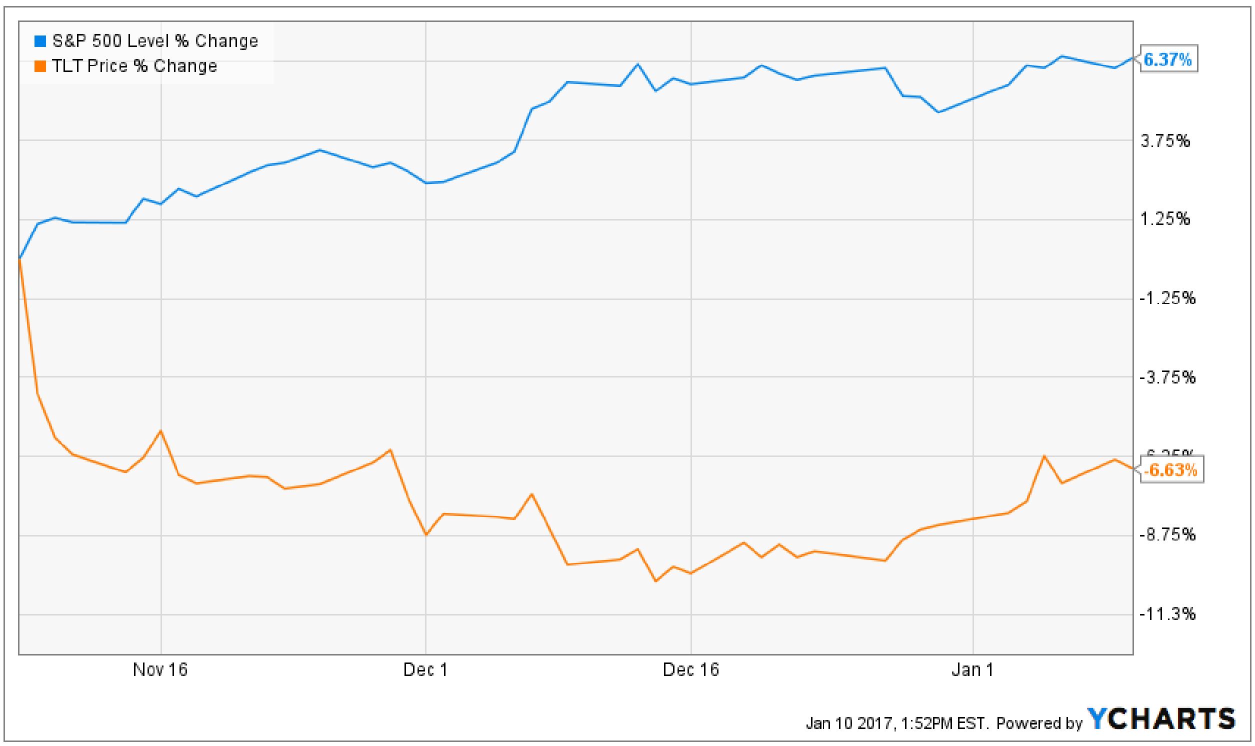
Market Update

January 10, 2017

Are Bond Prices Stabilizing As DOW Nears 20,000?

On December 15 2016, the Ten Year Treasury rate hit a recent peak of 2.61%. The TLT, a proxy for long term U.S. Treasury bonds, hit its recent price low of $116.80 one day earlier on December 14 2016. The importance of this is that bond yields move inversely to bond prices. This indicates that around the middle of December shortly after the Federal Reserve raised Federal Funds interest rates by 0.25% the bond market hit a near term price low and interest rate high. Since then, as I am writing this update, the Ten Year Treasury yield has moved back down settling between 2.34% and 2.39%. The TLT has recovered in price to above $121.00. Since the election and through January 9, 2017, the equities markets have rallied 6.37%, as indicated by the blue line for the S&P 500 in the chart below. Longer term bonds have fallen 6.63%, as indicated by the orange line for TLT in the chart below.



Information in this chart above was taken from sources we believe to be reliable; however we do not guarantee its accuracy or completeness.

So far in 2017 the S&P500 is up 0.49% through January 9th and the price of TLT has gone up 1.83%. In the chart above you can see from January 1st the orange and blue lines on the graph are both moving upward in the same direction.

In my last Market Update on December 9th, I mentioned that I believed that the move to lower bond prices would abate a bit and start to stabilize, as the majority of the repricing of bonds and interest rates

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seemed to have already occurred. This has happened in the short term and even some price recovery for bonds has occurred. We do still anticipate a rising interest rate environment going forward. The speed at which this will occur will certainly have to do with the Federal Reserve's timing and decisions on future interest rate increases. These are predicated on various economic data points. Inflation certainly will play a big role in investor's decisions to buy and sell bonds which will affect bond yields. Also, one of the Federal Reserve's mandates is to help manage inflation with monetary policy. Run-away inflation is a scenario we do not see happening. It would however cause concern for the economy and both equity and bond markets should it happen.

DOW 20,000 seems to be the sticking point, at the moment, after the recent upward move in equities. Many professional money managers and traders will tell you that DOW 20,000 in and of itself is nothing more than a number. It is a nice round number that is easily tied to a milestone and some investor psychology, but does not predict a specific top in the market or a continuation of the rally. More important to pay attention to is the current earnings releases this quarter, which are starting to come out, and the forecasts and comments from the companies themselves. This will give us insight into what the future of the U.S. economy might look like as CEO's provide information on their future business investment decisions. We feel that for at least the next 6 months to 1 year companies will look to invest more in new projects requiring the need for goods and services to support these investments. One concern that is important to mention is that a trade war could potentially have a negative longer term impact on the economy and prices. This requires trade negotiations that enhance our national interests but do not encourage a path of isolation in a global economic sense.

Overall, we still prefer domestic equities over international equites in the next 6 to 12 month period of time. However, Global equity exposure is still important to maintain. We will continuously monitor the U.S. and Global economic environment for signs that indicate a reason to be more favorable toward International Equities. Maintaining a low duration/shorter maturity outlook for bonds and fixed income is our view for the foreseeable future. Based on the current environment we feel it is prudent to maintain the lowest duration and shortest maturities possible specific to investor's individual needs.

If you have questions or would like to discuss this further with regard to your personal portfolio please contact me at 310-433-5378.

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