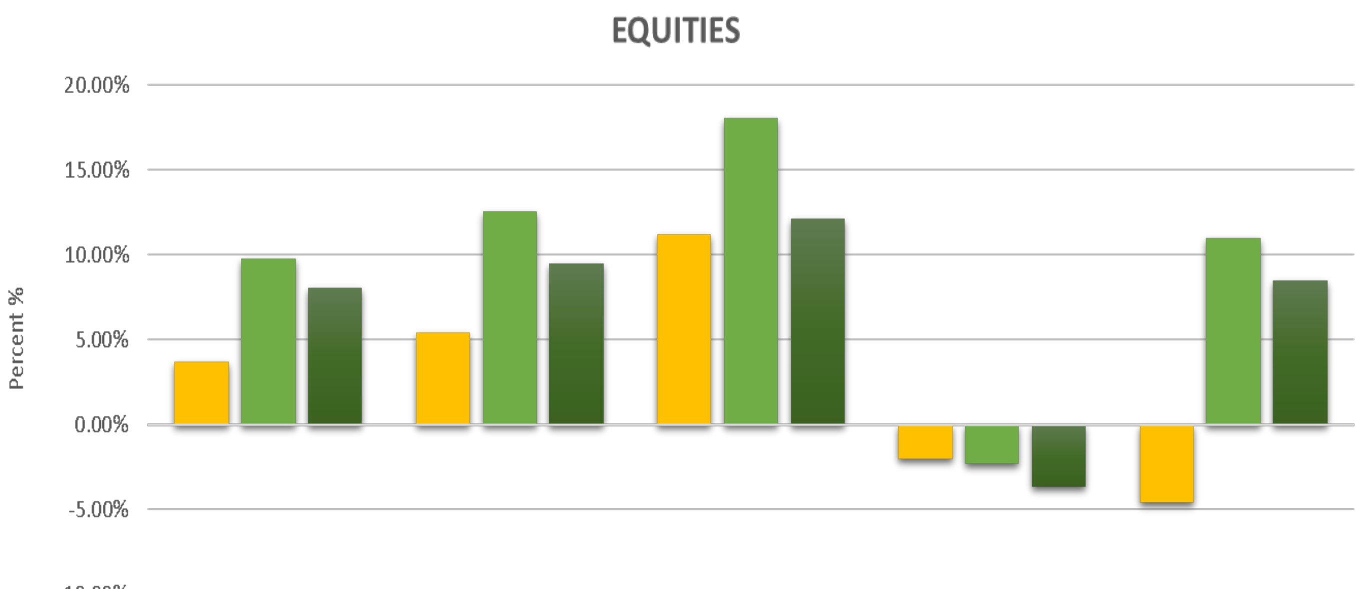
INNOVEST MONTHLY MARKET COMMENTARY

November 2016

Small Caps Trumped Up

President-elect Donald Trump wasn't the only winner this November. Despite the doom and gloom that dominated many headlines for the past year from those anxious about a Trump victory, equities have rallied so far – most likely in anticipation of pro-growth economic policies.



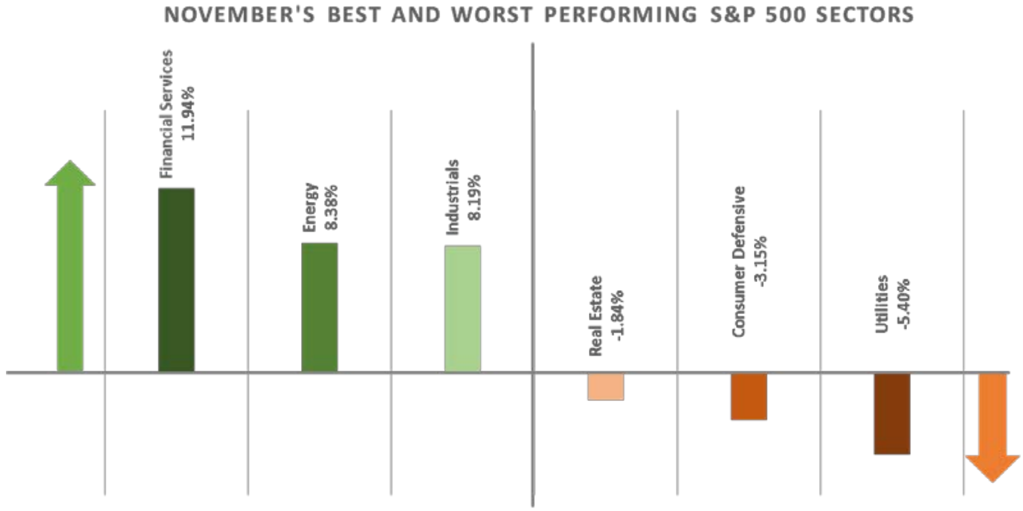
	Large Cap	Mid Cap	Small Cap	International (Dev.)	Emerging Markets
November	3.70%	5.39%	11.15%	-1.99%	-4.60%
YTD	9.79%	12.52%	18.00%	-2.34%	10.94%
1 Year	8.06%	9.50%	12.08%	-3.66%	8.47%

Benchmark Indexes: Large Cap - S&P 500; Mid Cap - Russell Mid Cap; Small Cap - Russell 2000; International (Dev.) - MSCI EAFE; Emerging Markets - MSCI

For stocks, bigger is not always better. Small cap companies bounced back, returning an impressive 11.2% in November. An increase in economic growth, as well as being more insulated from rising tariffs on trade, may benefit domestically focused small companies when compared to export-driven large US companies. That said, the recent rally in the small companies of the Russell 2000 may be merely a speculative bet, with investors chasing short-term returns. Edged out last month by the smaller companies, mid-sized companies posted a positive return of 5.4%, as measured by the Russell Midcap Index, and large companies returned 3.7%, as measured by the S&P 500. Though lower than small cap, these returns are still noteworthy considering the chaos many feared would follow a Trump victory on November 8.

If only all markets always went up. International equities seem to be viewing the election results from the glass-half-empty perspective. Emerging markets declined 4.6%, more than double developed nations' loss of 1.99%. The strong post-election rebound in the US dollar spurred an emerging markets selloff, as many countries' goods can become more expensive when the US dollar strengthens. In addition, fears of a global trade war added to the pressure on emerging markets equities.

From First to Worst



Coming off October, during which utilities were the best performing sector, they went straight to the bottom for the month of November, dropping 5.4%. On the other hand, less is more for some sectors. Expectations of reduced government regulation and a steeper yield curve spurred a rally in financial services, which returned a positive 11.9%. Following closely behind, energy returned a booming 8.4%, on the heels of an OPEC output deal at the end of November, while industrials posted a positive 8.2%. The outlook for rising inflation and interest rates certainly played a role in the weakness of the more rate-sensitive sectors of utilities and consumer defensive (-3.2%).

	Core Fixed Income	Munis	High Yield	Floating Rate	Commodities	MLPs
November	-2.37%	-2.68%	-0.47%	0.32%	1.33%	2.64%
YTD	2.50%	-0.88%	15.01%	8.63%	9.79%	13.88%
1 Year	2.17%	-0.69%	12.11%	7.60%	6.40%	11.38%

Benchmark Indexes: Domestic Fixed Income - Barclays US Agg; Municipal Bonds - Barclays 4-6 Yr Muni; High Yield - Barclays US Corp. HY; Floating Rate – CSFB Leveraged Loan Index; Commodities - Bloomberg Commodity; MLPs - Alerian MLP Infrastructure.

In the US, core fixed income was down 2.4% on the potential for rising inflation. Plus, it was even more disappointing in the global space, as the Bloomberg Barclays Global Aggregate index shed 4% this month, a total loss of $1.7 trillion and the worst month since the inception of the index in 1990. The "reflation trade" seems to indicate that many investors may be betting on the idea that Trump's policies will lift US growth and inflation. Put simply, investors are selling bonds and buying equities that would ideally benefit from an era of higher growth during a Trump administration.

Munis posted a negative 2.7% on concerns of higher inflation and less demand if income tax rates decline. High yield bonds and floating rate loans remained relatively flat during the month. MLPs were positive for November, up 2.6%, and commodities were up 1.3%. Prices in the space were affected by the November 30 OPEC decision that quickly boosted oil prices.

Deal or No Deal? Making OPEC Great Again

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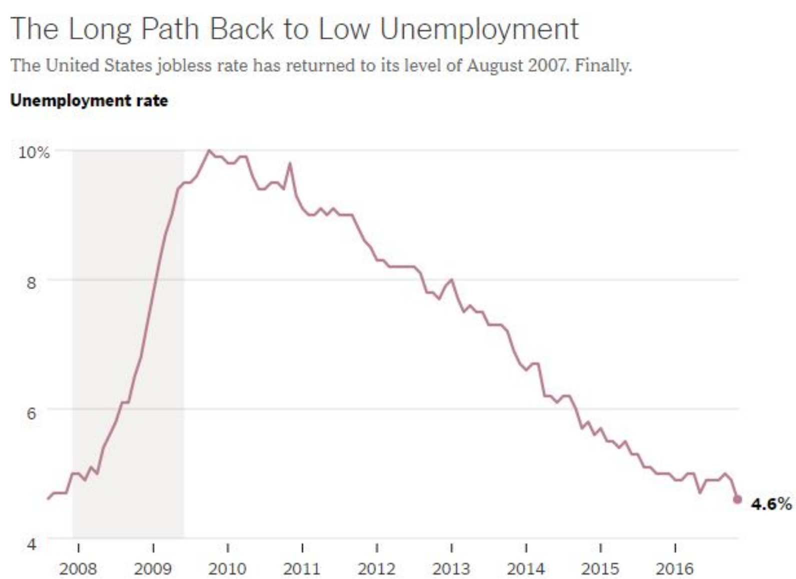
Deal! That was the result of the 171st OPEC meeting in Vienna, Austria. OPEC agreed to cut production of oil by 1.2 million barrels per day, with the expectation that Russia and other non-OPEC countries would cut production by a total of 600,000 barrels per day. While OPEC members will certainly benefit from the agreement, one individual in particular has been vocal about his opposition to the organization in the past.

In his 2015 book "Crippled America," Trump wrote: "I've never understood why, with all of our own reserves, we've allowed this country to be held hostage by OPEC, the cartel of oil-producing countries, some of which are hostile to America." Looking at the situation through the reality of a Trump administration, the political and policy response to spur an increase domestic drilling and US oil production might be the primary comeback to OPEC's price increases. Not surprisingly, crude prices skyrocketed on the news of the cartel reaching a deal to production cuts. Crude hit $49.20 per barrel, up almost 9% the day the OPEC news broke. While oil prices were clearly impacted by news of an agreement, the deal is anything but finalized and does hinge on the other non-OPEC members honoring their commitment to slash production as well.

While some analysts are relieved by the historic deal, OPEC doesn't exactly have a superb history of honoring their agreements. Oil analyst Dennis Gartman, sometimes referred to as "the commodities king," encouraged investors to exercise caution when the inter-governmental cartel makes any decision. Recently on CNBC, Gartman stated, "If I've learned anything in 40 years, it's that OPEC cheats. Every one of the members cheat…To think otherwise is naïve." With that in mind, and the fact that the oil cartel doesn't always seem to be playing by the same rules as the rest of the world, a little competition from the US may be the ideal situation for consumers to benefit from lower gas prices.

It's About Time



Source: New York Times, Bureau of Labor Statistics

Better late than never, the November jobs report indicated that the unemployment rate dropped from 4.9 to 4.6 percent, according to the Labor Department. August 2007 was the last time that unemployment sat at a rate this low, just before the subprime mortgage crisis.

The Federal Reserve forecasted a year ago that there could be four rate hikes in 2016. However, the month of December now stands alone as the last chance for the Fed to boost rates this calendar year. According to data from the futures markets, there is a 90 percent chance that the Fed will raise rates by 25 basis points on December 14. A positive jobs reports, along with the reality of potential tax reform under a new political party should give Janet Yellen and the Federal Reserve good reasons to raise rates at the final FOMC meeting. Additionally, President-elect Trump has promised spending on infrastructure during his administration, ranging anywhere from $500 billion to $1 trillion over the next decade. Trump's plan to spend on infrastructure coupled with potential tax cuts could lead to much-needed GDP growth and a strong argument for short-term rates to increase further next year.

Staying the Course

As a gross understatement, 2016 proved to be an unparalleled year for the US and the rest of the world, both politically and economically. As a volatile year full of twists and turns comes to an end, Innovest continues to recommend long-term asset allocation and a sound financial plan to guide investors through the uncertainties of the future. As always, please do not hesitate to reach out with any questions regarding the markets and your portfolio.