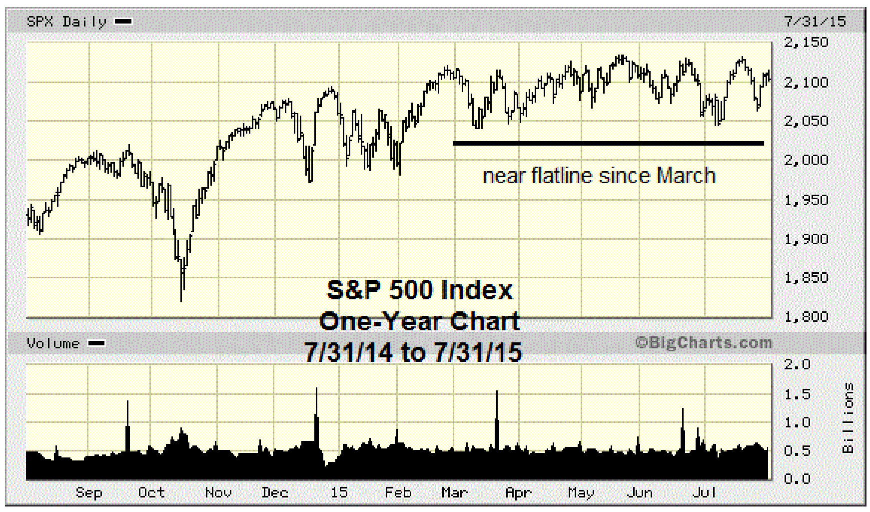
American Heritage Financial

August Update **August 3, 2015**

Dog Days of Slumber

Dog Days of Slumber: When 2015 began, we agreed with the consensus which expected another solid year for stocks. Most people thought stocks would continue the long bull market and provide gains in the high single or low double digit ranges. We are all still waiting. While the “bull” is still intact, the market has acted increasingly tired, investors have become increasingly uninterested and returns are amazingly flat.



As shown both on our one-year chart of the S&P 500 and the accompanying table, returns for the **major stock indices haven’t gone anywhere**. The Dow is negative by a fraction year-to-date while the S&P 500 is up about 2%. Other sectors have shown more volatility: transportation and utility stocks are down in the mid-single digit range while the NASDAQ is positive by a similar amount. Of course, the real action has been commodities. Key industrial commodities have been tumbling for a year but declines like **oil’s +20% plunge in July** (crude’s biggest monthly drop in seven years) and a new **five-year low for the price of gold** have sent shock waves through energy, materials and industrial stocks. There are also—*pockets*—of strength. High growth areas like healthcare (especially biotech) and dominant internet/tech stocks like Google, Facebook, Amazon or Netflix, have been on fire.

INDEX	***7/31/15 CLOSE***	***2015 YTD***	***52 WK CHG***
Dow Ind	*1769.86*	*--0.8%*	*7.3%*
Dow Tran	*8391.76*	*--8.2%*	*3.3%*
Dow Util	*583.94*	*--5.5%*	*8.0%*
S&P 500	*2103.84*	*2.2%*	*9.3%*
NASDAQ	*5128.28*	*8.3%*	*17.8%*

It is the strength of those select, large stocks in the biotech, internet and technology sectors which is providing some of the more interesting traits of this market. Those big stocks have a disproportionate impact on stock market indices like the S&P 500 (the indices are weighted by market cap), so **big gains in a minority of stocks are offsetting flat or weak returns in for the majority of stocks**. To provide statistical evidence of this; the S&P 500 “Equal-Weight” index is up 0.6% this year compared to the 2.2% gain in the benchmark S&P 500.

When market strength is isolated to only a few stocks, it implies **the overall market is not quite as healthy as the flat returns indicate**, but it appears this trendless market may continue since no major catalyst is obvious to force a move one way or the other. Uncertainty also continues to dominate the likelihood of the “expected” Fed rate hike in September. Janet Yellen, and most everyone else, is anxious to take that first step to “normalizing” capital markets by showing that the Fed can increase rates. Yet, the uneven economic gains combined with concerns about economies in China and Europe, along with plunging commodity prices, are all keeping decision makers (and regular stock investors) on edge.

One of the best things the stock market has going for it right now is the **skepticism of investors**. When investors are wildly bullish, the end of an uptrend is usually near while cautious investors typically let cash build as they await a signal to become more proactive. Investor caution is highlighted by the fact that the last two weeks of July saw $2.8 and $1.8 billion withdrawn from domestic equity mutual funds, according to Lipper data. In addition, the American Association of Individual Investors, which polls investors on their attitudes, reported only 21.1% of investors are “bullish” as of July 29, a drop of 11.4 percentage points from the previous reading and a five year low for bulls. AAII also reports that 40.7% of investors are “bearish,” not excessively high; and 38.2% are “neutral” –kind of like the market!

Longer-term, we have to keep our eye on the economy and profits. Both of **these critical metrics continue to grind forward.** The current (second quarter) earnings season is still young but Credit Suisse reports approximately 72% of companies reporting, thus far, have beaten earnings expectations. However, only about 51% of companies beat their estimated sales numbers, implying the profits have been generated by cutting costs. Most concerning about this quarter’s reports is downbeat future guidance provided by many companies. Still, economists are holding to predictions of earnings growth of about 9% for 2015 which could easily justify an S&P level of at least 2,175, or 3% to 4% higher than the July close.

As for the overall economy, the most recent read on the second quarter was 2.3% GDP (Gross Domestic Product) growth. Most economists still think the U.S. economy will grow at a rate over 2.5% for the second half and net 2% to 2.3% growth for the year. There are also some optimists predicting GDP growth of better than 3% for 2015. We would point to recent numbers showing the sales of existing U.S. houses climbed to an eight-year high in June and the National Association of Realtors said recently that prices have risen to a record amid tight supply. Employment is solid and the unemployment rate is at 5.3%, a seven year low while the number of new claims fell to a 41 year low in mid-July.

As all this suggests, it is certainly a **time to be careful and selective but there is little to warrant outright bearishness.** The bull market is long in the tooth but bull markets rarely end until euphoria is rampant or the economy is rolling over—or both. Neither of those conditions is currently present. One special point about this market is the narrow focus on high growth. Value investing and bottom fishing is not being rewarded but chasing winners is never a long-term winning strategy. We will be keeping all these ideas in mind as we continue to work to find the best combination of investments to keep portfolios on track to meet long-term objectives. Meanwhile, you may not miss much if you forget the market to enjoy the Dog Days of August!

Best regards,

Ted Ingraham

EGI Financial, Inc.
American Heritage Securities, Inc.

Questions or comments?

Email us at: ahs@egifinancial.com or call 330-535-0881. Visit us at www.EGIFinancial.com