ROOF ADVISORY GROUP, INC.®
INVESTMENT ADVISORY & FINANCIAL PLANNING SERVICES

INVESTMENT INSIGHT
1st Quarter Review 2017

Good Quarter All Around

Market Update

Equity markets extended their post-election rally in the first quarter of 2017. The S&P 500 Index advanced by an impressive 5.5% while registering a record streak of 109 trading sessions without a 1% daily decline. International and global stocks posted even stronger results than U.S. markets with the MSCI EAFE Index higher by 6.5% and the MSCI All-Country World Index returning 6.8%.

After a poor showing in the final quarter of 2016, bonds posted modestly positive returns this quarter with the U.S. Barclays Aggregate Bond Index advancing by 0.8%. The bond market showed some signs of skepticism over the potential for above-trend growth rates as the spike in interest rates that occurred in the fourth quarter fizzled out.

Economic Update

Economic data was supportive of the move higher in equity markets and other risk assets with the majority of the incoming data pointing to a strengthening economy. The employment picture continued to improve with monthly job gains averaging well over 200,000 and initial jobless claims falling to new post-1973 lows. Workers seem to be gaining confidence in their opportunities to improve their employment situations as the voluntary quits rate rose to the highest level in 16 years.

Outside of the positive employment picture, there were a number of additional encouraging economic data points. Small business optimism and consumer confidence surveys surged to levels not seen in the past 15 years. First quarter corporate earnings are projected to grow at the fastest pace since the final quarter of 2011. And we have seen a measurable pickup in economic activity outside of the U.S., with Europe, Japan and China showing a notable improvement in economic data.

Another noteworthy development on the economic front was the Federal Reserve's decision in March to raise interest rates for the third time in 15 months. This move was well telegraphed and financial markets interpreted the interest rate hike as a sign of the Federal Reserve's confidence in our economy.

Portfolio Positioning

We maintained a neutral or mid-point equity allocation for the duration of the first quarter. The most significant portfolio shifts this quarter occurred within our fixed income allocation. We increased our allocation to one of our higher-yielding, opportunistic focused strategies which has produced an outstanding long-term performance track record. Some incremental exposure was also added to floating-rate Preferred Stocks. This is an asset class where we continue to maintain a positive view due to the high level of income and limited sensitivity to the negative impacts associated with rising interest rates.

Performance Attribution

Similar to the final quarter of 2016, we are very pleased with performance results for the first quarter of 2017. While we maintained a mid-point equity weighting, this quarter's performance results were generally comparable to a significantly more aggressive portfolio allocation. Or more simply stated a lot of our portfolio strategies worked really well for us this quarter. Fixed income performance was strong on a relative basis with the vast majority of our strategies posting measurably higher returns than the broad bond market index. On the equity side of portfolios, performance was benefited by a number of factors – including – a meaningful allocation to the technology and healthcare sectors, solid outperformance from growth oriented stocks, exposure to international equities and a handful of individual stocks that performed exceedingly well.

Performance detractors were few and far between this quarter. After a year of substantial outperformance in 2016, domestic large-cap value stocks trailed the broader equity market in the first quarter. Underperformance in this segment of portfolios had a negligible impact on overall quarterly portfolio returns and was overwhelmingly offset by the positive contributors outlined above.

Closing Thoughts

Our views and corresponding portfolio positioning has not changed drastically from our last quarterly update. We recognize and are encouraged by the recent economic and fundamental data that has been skewed to the positive. However, we also recognize that stocks (as measured by the S&P 500 Index) are up roughly 10% since the Presidential election and a whopping 30% from the market bottom in February of last year. This steep upward ascent has resulted in rich equity valuations and in our view is a good reason for a somewhat cautious stance going forward.

We have discussed the dramatic and impressive improvement in sentiment and confidence levels among consumers, small businesses and corporate executives. This is certainly a step in the right direction. However, we have yet to see consumers and businesses really put their money where their mouth is. So far we haven't seen the surge in consumer spending, capital expenditures, industrial production, or GDP growth that one would expect given the parabolic move higher in confidence levels. It may be coming but we would like to see more evidence before taking a more aggressive stance in portfolios.

Many would agree that this increased optimism is at least in part driven by expectations for the new administration's agenda. Here we fully recognize the potential positive impacts from tax cuts, an aggressive infrastructure spending plan, the ability to repatriate corporate profits and deregulation. However, we are very aware that the final product may look much different than these lofty aspirations. We witnessed a prime example of how complicated and difficult it can be to actually enact policy changes with the healthcare reform attempt in March. We remain focused on assessing the potential outcomes and impacts of these agenda initiatives. But our view that a mostly positive outcome is already priced into equity market valuations is also a solid reason for avoiding an excess amount of risk in portfolios.

We welcome all Roof Advisory Group clients to attend our interactive online webinar discussion scheduled for 1:00 pm EDT on Thursday April 13th. The purpose of this webinar is to provide a more in-depth overview of the most recent quarter, financial market conditions, portfolio positioning, as well as our firm's outlook going forward. Invitations to register for the webinar are currently being emailed to our valued clients.