American Heritage Financial

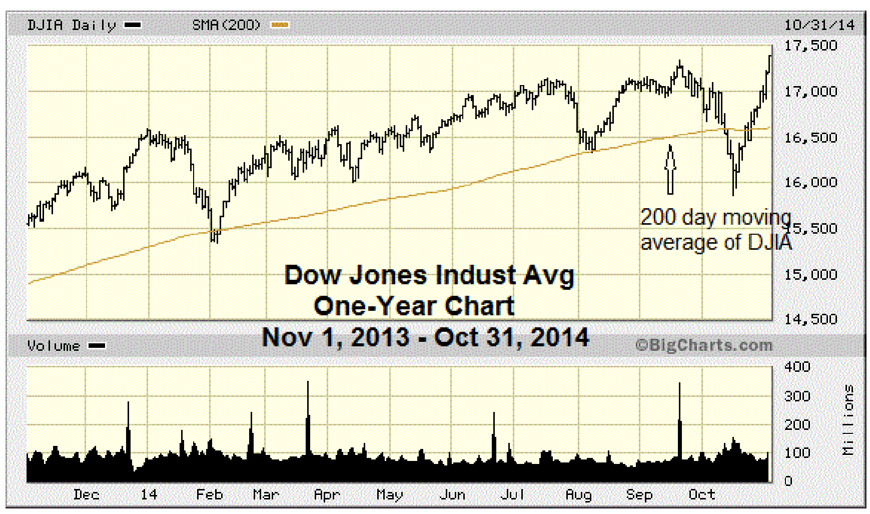
November Update **November 4, 2014**

VOCTOBER

V is for Volatility!

Borrowing from the popular trend of blending two or more words and meanings into one word,***** we officially designate last month as ***"Voctober."*** Stock market charts formed a near perfect "V" during the month, as illustrated in our one-year Dow Jones Industrial Average chart below. That **"V"** also represents the bone-numbing ***volatility*** investors were subject to all month long.

The descending leg of the "V" actually began September 22 as markets slipped from record highs. However, the wild leg of the ride occurred from October 8 through October 15. During those six trading days, the Dow **lost 853 points and saw intraday swings as high as 458 points**. From the September peak to the October trough, **the market declined by 7.7%**, not quite the 10% that defines a "correction" but the volatility and near-panic conditions created a textbook mini-correction that was sufficient to put fear in the hearts of most investors. The reversal back up was just as crazy with the Dow gaining 1,273 points in the last eleven days of October to reestablish a new all-time high on October 31.



So what caused all the turmoil and where does it leave us? The decline was long anticipated and long overdue. Many investors were just looking for an excuse to take some profits and the early selling can be attributed, mostly, to global issues. It began with renewed concerns about slowing growth in China; ebbing growth in the world's second largest economy has long been a drag on the global economy. U.S. led air strikes on ISIS targets in Syria began in the final week of September and also had a chilling impact on our financial markets. Additional concerns layered on like an accelerating snowball in the form of a few weaker than expected U.S. economic numbers, continued European economic woes, uncertainty about the Federal Reserve's interest rate policies, panic over Ebola and plunging commodity prices. These issues pushed the market into a true free-fall and, suddenly, the themes of mid-Voctober were ***deflation***, ***$80 a barrel oil***, ***growth concerns*** and perpetually ***low interest rates***.

Then, the market reversed. The sudden pivot back up can be attributed to three factors: 1) Soothing words by the Fed—reassuring investors that the economy remains healthy, yet, it won't hike rates anytime soon; 2) Better than expected earnings (in most cases). Strong third quarter results were gushing in by the third week of October; and, 3) Investors with no better alternative than U.S. stocks and still high cash hoards felt pressure to begin bargain hunting. As the month ended, the certainty that the Fed was following through with its plan to end quantitate easing (QE), along with Japan's stunning announcement of an aggressive monetary stimulus program, combined to push investors into a buying panic that was as powerful as the selling panic of two weeks earlier.

So after all this volatility the market is back at new record highs. In fact, the S&P 500 has managed a new record high every month for the past 16 straight months—the longest such streak in its history. During these record setting 16 months, it has gained nearly 29%. Considering that we prefer to "buy low and sell high," we're not crazy about markets at record highs but we believe the market today, at the beginning of November, looks more appealing than it did at the beginning of October or many of the immediately preceding months. Conditions are more favorable now mainly because the market worked its way through a rough (even if short and shallow) correction and has come out the other side stronger. Also, corporate earnings have proved supportive of more market gains; with half of the S&P 500 companies reporting, earnings have been better than anticipated and earnings are now expected to grow by 6.7% this quarter versus earlier estimates of about 5% growth. Another positive is Fed comments on economic growth and their elimination of the 37 month QE stimulus while, at the same time, providing assurance that short term interest rates will remain low. A slow-growth economy is good for stocks and the economy continues to stagger, not stumble, ever forward—the preliminary GDP estimate shows we enjoyed 3.5% growth in the 3rd quarter, the top of analyst's range of expectations. Last, the huge decline in the price of oil will provide a windfall of spendable cash that will help drive the largest sector of the economy, consumer spending. (Although the decline in oil and other commodity prices is a double-edge sword, it reflects global economic weakness and is troubling to America's booming energy industry.)

All-in-all, the positive environment for equity investors should continue. We expect a continuation of the heightened volatility and investment returns will be selective, rewarding growth and stability while penalizing poor execution and uncertainty, but it appears the correction worries are off the table for at least a few months. One last piece of market minutia: mutual funds are underperforming their benchmarks going into the final two months of the year. Eight out of 10 U.S. stock funds focusing on large growth companies are trailing their benchmark index, the second-highest proportion in a decade, according to data compiled by Morningstar. Declines in small caps and technology companies have left fewer equities beating the index than at any time since 1999. The "average" stock is up 4.4% this year, about half as much as the S&P 500. This does not simply mean large is better because the large-cap, blue chip Dow Jones Industrial Average of 30 companies is underperforming the S&P 500 Index by 4.3% year-to-date through September. The Dow is up just 4.9% versus 9.2% for the S&P.

*** There is a word for that:** "portmanteau" means blending two or more words and meanings into one word. It originates from a French word for a suitcase or trunk which opens up into two parts. Of course, we had to look that up (Wikipedia) but our Voctober idea originated as an offshoot to the increasingly popular ***Movember*** movement.

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