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Fourth-Quarter 2016 Market Review

Party Like It's 1999!

January 2017 - Stocks partied like it was 1999 in 2016, as the three widely-followed market bellwethers advanced to record levels on the same day in August and repeatedly in a post-election bounce, the first time since 1999. Between November 9th and year end, the Dow Jones Industrial Average jumped 7.8%, the Standard & Poor's 500-Stock index (total return) rose 5.0%, and the NASDAQ Composite index added 3.7%. The prospect for higher corporate profits from the trifecta of lower corporate taxes, infrastructure spending, and deregulation propelled stocks to record highs. For all of 2016, the three market barometers climbed 13.4%, 12.0%, and 7.5%, respectively.



With the potential for less regulation having a more positive effect on smaller-company profits, small cap stocks surged. The Russell 2000 index vaulted 13.6% between election day and year end, and soared 21.3% for all of 2016. Large and mid caps posted low double-digit returns for the year. Commodity stocks nearly erased 2015's sell-off of 27.0% with a rebound of 25.3%.

International stock indices all lost ground in the fourth quarter as interest rates shot up and the U.S. dollar strengthened. Nevertheless, Emerging Markets put in a solid year, picking up 11.6%, while developed international markets provided low single-digit returns.

Post-election bond yields leapt on the expectation for stimulative and inflationary fiscal policies. The 10-year Treasury note yield essentially made a round trip during 2016: beginning the year at 2.27%; dipping to a record low of 1.36% in July in the wake of the Brexit vote; and closing the year at 2.44% (up 84 basis points from 1.60% for the fourth quarter). Since election day, the yields on 10-year Treasury bonds and 30-year fixed-rate mortgages have expanded by more than one-half percent.

With higher interest rates, all fixed-income sectors declined in the fourth quarter, except for U.S. Corporate High Yield, which moved ahead by 1.8% on the prospects for economic stimulus and improved corporate profits. Nevertheless, all major bond sectors gained in 2016, with high yield swelling 17.5%.

As expected, the Federal Reserve hiked its target interest rate by a quarter percent to a range of 0.50% to 0.75% from a range of 0.25% to 0.50%. It was the first time in a year and only the second time in 10 years that the central bank lifted its short-term benchmark. The Fed expects the economy to expand by 1.9% in 2016 and 2.1% in 2017, leading to a forecast of three interest rate increases to a benchmark target of 1.4% by the start of 2018.



Below are rates of return for selected market indices for the fourth quarter of 2016, full-year 2016, and the three, five, and 10-year compound annual returns as of December 31, 2016.

	<u>4Q:2016</u>	<u>2016</u>	<u>3-Year</u>	<u>5-Year</u>	<u>10-Year</u>
<u>Equity (Stock) Indices</u>					
Domestic					
Russell 1000 - Large Cap	3.83%	12.05%	8.59%	14.69%	7.08%
Russell Midcap	3.21%	13.80%	7.92%	14.72%	7.86%
Russell 2000 - Small Cap	8.83%	21.31%	6.74%	14.46%	7.07%
Real Estate (FTSE NAREIT Equity REITs)	-2.89%	8.52%	13.38%	12.01%	5.08%
Commodity (Dow Jones Global Equity 100)	3.13%	25.28%	-7.17%	-4.07%	NA
International					
MSCI EAFE Developed Large Cap	-0.68%	1.51%	-1.15%	7.02%	1.22%
MSCI EAFE Developed Small Cap	-2.82%	2.55%	2.45%	10.92%	3.30%
MSCI Emerging Markets	-4.08%	11.60%	-2.19%	1.64%	2.17%
Global - MSCI All Country IMI	1.38%	8.96%	3.79%	10.20%	4.38%
<u>Fixed-Income (Bond) Indices</u>					
Bloomberg Barclays					
Global Aggregate - Unhedged	-7.06%	2.09%	-1.01%	1.34%	4.00%
Global Aggregate - Hedged	-2.34%	3.95%	3.97%	NA	NA
U.S. Aggregate	-2.98%	2.65%	1.45%	3.25%	4.52%
U.S. Treasury TIPs	-2.41%	4.68%	0.03%	3.99%	4.66%
U.S. Corporate High Yield	1.75%	17.13%	0.45%	4.27%	6.56%
Municipal	-3.62%	0.25%	4.16%	5.96%	5.02%
International Emerging Markets	-2.61%	9.88%	2.40%	6.26%	7.30%

Source: ftserussell.com, reit.com, djindexes.com, msci.com, barcap.com

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