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After a brief and shallow pullback mid-month, stocks resumed their march higher in May to finish the month with modest gains. The S&P 500 had a 1.4% gain for the month which brought its year-to-date return to 8.7%. The small cap stocks in the Russell 2000 index failed to participate in the rally and finished the month with a -2.0% loss leaving it up only 1.5% year-to-date. International stocks in the MSCI EAFE index continued their outperformance and returned 3.7% in the month and 14.0% year-to-date. Emerging markets stocks were also strong with a 2.7% return for the month and a 17.0% year-to-date return. Yields on the ten-year US Treasury moved higher mid-month before declining to finish the month at 2.2%. Because that was still lower than where yields started the month, the Barclays Aggregate Bond Index gained 0.8% in May and had a year-to-date return of 2.4%.

The market seems to be losing confidence in President Trump's ability to implement his agenda as we've seen sectors that rallied sharply after the election give up much of their gains over the past month or two. The most obvious example of this is the financial sector that was expected to benefit from a reduced regulatory burden, higher interest rates and increase economic activity.

GDP for Q1 2017 was revised higher to 1.2% from 0.7%. That figure matched the original forecast and was welcomed news to the markets which breathed a collective sigh of relief. Much of the adjustment came from consumer spending and business investment which both were better than previously estimated; in fact, business fixed investment grew at an 11.4% annual rate in Q1, the fastest pace in 5 years. This supports evidence of a marked improvement in business optimism. In addition, inventories were revised lower. This points to improving prospects for the coming quarters.

Corporate earnings continued to grow during the first quarter. According to Earnings Insight, the blended S&P 500 earnings growth rate for the 1st quarter was 14%. This is the highest year-over-year earnings growth rate of the index since the 3rd quarter of 2011. This pattern of improving earnings growth is also finally occurring in international markets creating improving equity performance internationally.

The Federal Reserve has reiterated its plan to continue to raise interest rates gradually in 2017. They raised rates in March and are forecasting two more increases this year. Right now it looks likely the Fed will raise rates again when the FOMC meets later this month. So far this year, longer term rates have remained low despite short-term increases by the Fed. Eventually we expect the increases on short-term instruments to pressure long-term rates higher. Higher yields will benefit income oriented investors when they can derive more income from bonds rather than more volatile sources.

Even though the current bull market in stocks has run for quite some time, the trend is still intact. Bond yields should feel some upward pressure as the Fed continues to raise rates. If you have questions about your account, please do not hesitate to contact your advisor.

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