MURRAY
INVESTMENT MANAGEMENT

4th Quarter 2016 Update

Economic Review

The U.S. economy continued to grow modestly during 2016 with 4th quarter growth expected to be around 2.9%. During the quarter and for the year, the U.S. economy expanded but at a pace below our long-term potential as it has for most of the current expansion.

The employment situation continued to be a bright spot for the economy with an average of 180,000 new jobs created each month during the year and the unemployment rate falling to 4.7% from 5% at the end of 2015. Overall, job creation has been strong for the last several years and has significantly contributed to the growth of the economy.

For the first time in 12 months, the U.S. Federal Reserve raised interest rates .25% to a range of .50% - .75% in December. The Fed raising rates is a good sign as it indicates that the overall economic environment is improving.

Equity Market Performance

	QTD	YTD
S&P 500	3.82%	11.96%
MSCI EAFE (International index net return)	-0.71%	1.00%
Rusell 2000 (small cap)	8.83%	21.31%

Equity markets rallied strongly after the U.S. Presidential election, and the S&P 500 finished the year up 11.96%. The S&P 500 index (domestic equities) has performed extremely well over the last 5 years and has solidly outperformed the broad international space for the 1, 3 and 5 year periods. For 2016, the S&P 500 outperformed the broad international index by almost 11%. These performance trends tend to go in cycles, and it would not be surprising to see the international space outperform domestic at some point in the future.

Bond Market Performance

	QTD	YTD
Barclays US Aggregate Bond (Broad Bond Market)	-2.98%	2.65%
Barclays Municipal	-3.62%	0.25%
Barclays US Treasury Long	-11.67%	1.33%
Barclays US Corporate	-2.83%	6.11%
Barclays US Corporate High Yield	1.75%	17.13%

With the 10 year Treasury rising from 1.60% to 2.45% during the quarter, the fixed income space had a tough 4th quarter but generally finished the year in positive territory. Longer maturity securities can perform poorly in a rising rate environment, and we experienced that in 2016 with long Treasuries down over 11% in the 4th quarter.

Economic Outlook

Regardless of what anyone thinks about President elect Trump, it cannot be denied that he has made it clear that he intends to have a pro-business administration. Lower taxes (both personal and corporate), increased federal spending and a reduced regulatory environment are all part of the new administration's plan and should serve as a favorable backdrop for an improving economy. The expectation is that these policies will lead to a significant increase in business confidence, capital expenditures and hiring, all of which could lead to accelerated GDP growth.

Executing these new policies will be easier said than done, and the degree to which the new plan can be implemented will be critical. The major question that will be resolved over the next several years is whether or not these new policies are successful and serve to stimulate the U.S. out of its low growth environment or whether the implementation of the policies gets derailed in Washington.

A stronger dollar, rising interest rates and higher oil prices will weigh against this positive backdrop, but overall, the good should outweigh the bad and produce a better economy in 2017.

Market Outlook

Domestic equity market valuations are trading at multiples that are on the higher end of their long term averages, so we will likely need solid earnings growth to drive markets higher during 2017. The good news is that, with an improving economy and potentially lower taxes, forecasting a good earnings year is a reasonable expectation, and we could see a strong earnings cycle that drives equity markets higher. We should, however, expect it to be a bumpy (volatile) ride in the equity markets throughout the year.

Interest rates remain low, but the Fed is expected to raise rates 3 times this year. As such, the risk / reward profile for many fixed income securities is not very favorable with very few attractive options. If rates increase as expected, this view could change, and portfolios would be adjusted accordingly. Currently, holding a larger level of cash and shorter term securities in the fixed income allocation seems to be a reasonable approach.

Murray Investment Management

If you would like help with establishing an investment plan or would like to schedule a portfolio review, please give us a call. Also, please pass along our name to anyone that may be in need of investment advice.

Source: bls.gov, federalreserve.gov, frbatlanta.org, Morningstar, Bloomberg, The Wall Street Journal and treasury.gov
The performance data shown represents past performance, which is not a guarantee of future results.
Return data is as of 12/31/2016. Except as noted, index returns are total returns.

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