knowledgeable thoughtful ethical experienced interactive

summaries

SIGMA INVESTMENT COUNSELORS

the official newsletter of sigma investment counselors December 2016

Shifting Investment Landscapes

A key takeaway from the market reaction to the election results underscores a fundamental principal of Sigma's investment philosophy: Stay the Course.

Headed into Election Day, many market pundits and advisors were encouraging investors to "go to cash" until the election was over. Not only was the advice wrong but for those that got out or stayed on the sidelines they now face a dilemma: When do they step back into the markets? Will they step in as the market continues to climb or will they wait for a market correction? And, will they have the courage to step in during a market correction? Conversely, for those that stayed the course the decisions were made well in advance of the market activity. Those investors continue to profit both in the short term and the long term as they maintain the steady path to achieving their long term goals.

For the month of November the S&P 500 stock index was up 3.7%, with the S&P small and mid sized company indices up 12.5% and 8.0% respectively. At the time of this writing, the 10-year US Treasury yield is at an 18 month high of 2.49%, up from 1.85% on election day and up a stunning 85% from this year's July low of 1.36%. Clearly investors expect the changes that accompany a Trump administration will be deep and far reaching. What does that mean for both the economy and the investing public?

It is no secret that the recovery from the depths of the 2008-2009 recession has been lackluster. Investor reaction to the election outcome focuses on a few key issues expected to result in a significant boost in the growth rate for the US economy. Specifically the expectation is for policies of the new administration to result in lower tax rates, a much less burdensome regulatory environment and significant infrastructure spending. If executed correctly, investor expectations are that these three initiatives will serve as pillars of a foundation on which economic growth will flourish. (To use our President Elect's words, it will be "UGE".)

A lower tax rate provides significant stimulus to the economy. Paying less in taxes frees up cash for companies, both large and small, to reinvest in their businesses. Reinvestment leads to increased business activity (increased production of goods and services). Second, lower tax rates place the US on a more even playing field with the tax rates of other developed nations. This makes the US more globally competitive with other countries as a place to locate businesses and factories. Third, lower individual tax rates should result in more consumer spending. Consumers represent two thirds of the US economy so an increase in consumer spending would certainly fuel economic growth.

Reinvestment is a key piece of any economic equation. A combination of high taxes and onerous regulations has created an unattractive environment for companies to reinvest in research, development and innovation for new goods and services. Instead, during the past several years, much of the excess cash flow at corporations has been used to raise dividends, buy other companies and buy back common stock. Capital will be allocated to opportunities which offer the most attractive returns. Lower tax rates should provide more attractive returns, encouraging more companies to invest in the US versus building abroad or transferring headquarters overseas.

Reducing the cost of regulation also makes the US a more attractive option for business investment. If

27777 Franklin Road • Suite 1100 • Southfield, MI 48034 • tel (248) 223-0122 • fax (248) 223-0144 • www.sigmainvestments.com

successful, this would represent a cultural shift in the way the US government agencies go about their activities and provide tremendous opportunity for business growth. Aside from the hassle of dealing with compliance issues, the cost of regulation can be merely outrageous for a large company, but cost prohibitive, for a smaller company. While regulation is necessary, the amount of time, energy and money devoted to complying with excessive government regulation creates great waste in our society.

Elimination of unnecessary regulation frees up the resources of time, energy and money to become available for more productive activities, helping to create a more vibrant and productive economy.

Finally there is infrastructure spending where opportunities seem endless as many of our roads, bridges, water and sewer systems, are in disrepair. The prospect of new projects such as high speed trains has great appeal. Infrastructure development also has the benefit of providing well paying jobs for people.

Gridlock in Washington DC has resulted in the Federal Reserve being tasked with all of the heavy lifting for economic stimulus by way of monetary easing. The icy relationship between the President and Congress as well as the discourse between the parties has led to little, if any, fiscal stimulus to help the economy. With a President and both houses of Congress of the same party, there is a much higher probability that fiscal stimulus measures will be passed. This offers a powerful opportunity for growth at much higher levels versus current levels.

As we move into 2017, the key signposts will revolve around the ability of the President and Congress to actually deliver on these objectives. Any sign of a "break in the ranks" in setting any of these initiatives into motion, particularly with regard to tax and regulatory issues, could weigh heavy on investor sentiment. In addition, many fear President-Elect Trump's policies may prove to be protectionist. We don't share this concern. However, should we see major trading partners or some of our "frenemies" begin to take actions against the US with regard to trading policies, markets will not respond kindly. Additionally, should activity on infrastructure projects not begin in a timely manner, investor sentiment will be tempered.

Overall we are optimistic that 2017 will be a strong year for the economy. However, we know it will be important to read the tea leaves carefully and in great detail as a new President and a new Congress begin their terms.

Year end always proves to be a time for reflection and hopes for the coming year. My colleagues and I at Sigma appreciate the opportunity to serve you, our clients, as their trusted advisor. It is truly our privilege and we thank you.

To all our clients and friends we wish you a very Happy Holiday Season and a wonderful New Year filled with much joy, health, happiness and prosperity.

Denise M. Farkas, CFA
Chief Investment Officer