Investment Opportunities

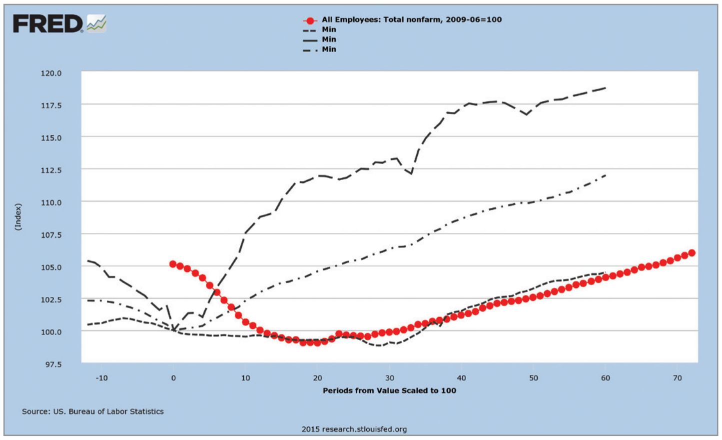
In this newsletter we present views expressed by our partners, Ken Nesler and Nick Healy. The US economy is experiencing strong but measured growth, and we expect a continued steady growth in output through 2015. This gives us a positive outlook for the US investment markets.

Economic and Market Outlook

January 2015

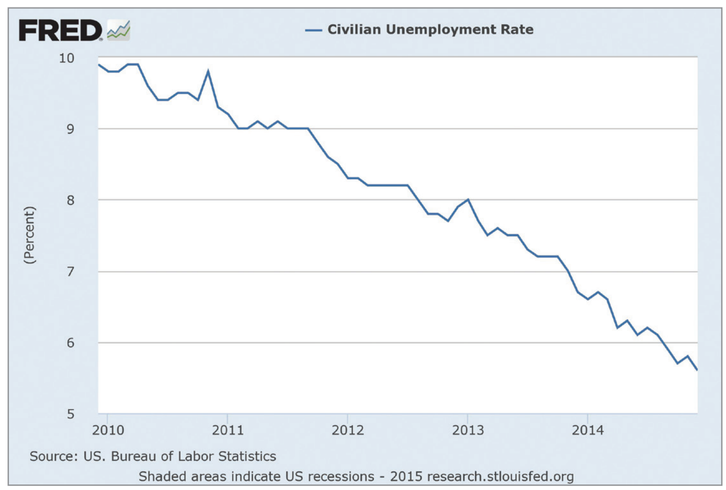
America is on top again. Following a major setback in 2008-09, the economy hasn't exactly bounced back but has steadily improved while growth rates of other countries have slowed. With a strong currency, low inflation and rising stock prices, our economy has become the place to be in 2015.

Our economy is changing, there is no doubt about that. Many jobs previously completed by workers are now done by robots. Technology has changed the landscape immensely, and with it the job skills required of American workers. As we came out of the recession, employment was slow to expand.



The above graph shows the historical recovery of US employment from previous recessions; the top line represents the best recovery, the bottom line the worst recovery, the center line the average recovery and the red line is the current recovery. As can be seen, this has been one of the worst economic recoveries for employment in history.

The US economy has experienced its recent growth primarily through a manufacturing renaissance. We have ample labor, available capacity, lower energy costs and a creative technology environment. The economy is now picking up steam and this higher activity translates to additional jobs. The unemployment rate is now at 5.8%, down from nearly 10% at the height of the recession.



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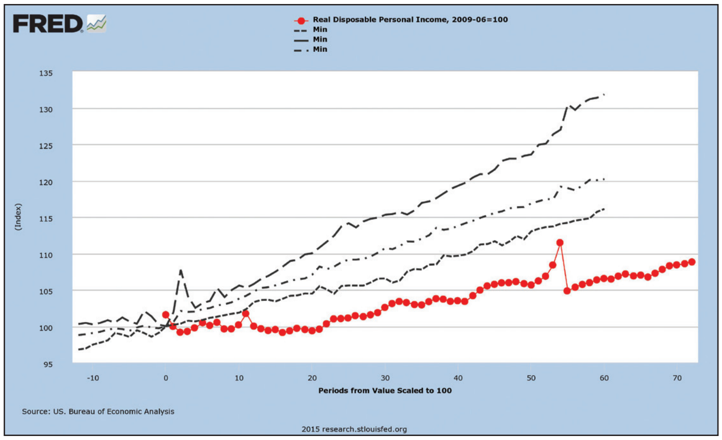
We believe the employment rate is a critical element in the continued growth of the US economy. According to the US Bureau of Economic Analysis (BEA), 70% of the US Gross Domestic Product, or GDP, is Personal Consumption Expenditures. These are the goods and services produced for household use. There is a very strong correlation between income and consumption, so the more jobs and income Americans enjoy, the more goods and services which will be consumed.



Personal income, much like employment, is experiencing its worst recovery in history from the most recent recession.

Growth in jobs should bring disposable income more in line with previous recoveries, and with this higher income comes higher consumption of goods and services.

However, we should temper these words of optimism with a few cautions:

As we begin 2015, US equity prices are not cheap. The S&P 500 Index, for example, is selling at 18 times trailing earnings. Not outlandishly high, but high enough to cause some concern. Besides, there are a few areas in the world that are expecting much stronger economic growth and whose stock prices are selling at more attractive prices. Therefore, the US might be a good, but not the only, place to invest.

The coming increase in interest rates has been well publicized. We all know that when rates do go higher, there will be a negative effect on bond prices, as well as other income investments. In other words, to get from today's low rates to higher interest rates, investors might experience some losses in their current investments. Nevertheless, the good news is that these higher interest rates should be accompanied by a stronger economy, higher stock prices and more income for those who in invest in bonds.

The drop in oil prices was a surprise and has a mixed impact. While the lower cost of gas will encourage consumers to spend more, it can have a negative effect on oil producers and countries that export oil. One country that exports a good deal of oil is Russia. Lower oil revenues, weakened currency and the ongoing economic sanctions imposed on the country by the US and others have already had a devastating impact on the country. How Russia will react to this and how these events will affect other countries in the region is unknown. But it does raise another concern – the geopolitical environment.

The world is not a stable place. With many unsettled factions seeking political, religious and economic change, we must accept this risk not knowing the magnitude or nature of any eventual event. Unknowns such as cyberattacks, possible drone attacks and spreading of religious wars are examples of new threats to our country.

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At present, of course no one has the answer to what will happen in 2015. Experience, however, has taught us that 1) there is always concern and sometimes fear about the future, 2) investing in times of uncertainty can generate attractive gains in the future just as investing in times when everything seems to be going right can set you up for some unwanted losses, and 3) a healthy respect for the market is probably the best asset any investor can have.

In conclusion, 2015 is starting out looking like another good year as world economic growth rates are positive and selected stock prices have room to increase. However, we encourage everyone to be cautious as economies transition from a low interest rate, low inflation, and slow growth environment to more normal levels of growth. The transition could be challenging at times.

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