First Quarter Commentary, April 2016

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Big Swings This Quarter

The first quarter of 2016 was filled with a unique combination of optimism and fear. In these mixed emotions, we observed the S&P 500 start from 2,038 on January 4th, to go as low as 1,810 on February 11th, to ultimately closing the quarter out at 2,059 on March 31st.

This recovery alleviated the concern of the U.S. possibly heading into a recession, and this concern was further reduced by the U.S. Federal Reserve making the decision to not raise rates in March. That said, the global economy is in a unique historical circumstance of cheap money and negative interest rates. Yet, this globally, uniform monetary stance is unchartered as far as what it means for global currency and how it will impact the perceived fragility of the global economy. Put simply, there is no playbook as far as what the outcome will be for negative rates for the global economy – good or bad.

However, it is imperative to think critically and act logically when it comes to how the markets impact our investments and purchase decisions. For example, a young family should absolutely look to buy a home to capitalize on these low rates, which in time will be a meaningful investment as rates rise and inflation elevates home prices. Also, despite the volatility and uncertainty of the equity markets, they remain the greatest long-term wealth builders for those with a time horizon over ten years. Put simply, we as a firm, believe that wealth is built by being diversified across equities, fixed income, cash, commodities and real estate. If you stay prudent and disciplined with this approach of remaining diversified and investing based on time horizon, you will do quite well.

U.S. Equities

The S&P 500 Index finished the quarter 1.35% while the S&P 500 MidCap 400 Index fared better, ending the quarter up 3.78%. The laggard for the quarter was the Nasdaq Composite Index finishing -2.75%. Worries of China and slow global growth impaired U.S. equity performance reaching 52 week lows by February 11, 2016. Equities and Oil were moving in lock step and many feared a collapse in oil would lead to systematic failure across some sectors including the banks.

The S&P 500's recovery was led by inflows into safer large cap companies that had consistent and stable cash flows such as telecom, materials and utilities. Ironically, it is these sectors that tend to outperform as we near the end of an economic cycle. That said, we do believe we are nearing the end of the mid-cycle and entering the late-cycle leg of this bull market which started spring 2009. However, we remain optimistic that larger innovative companies will continue to do well moving forward and U.S. equities remain favorable to global equities - typically this phase usually last 1.5 years ahead of a recession. Also, as the dollar continues to come off multi-year highs we believe this will shift to a tailwind for international revenue.

It is important, as investors, that we remember our time frame invested in equities is for the long-run. Here at Geier Asset Management, Inc. we identify secular themes that can last 10 – 30 years. Some themes we invest in include big data, healthcare innovation, internet of things (IoT), and the economic impact of a rising global middle class. It is through these themes that we can identify the best companies and managers to utilize in our investment portfolios.

International

The biggest theme in the international stock market is accommodative monetary policy in developed and emerging economies. The European Central Bank (ECB) continued to reduce key interest rates, and dropped rate deposits to -.40%. The initiative here is to force leverage, lending and spur economic development. However, developed nations have been slow to recover despite stimulus efforts and rate reductions. Indexes pushed lower internationally for the same reasons here in the U.S. because of concerns in China, falling energy and the potential systemic issues caused by both failures. Yet, as volatility ebbed, oil prices began to elevate, and China's GDP forecasts showed stability which allowed international markets to stabilize. The EAFE index (Europe, Australasia, Far East) finished the first quarter -2.88%, which was a dramatic improvement from its bottom earlier in the quarter. Emerging markets fared the best by the gradually weakening dollar of its highs finishing the quarter up 5.75%.

Over the next year it is possible that emerging market equities will be the best performing sector because of the declining dollar value and increase in commodity prices. The markets tend to be efficient and U.S. equities have outperformed emerging markets by 84 percentage points over the last five years. It is unlikely that this trend will persist and as markets tend to revert to the mean it is likely to see an outperformance relative to domestic equities over the next several years. A conservative way to bring exposure here besides investing directly in these companies and the index would be to allocate towards companies in the materials sector that directly participate in these economies both via operations and product. The world is getting flatter and large U.S. companies directly generate international and emerging market revenue.

Fixed Income

Fixed income, aka "bonds", remain a wonderful way to diversify your portfolio, provide a low correlation to the stocks in your portfolio, and as a tool to generate income off your investments. U.S. Treasuries will remain a safe haven for international investment for at least the foreseeable future, and with that comes less volatility than those pundits on T.V. anticipate. Specifically, with negative international interest rates, U.S. Fixed Income becomes a better alternative for the rest of the world. Conversely, with much of the world in low interest rates, it will remain difficult for U.S. rates to move higher. That said, the Barclays U.S. Aggregate Bond Index finished the quarter up 3.03% while the Barclays Global Aggregate Ex-U.S. Dollar Bond Index performed significantly stronger up 8.26% as the weakening dollar becomes more noticeable.

U.S. investment grade fixed income will benefit as investors seek safe-haven securities. With the volatility we saw this first quarter, yields on long-term treasuries finished at their lowest quarter-end levels in several years. It is for this reason that we should not ignore investment grade debt in our portfolios because this investment will most likely continue to perform well when the equity portion of your portfolio performs less than ideal. Further, fixed income remains a meaningful way to rebalance your portfolio when stock values pull back during the conclusion of the economic cycle.

Conclusion

Life is a lot like investing in the sense that we are always faced with a choice in a decision to act – do nothing or do something. And often this decision is weighed by anticipating our downside or our upside. So too, successful investing requires taking gains and mitigating risks through diversification. It is for this reason that we rebalance your portfolio, objectively offer advice on when to allocate towards assets like real estate, and consider building your cash position for an emergency safety net. You should only have to become "wealthy" once, and successful investing requires anticipating your downside and not being "greedy" with the upside potential. As we enter the spring of 2016 a lot of us will have new opportunities, new challenges, and new lessons to be learned. However, the one singularity that we always strive towards is *progress*. Progress to be better investors, progress to be one step closer to retirement, and progress towards reaching our goals. Yes, all these often can and do come together.

As always, we appreciate your trust and business. Have a safe and fantastic spring!
