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What, Me Worry?

Global Markets and Regions

	1st QTR	2015 YTD
US	1.40%	1.40%
Developed Europe	3.60%	3.60%
Asia	7.40%	7.40%
Emerging Markets	2.30%	2.30%

US Markets

	1st QTR	2015 YTD
Dow 30	-0.26%	-0.26%
Large Cap Cos.	1.14%	1.14%
Mid. Cap Cos.	5.23%	5.23%
Small Cap Cos.	3.96%	3.96%
Bonds	2.06%	2.06%

Investment returns in 2014 were modest and mixed and it appears 2015 may also deliver mixed returns but with a different cast than 2014. US stocks did reasonably well, though most of the returns were concentrated in larger capitalization stocks. The majority of the gains were delivered by a relatively few companies and a relatively few industries. Apple Computer and Biogen helped the larger capitalization indices such as the S&P 500 and the NASDAQ, but not so much Exxon-Mobil or Caterpillar. Smaller companies barely delivered middling single digit returns. This year's modest mix appears to be changing.

Foreign stocks were losers and commodities were big losers. Foreign stocks are strong so far this year and commodities are flat. US bonds produced reasonable returns last year, but not from interest payments. When a 10 year US Treasury bond pays 2% and a European Government bond pays less than ¼ % which do you think investors would rather own? It's not hard to see what might happen to bond prices if interest rates ever begin to rise. The risk reward trade off does not appear favorable, but the large interest rate differential between US and Foreign bonds continues to support prices. It will be interesting to see how bonds respond when or if Central Banks begin to raise interest rates.

The perception of the general investment climate still seems to be benign. The markets are continually reporting new highs, even if the highs are just fractionally higher than the last ones. The absence of any sustained price decline of more than a few percent seems to have contributed to the perception of calm. Historically, markets have been prone to periodic declines of 15% or more lasting six months or longer without changing the overall trend of the market. It has been several years since the markets have seen such turbulence. The only major price decline last year was in oil, and who can argue with

cheaper gasoline? With summer vacation season just around the corner, I don't think you will hear many complaints.

The pattern of returns this year is changing. Last year's losers are starting out as this year's winners. The modest label still seems to apply to both winners and losers. One thing that has moved beyond modest is volatility. Large daily moves in prices are becoming more frequent. Over time this kind of turbulence can undermine investor confidence and their wiliness to continue to invest. There is clearly no shortage of potential "worries" for investors, though I guess it's safe to say there never really is. With stock valuations at the upper end of historic ranges and bond yields at historic lows, it would seem that markets are priced to deliver modest returns.

The Russians have been fairly quiet this year. Mr. Putin even took an extended, unannounced and unexplained vacation. "Game of War" Ukraine has also been quiet, but Putin's back tanned and fit. ISIS and their various affiliates have been very busy this year, first in Nigeria and now in Kenya. While the carnage they have spread has been appalling, they haven't yet upset any major markets. Iran, a potentially large oil producer, seems poised to be re-introduced into the formal world economy with the potential lifting of economic sanctions. Maybe they will or maybe they won't. In the meantime they are extending their influence into Yemen which shares a border with Saudi Arabia. What could go wrong with that?

Greece may run out of money any day now. At least that's what we're told. The Germans seem to come up with some extra change whenever it is needed. While it appears that Greece and the rest of Europe are not really compatible economically, they still are intent on remaining in the European Union for now, particularly since the European Central Bank has embarked on their version of Quantitative Easing. It's worked so well everywhere else it's been tried maybe they want to be around to see the results. Hopefully Ben Bernanke sent them the instruction manual. I'm sure they can consult with Janet Yellen on the details, though she may be busy managing interest rates here in the US.

Earnings season opens again soon. Early forecasts are that we will see the first decline in earnings since 2009. That's right, declines. Declines are not losses. The ability of corporate America to continue to increase earnings in the face of a modest economic recovery from the Great Recession has been the story behind the generally positive stock returns. Investors have been willing to pay more for a rising stream of earnings and dividends. The Federal Reserve, by keeping interest rates artificially low, has made their job easier. Whether and how long they will remain low is now being debated. It usually takes a recession, an actual decline in economic growth, to negatively impact stocks. The next recession does not seem to be directly in front of us. The "worries" of the future are always in front of us, until they're right on top of us.

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