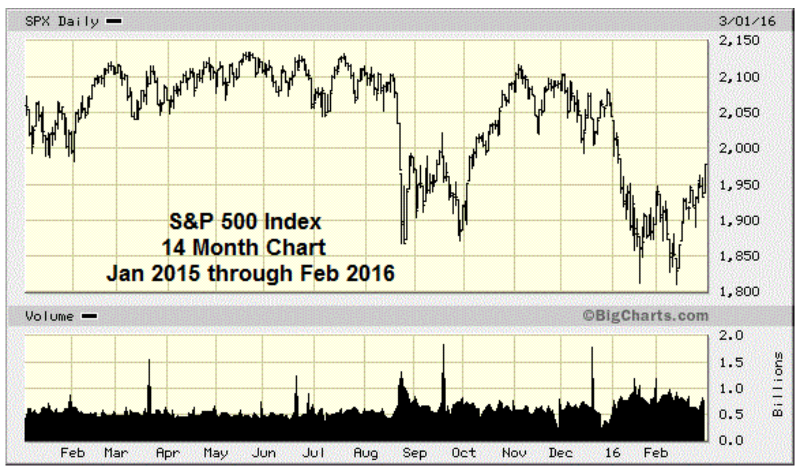
American Heritage Financial

March Update **March 2, 2016**

Really Really Incredible!!!

2016 is off to an ***incredibly*** rocky start (I had second thoughts about using that adjective—considering its constant usage by a particular Presidential candidate. Then, on further reflection, it seems the candidate's usage has made the word even more fitting as a description of recent market events!) We will focus only on the incredible financial markets—although the political environment certainly reflects investors' frustration and it may soon have a larger impact on financial markets.

The mystifying gyrations of stocks, bonds, currencies, and commodities (particularly oil) are a reflection of numerous strange financial and economic conditions. The economy and market were plugging along in a fairly resilient fashion up until about mid-2015 when small cracks started to appear like stress fractures in a 747. An accumulation of unusual conditions—which had been evolving for years—began to impact our otherwise healthy market and economy last year. The list of issues that have caused the current financial malaise begins with the effects of ***unorthodox monetary policies of the world's central banks*** (led by our Federal Reserve), including low interest rates, zero interest rates, negative interest rates, QE (quantitative easing) and other efforts to boost growth and/or avoid financial collapse. When we add extremely high debt loads, stifling regulations, aging demographics, political turmoil, horrifying terrorist activity and the normal turn of economic cycles (accentuated by the Chinese super-growth cycle) to the unusual monetary policies, it is easy—well, easier—to understand what ails our financial markets.



Many of the issues mentioned above are present in the United States but are much more extreme in foreign economies. It is far beyond the scope of this commentary to go into detail on all these causes of financial stress, but we will try to understand the resulting impact to our financial markets.

The problem created by extreme monetary policy is the impact it has on asset values. The economic principle is that low interest rates and other sources of "easy money" incentivizes capitalists to take advantage of that money to produce goods and services—or, put in other terms, low cost money provides opportunities to invest in businesses—thus creating growth and jobs. Unfortunately, excessively easy money policies since the financial crisis have had only limited success in achieving that objective while there have been unintended consequences of inflating those financial assets which have served as a parking place for the excess cash. Investors (or, the more precise but politically incorrect word is capitalists) have not been sufficiently motivated by low cost money or near zero interest loans. Their reluctance relates to a number of the causes mentioned above, especially excessive regulation, political turmoil and declining economic cycles in many corners of the globe.

The results are most easily seen in elevated prices of financial assets such as stocks and bonds (high priced bonds equal lower interest rates) but many other parts of the global economy have also been impacted. Currencies have been distorted; first by countries lowering their currency in order to compete in the global economy and, second, by the U.S. Dollar appreciating due to the relative attractiveness of the U.S. in this time of global economic weakness, political turmoil and heightened terror activity. Commodities, in general, are weak because of the struggling global economy and because they are priced in Dollars (commodity prices decline as the Dollar strengthens). Oil—the most critical commodity—has declined much more than most commodities because it is suffering from the success of efficiency (both more efficient production and efficiencies that have led to lower consumption). Global economies continue to struggle, partially due to the normal business cycle but they are also burdened by over-regulation, weak commodity prices (hurting commodity exporting countries), aging demographics and political turmoil. To add more confusion to these issues, consider that the U.S. central bank has decided our economy is strong enough to move back to more market based (i.e. higher) interest rates and less accommodative monetary policy at the same time that the rest of the world is moving to lower—even negative—interest rates as they continue to try to stimulate their economies.

All this either makes your head swim or you see (more easily than I) that all of these issues are inter-related. The world has tied itself into a complex knot and unwinding these problems won't be easy or quick. The volatility and disruption over the past nine months or so is simply the financial markets' means of digesting such issues.

While these issues are shared by the U.S. and global economies, our economy is healthy—very healthy relative to the rest of the world. Of course we are very much in a global economy and global issues impact us. Our manufacturing sector, for instance, is particularly hurting due to the strong dollar and weak global demand. It also highlights the tremendous strength of many, many great U.S. companies. If you look at your portfolio you will see quality names such as GE, CVS Health, McDonalds, Proctor & Gamble and many more. These companies are not going away. If the price has declined recently it is, in most cases, an opportunity to purchase the stock at a great price and reap attractive dividends as the market completes this current digestive phase. The long-term outlook for our market and economy remains very positive.

As we said above, the market has been incredibly difficult recently due to some incredible conditions. It may continue to struggle throughout this year, but it is not a time to panic or abandon investment strategies. It is a time to reassess and invest when low priced opportunities are available. If you are uncomfortable with your current portfolio or investment strategy, please don't hesitate to contact us for a full review.

Best regards,

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Questions or comments?
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