American Heritage Financial

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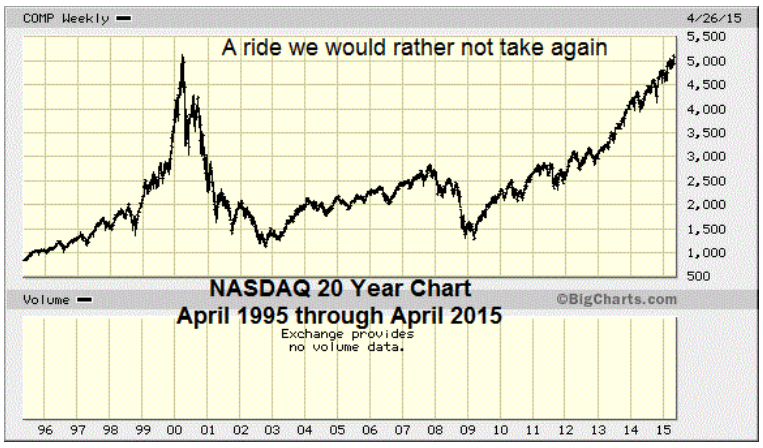
Stuck in a Rut at New Highs

It was a long time coming but on April 23rd, the NASDAQ exceeded its old "dot-com" high of 5,049, a level last attained 15 years ago on March 10, 2000. The new NASDAQ high, and the technology stock influence of that index, have led the stock market in 2015 but that is about the only similarity we can draw between the recent record and the crazy days of 2000.

The NASDAQ's year 2000 high was the culmination of its latest surge which saw it gain 85% in the five months from October 1999. And, that last leg was only a fraction of the four-fold gain in the NASDAQ from early 1995.



NASDAQ 20 Year Chart
April 1995 through April 2015

The current record is different in its velocity and valuation. While the NASDAQ has led all other broad-market indices of late, the recent record was reached much more slowly than the old one. The NASDAQ is up "just" 20% in the past twelve months and has a 4.3% year-to-date gain for 2015. In 2000, the NASDAQ's valuation was reflected in a price-to-earnings multiple (P/E) of 75; currently the P/E is just over 20. Fifteen years ago, the index consisted of 69% technology stocks; today tech representation is down to 42%. Moreover, in the dot-com era, the index was heavily influenced by hot internet start-ups, today the most influential stocks are behemoth's Apple, Google and biotech bellwethers Amgen, Gilead, and Biogen.

INDEX	4/30/15 CLOSE	2015 YTD	52 WK CHG
Dow Ind	*17840.52*	*0.1*	*7.7*
Dow Tran	*8592.89*	*-6.0*	*11.3*
Dow Util	*586.63*	*-5.1*	*5.6*
S&P 500	*2085.51*	*1.3*	*10.7*
NASDAQ	*4941.42*	*4.3*	*19.7*

Comparison of today's NASDAQ record to its previous peak is interesting but the bigger picture it paints reflects the entire market. Stocks continue to march higher—all broad market indices are at or close record highs—but markets are straining to make additional gains and investors are far from euphoric. The Dow and S&P 500, for example, are only marginally positive for 2015, as reflected in our accompanying table. The AAII Sentiment Survey, which measures individual investor's confidence in future market gains, is currently showing a 30.8% bullish reading compared to its long-term average bullish reading of 38.9%. More telling is the 47.2% of investors who see a "neutral" outlook—reflecting today's predominate uncertainty in the stock market. Also, unlike 15 years ago, stocks that don't deliver fundamentally are not forgiven. For example, within days of the new NASDAQ high, two of the more speculative leaders, Twitter and LinkedIn tumbled 25% and 20%, respectively, on disappointing earnings reports.

Considering that investors are relatively flush due to low interest rates and a simulative Fed, and this bull market has been rewarding participants now for six years (with a 140% advance since March 2009), why has it been so difficult to achieve additional gains? The answer is the same as Bill Clinton pointed out in 1992, it's the economy…. The market's stubbornness has been nothing compared to the slow moving economy. Sluggish economic growth, weak earnings, a rising dollar and the prospect of higher interest rates have kept U.S. stocks in a trading range since November—in spite of the record in the NASDAQ. The most recent blow was the disappointing report at the end of April that the U.S. economy grew at just a 0.2% rate in the first quarter of 2015. That compared to estimates of 1% growth but the good news is that 1Q 2015 was a 2.3% increase over conditions in the first quarter of 2014 (both were negatively impacted by severe weather).

Many analysts are dismissing the weak first quarter GDP growth and point out that the same thing happened last year but 2014 still provided strong growth after the first quarter and stocks gained 9.3% from May through December. There could be additional headwinds this year. In 2014, S&P earnings grew nearly 10% during the year's last three quarters. This year, analysts are predicting little net gain in earnings over the next three quarters. In addition, the P/E on forward 12-month EPS was 15.9 at the end of April 2014, versus the current 17.7, according to Capital IQ.

The good news in the economic gloom is that the Fed continues to hold back on tightening while other central banks around the world are still in the early stages of priming their pumps. Also, many analysts believe the timid consumer, who has been paying down debt for six years, has seen solid increases in home and investment values and is benefiting from the greatest energy related windfall in memory, will suddenly come to life and propel the economy into high gear. It all makes for interesting times for investors—times we believe will continue to reward those who take a prudent buy positive approach with a diversified equity oriented investment strategy.

Best regards,

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Questions or comments?

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