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market update

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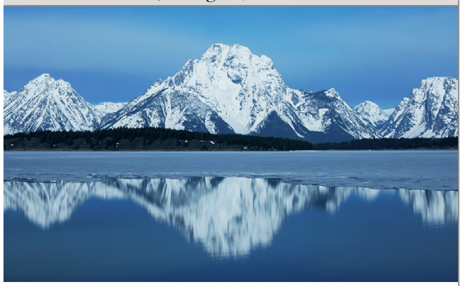
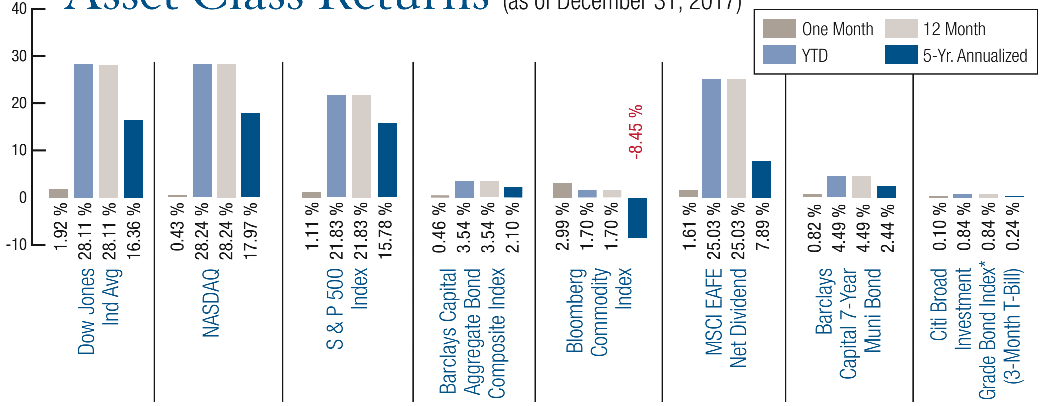
From the Office of:
Jeff Sgroi, CFP®



"The way to get started is to quit talking and begin doing."

-Walt Disney

Asset Class Returns (as of December 31, 2017)



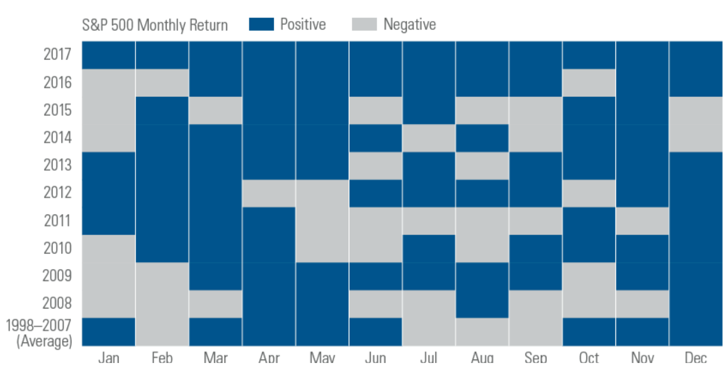
Material prepared by Raymond James for use by its Financial Advisors

Market/Economic Synopsis

- The S&P 500 experiences unprecedented rally in 2017, rising in every single month of the year.
- Fixed income yields end 2017 generally flat.
- The U.S. Dollar Index drops nearly 9.8% in 2017 – its biggest annual slide in nearly 15 years.
- January 19th marks another deadline for federal budget wrangling in order to avoid government shutdown.
- Bitcoin and other cryptocurrencies grab headlines toward year end as values run up at parabolic rate.
- Tax reform bill signed into law December 22nd set to lower highest corporate rate to 21% and highest personal income tax rates to 37%.
- Massive cold front puts East Coast into deep freeze.
- Federal Reserve expected to continue gradual rate hikes through 2018, matching 2017 rate change trajectory.
- Oil ends 2017 priced at $60.12 a barrel, up +12% from its 2016 close of $53.72 – closing above $60 a barrel for the first time since 6/24/15.

2017 - The Year in Recap

Looking back at last year's market activity is important for historical context, and helps us learn from victories and mistakes. The chart below provides a simple summary of the year, and, in a word, says it all – unbelievable. Looking back over the past 10 years, we have enjoyed a generally strong stock market in the United States, specifically since March 2009.



Source: GSAM. As of December 29, 2017.
*Based on S&P 500 Index from January 1998 through December 2007. **Past performance does not guarantee future results, which may vary.**

2017 was special in that every month of the year the S&P 500 had a positive return. As the chart indicates, this has been the only year in the past least 10 years where this has occurred.

The way in which this happened was due to exceptionally low volatility. The CBOE Volatility Index finished 2017 below 11, and earlier in the year dipped below 10 (lower VIX figures indicate lower volatility). If history is prelude, I expect healthy performance in 2018, but do not expect a repeat from a consistency and volatility standpoint.

2017 Tax Reform – Key Components that May Affect You

Much has been made of the recent tax bill passed in Washington, and for good reason. With the last major federal tax legislation not having passed since President Reagan's second term, and challenges in passing any sort of legislation recently, many see the new tax laws as a victory for most Americans. Changes are scheduled to go into effect in the 2018 tax year.

On the personal income tax side, most taxpayers will be affected by adjustments to both tax brackets and rates. Broadly speaking, both single filers and those married filing joint returns will enjoy a lower tax rate, as well as income brackets that have bumped higher.

Although personal exemptions will be eliminated, standard deduction levels are approximately double the 2017 levels beginning in the 2018 tax year. This is in line with a goal to simplify the tax code, and correspondingly, tax returns. By doubling standard deduction levels, the expectation is that many tax filers will no longer itemize deductions.

For higher net worth individuals, there are a number of noteworthy changes. Estate tax exemption limits will be doubled, to $11.2M for individuals in 2018, indexed for inflation. Additionally, the alternative minimum tax exemption phase-out threshold has been raised to $1MM for joint filers, meaning many subject to the AMT in years prior will likely be no longer be subject to it.

Much has been made of the State and Local Tax (SALT) deductions, primarily in high tax regions of the country. In 2017 (and years prior), tax filers were permitted to deduct taxes paid to state and local governments, including property taxes. The new tax law caps state, local, property and sales tax deductions at $10,000.

On a corporate level, top rates will drop from 35% to 21%. This will help company bottom lines, which, of course, is impactful for investors. Moving to a territorial tax system is also a key part of the corporate tax reform, creating a more "level playing field" for multinational, U.S.-based companies. Reduced rates on repatriated corporate earnings should bring financial assets back into the United States, with the administration expecting those dollars to fund capital expenditures and workforce expansion. Critics claim that money will go back into share buybacks and dividends; where executives choose to spend remains to be seen.

Capital expenditures will be immediately 100% deductible for the next five years, rather than on a depreciation schedule.

All in all, the tax reform will likely lower federal revenues. Republicans expect economic expansion to fill the deficit gap. Democrats claim this thinking is flawed economics. In either case, taxpaying Americans will likely see more money in proverbial pockets. Investors are likely to see better earnings reports. Much of the stock market rally we saw at year end was due to the expectation of this tax bill passing, which as investors, we have all benefited from.

2018 Market Outlook

One of my favorite market perspectives is the first quarterly report of the year published by the Raymond James Investment Strategy Committee. It includes a variety of different views – coming from economists, equity and fixed income analysts, sector specific analysts, and others.

A few highlights I found pertinent in the most recent issue are part of the committee's recap section. The comments below are talking points we are taking into consideration when adjusting client asset allocations, setting investment strategies and rebalancing portfolios. Thankfully, because this report is published on a quarterly basis, we continue to receive timely updates throughout the year.

U.S. Economy – Scott Brown, Ph.D., Chief Economist, Equity Research

- "The leadership transition at the Fed should be smooth, but the monetary policy outlook is more clouded beyond the middle of the year, just as the risks of a policy error start to mount; personnel changes are expected to lead to a lighter regulatory outlook."

U.S. Equity – Andrew Adams, CFA, CMT, Senior Research Associate, Equity Research

- "The bigger story last year was the limited amount of downside, and 2017 is right up there with 1995 as the year with the lowest drawdown. We've gone about 400 calendar days now without a 3% dip in the S&P 500 on a closing basis. That's an all-time record so we are literally in unprecedented territory."
- "Next year is going to be more volatile, and we're going to see more downside than this year. That's about the only guarantee I can give."

U.S. Equity – Michael Gibbs, Managing Director, Equity Portfolio & Technical Strategy

- "Our bullish tone remains intact, given the normal pullbacks that are likely to develop at some point. The general markets remain strong with firm pillars of support in place."
- "If you look at the pillars of support, and if you back that up with technical support, you can't come up with any case where this market is going to roll over any time soon."

International Equity – Chris Bailey, European Strategist, Raymond James Euro Equities

- "When I look at 2018, it's actually all about reform and change: tax reform, labor market reform, and economic change."

U.S Fixed Income – James Camp, CFA, Managing Director of Fixed Income, Eagle Asset Management

- "The curve is telling you something. It's telling you investors are not scared. Financial conditions, more broadly measured—forget just global interest rates—are as loose as they've been since 2008. This is not a tight market. And that absolutely has major effects on risk asset allocation. Central banks have modified corporate behavior and they've modified investor behavior. And to suggest otherwise, I think, is wrong."

If you would like to see the full 36 page document, it is available on my website (www.raymondjames.com/sgroi) under the Resources tab; filter for 2018, and it is the link titled "2018 Outlook: Unprecedented Territory". Our office is also happy to send you a printed version or email a copy to you upon request.

My takeaway from these comments is one of optimism heading into the New Year. We finished 2017 on a very strong note. Markets tend to follow momentum, and flipping the calendar is not, in my opinion, a momentum disrupter. As always, we will continue to assess market conditions specific to your objectives and risk tolerance. If you would like to discuss any of these opinions, and how they affect your portfolio, we welcome your call. Happy New Year and best wishes for a healthy, prosperous 2018.

If you prefer to receive this newsletter via email, please notify us at jeff.sgroi@raymondjames.com.

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