The first quarter of 2017 was marked by a disconnect between news and action. Until March 21st, the S&P 500 had gone 104 consecutive trading days without closing down more than one percent and since the election, from November 9th, there have been only four such days where the market was either been up or down by more than once percent. This streak of remarkable dullness from investors contrasts with the equally remarkable, nee unbelievable at times, circus, out of Washington.

At first glance, the strong returns for January and February were akin to an irrational exuberance; hopes for tax reform, a strong pro-business agenda and reduced regulations across the board, buoyed stock prices. Yet, in examining the above data, it actually shows a market lulled in to complacency, more than the animal spirits run amok. Recent stumbles by the new administration in enacting health care reform and immigration policy, as well as the ongoing allegations of corruption, nepotism, party in-fighting and the never-ending tweet stream seem to have tempered expectations.

Though the return for the stock market in March was a more meager 0.12%, on the whole, the quarterly return was what one might expect at year-end, not just for the first three months. This is surprising and also disconcerting, given the current environment, as expectations and reality seem mismatched. President Trump has promised to double GDP growth, yet we find ourselves in the midst of an expansionary period that is already more than seven years old. The unemployment rate, which currently stands at 4.5%, is at its lowest level in more than ten years, almost certainly indicating an economy that is at full employment. Trump's proposed fiscal spending increases and tax cuts may have a harder time driving growth amid a tight labor market and indeed seem at loggerheads with the Fed's mandate of curbing inflation.

While inflation remains modest, the Fed has raised interest rates twice since December, with the federal funds rate target now between 0.75-1.0%. Steepening of the yield curve may be tempered somewhat by foreign demand for US debt, given the attractive spread that exists, yet nonetheless, bonds remain under pressure from the prospect of more rate hikes to come. Coupled with the continued strength of the US dollar, it could be tough sledding for domestic stocks; there is a reason the phrase "don't fight the Fed," exists.

That being said, the current economic fundamentals are healthy; the previously referenced employment numbers, together with strong PMI index readings, moderate inflation and GDP growth forecast in the 2-3% range, are all positive signs. Forecasts for corporate earnings are quite robust also, as analysts expect profits for S&P 500 companies to increase 9.4% year-over-year, the fastest such growth since 2011. Technology, energy and financials are projected to lead the way. The market has seen oil prices moderate and an uptick in M&A activity within the sector points to that industry perhaps finally turning the corner from the tumult of 2015. We will be watching earnings announcements closely, as those projected growth numbers will be important in supporting stock prices at their currently stretched levels.

The murkiness of the current environment certainly gives us pause, as the number of risks is not to be discounted. Stocks remain the best and most viable option going forward, yet we've taken steps to moderately rebalance the portfolio, taking profits in those companies where we see the risk/reward balance tilting slightly against us (General Mills, Gilead and Coca Cola). Likewise, we've looked to diversify geographically, initiating a position in a currency-hedged European ETF. The European market appears to finally have turned the corner and though headwinds remain, the outlook is promising. Likewise, by currency hedging, we are protected in a rising US dollar environment, which we expect to continue. We do anticipate making further adjustments, as we identify attractive diversification alternatives. We expect to maintain our current weighting in fixed income during the predicted rising interest rate climate; because our holdings are heavily weighted towards adjustable-rate and short-to-intermediate duration securities with reasonable yields, we are afforded some insulation from interest rate risk. We deem it prudent to proceed with caution and to be selective, waiting until the market's direction has been fully fleshed out, rather than throwing proverbial darts.

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