POST OAK PRIVATE WEALTH ADVISORS

ADVISORY, CONSULTING & INVESTMENT MANAGEMENT

Monthly Economic & Market Update

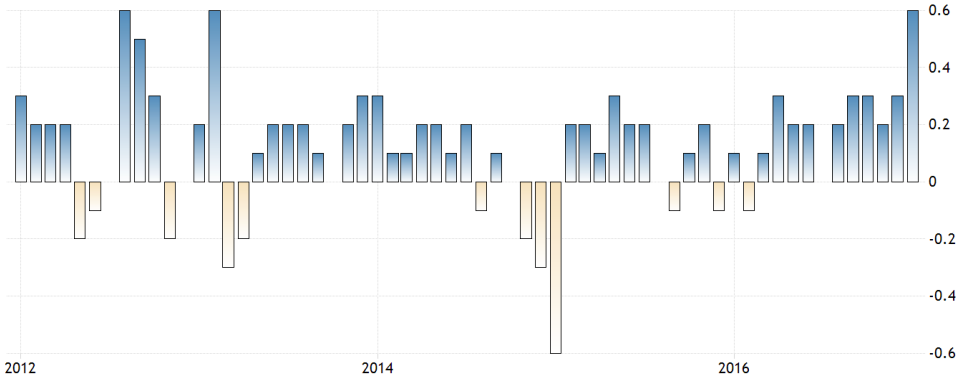
February 2017

U.S. stocks pushed higher into record territory in February as the Trump/reflation rally continued. With the economy showing signs of gathering strength, the possibility of a Fed rate hike and higher interest rates became more likely.

The Economy:

January's inflation report may not have come as a surprise—inflationary pressures have been building in recent months—but the annual rise of 2.5% was sharp enough to make headlines in February. The monthly jump of 0.6% in January was the largest increase in consumer prices in four years. (See chart below.) Even the annual core inflation rate, which excludes volatile food and energy prices, came in at 2.3% in January, at the top end of its recent range. Consumer spending has remained strong despite the pickup in inflation, and was a leading factor in the 1.9% annual growth rate for the U.S. economy in Q4 of 2016. That still represents a sluggish pace of growth. For the 2016 calendar year, the U.S. economy expanded at a 1.6% rate, the slowest annual rate since 2011.

Chart 1: U.S. Inflation Rate, monthly change. Jan. 2012-Jan. 2017



SOURCE: WWW.TRADINGECONOMICS.COM | U.S. BUREAU OF LABOR STATISTICS

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Equities:

U.S. stock markets continued to set new records on a daily basis throughout February. Most notable was the 12-day run of record-setting days by the Dow Jones Industrial Average (Feb. 9-27). Much of the ongoing rally has been fueled by continued investor optimism for President Trump's tax reform and economic growth proposals, even though the details of these plans remain vague and fluid as they are discussed in Washington. For the month, the S&P 500 Index gained nearly 4%, while small-cap stocks lagged with a 1.6% monthly return as measured by the S&P SmallCap 600 Index. Among industry sectors, health care led the way as investors saw potential regulatory changes to the Affordable Care Act and the FDA benefiting the industry as a whole. Energy stocks mostly languished as oil prices remained bound within their trading range for the month.

Sector Performance:

Ranked by previous month total return best to worst

Health Care	6.4%	A good month for pharma stocks with the possibility of FDA reform on Trump's agenda
Utilities	5.3%	With interest rates stalled, yield-seeking investors returned to electricity producers
Financials	5.2%	The outlook brightened for banks with the potential rollback of Dodd/Frank regulations
Technology	5.1%	Strength of hardware manufacturers drove good monthly performance
Consumer Staples	4.9%	"Sin" products (tobacco, alcohol) among better performers; food retailers lagged
Real Estate	4.7%	Strong month for residential and health care REITs, although flat for retail REITs
Industrials	3.8%	Hopes of higher military spending sparked a rally in defense and aerospace firms
Consumer Discretionary	1.9%	Another good month for internet retailers, but cable and entertainment firms struggled
Materials	0.7%	Weakness in precious metals offset gains by chemical producers
Telecom	–0.4%	Weak performance over the last 12 months continues
Energy	–2.2%	Lack of upward trend in oil prices hurt energy stocks

Source for equity sector total return data: S&P Dow Jones Indices, Index Dashboard: U.S., February 28, 2017

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Bonds:

Yields on the 10-year Treasury note were down slightly for the month, closing at 2.39% on February 28. The government bond market treaded water as investors waited for signals on the direction the Trump White House or the Republican Congress would take with their legislative agenda. In the absence of any firm plans from the administration, bond investors took their cues from the Federal Reserve. The Fed seems committed to their stated intention of three rate hikes this year, with the first hike likely to come by June. But as the month ended, the likelihood increased that rates would rise at the next Fed meeting in March. Beyond the government debt markets, high-yield corporate bonds were the best performers, rising 1.35% for the month. Investment-grade corporate bonds rose 1.0% for the period.

The Month Ahead:

President Trump's address to Congress on February 28 may buoy investor optimism for the future, but it gave the market little in the way of the details they were seeking about possible reforms. This optimism may help the current bull market for U.S. stocks roll on, even as it crosses its 8th birthday in March. Only the dot-com era bull market of the 1990s lasted longer. But as stock values continue to rise, concerns about over-valuation will grow as well. As March begins, the market's attention will likely focus on the next Fed meeting on the 15th. Recent public statements from Federal Reserve regional presidents have made a quarter-point hike in March more probable. Much will depend on the upcoming economic reports on jobs, wages, inflation and Gross Domestic Product to solidify the Fed's position.

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