

2014 Second Quarter Investment Commentary

July 25, 2014
Michael J. Porro, CFP, EA

Our accounts are up an average of 6.1% for the first six months of 2014.

We'll take this!

'Once we acknowledge that, in life, we are playing soccer, not baseball, a few things become clear. First, awareness of the landscape of reality is the highest form of wisdom. It's not raw computational power that matters most; it's having a sensitive attunement to the widest environment, feeling where the flow of events is going. Genius is in practice perceiving more than the conscious reasoning.'

- David Brooks, [The New York Times](#)

"...Collaboration and sharing inspiration most often result in something greater than the sum of the parts. Collaboration requires initiative to act on one's inspiration and to participate with others to give rise to invention and entrepreneurship. In many cases it is only fear that prevents us from taking the initiative necessary to turn ideas into acts. We don't need to accept the notion that as just one person we could not make a difference in the advancement of society."

- Michael Mooslin, [the Christian Science Monitor](#)

"I work in Washington, right in the middle of intensely public political battles. Bar none, the unhappiest people I have ever met are those most dedicated to their own self-aggrandizement- the pundits, the TV loudmouths, the media know-it-alls. They build themselves up and promote their images but feel awful most of the time. That's the paradox of fame. Just like drugs and alcohol, once you become addicted, you can't live without it. Celebrities have described fame like being 'an animal in a cage; a toy in a ship window; a Barbie doll; a public façade.' Yet they can't give it up."

- Arthur Brooks, [the New York Times](#)

'We ought to say to these children, "Welcome to America. You're going to go to school and get a job and become American's." We have 3,141 counties in this country. That would be 20 per county. The idea that we can't assimilate these 8-year-old "criminals" with their teddy bears is preposterous.'

- George Will, Conservative commentator on 'Fox News'

Please send to Congress only those people who understand that we work best when we work together, that no person is right or wrong, that each of us has gifts and talents and when placed together can create miracles and that "We the People" deserve better than what they presently are giving us.

- Michael J. Porro, Investment Maven

One hundred years ago on June 28th, the spark that ignited World War I, "The War to End All Wars", was struck with the assassination of Archduke Fernand in Sarajevo. By August 4th war was declared as stresses that had been building up over the preceding fifty years exploded and mankind fell into a morass of murder that consumed the lives of over 16 million during the ensuing four years. Are we any

better off today? Look around us: we have Russia apparently nostalgic for its cold war “superiority”, tossing treaties aside to usurp Crimea and eastern Ukraine, shooting down commercial airlines without compunction, Syria and Iraq imploding with the extremists of ISIS crucifying and beheading any who don’t bow to their brand of religion, Israel and Hamas doing their best to turn the land of Gaza and Israel red with blood, Boko Haram holding Nigeria hostage to their brand of Islam, while Libya, Egypt, the other countries of the Arab Spring, Afghanistan and Pakistan remain in civil turmoil or war. China is flexing its ever strengthening muscle in Asia while Japan slips on its cloak of “Abe Supremacy” not seen since the end of WWII. Central America is sending its children for refuge from drugs, rape, gangs and dismal future to the United States for salvation. The US Congress continues to play political fiddle instead of exercising higher order collaborative efforts to address the problems before us. France elects a Nazi sympathizer, Marine Le Pen, seeker of a “Paris-Berlin-Moscow Axis”, to the European Parliament. Argentina defaults (again) and Cyprus (banker to the Russian oligarchs) remains in financial crisis. The Cyprus crisis, and that in Portugal, brings on thoughts of the small Viennese bank, Credit-Anstalt, which folded in 1931 and exacerbated that Great Global Depression. I could go on, but why bring on a full scale mental and emotional depression?

Yes, bull markets climb a wall of worry indeed.

Oh, did I mention that the Dow Jones Industrial Average closed above 17,000 on July 3rd? Or that our investments are up an average of 6.1% for the year through June 30th? Or that our country and most of the worlds’ economies appear to be slowly climbing out of the carnage for the 2008 financial collapse?

Your Progress Reports for the first six months of 2014 are enclosed. Measure your progress against our average. Of course many will be higher, since the 6.1% is the average. We are pleased with our results again this quarter in light of the meager increase of 1.5% in the DJIA, the 5.5% increase in the NASDAQ, the 2.5% increase in the Russell 2000 and the 6.1% (oh my goodness, this matches our average) in the S&P 500 Index. It appears that our eclectic mix of large cap, small, foreign, growth, income, niche, beaten down babies, dividend paying investments is working well in this environment. It may be that it’ll work well in all environments. We shall see as time marches on, but I will tell you that it’s a pleasure to see the hundreds of dividend payments deposited into our accounts each day. These should shoulder any upcoming downturn.

We still haven’t experienced a severe 10% or more correction in this latest move up in equity prices which began in March 2009. Stock markets appeared to begin a downturn as July ended, with the DJIA falling from its all-time high of 17,138 on the 16th to its recent low of 16,368 on August 7th (a 4.5% pullback), but it recovered a quickly as it began with the Dow trading above 17,000 today, August 21st. We still anticipate a more severe pullback and therefore are cautious short-term.

Countering the global political negatives are the following domestic economic positives:

1. The Federal Reserve is bound and determined to keep our economy from falling into recession. This is a great underpinning to higher equity prices.
2. Interest rates continue to remain historically low, with 5yr US treasuries yielding 1.763%, 10 yr. at 2.54%, 1 yr. CD’s at 1.10% and 5 yr. CD’s at 2.3%. Stocks, many with yields above these along with appreciation potential, still present attractive alternatives.
3. Enthusiasm for stocks continues to appear scarce. The Great Recession has chastened many Americans. Apparently, according to a recent study by a consulting firm, Moebis Services Inc., Americans are hoarding more cash in their checking accounts than at any time in the last 25

years. This is good and points to the great possibility that Americans are not over leveraged, as they were at the beginning of the 2008 downturn. As a result they will not have to liquidate holdings at fire sale prices when the market turns and this will keep any downturn from getting out of hand.

4. Fewer Americans are piling up credit card debt or taking risky mortgages. Another sign of a healthier consumer from a financial perspective and better able to withstand any stock market or economic downturn.
5. The S&P 500 Index trades at a PE of about 16.5, well below the peak of 30 in the year 2000 just before the dot.com bubble popped. Despite the run up to recent new all-time highs in this index, it is still not at frothy levels.
6. CPI, or inflation, is subdued, as are labor costs. This points to continued slack in the economy.
7. Industrial production continued to advance, but at a moderate level of about .4% annually. Moderate, but sustainable points to a more prolonged recovery.
8. Capacity utilization holds at about 79.1%, still under its long term average of 81% indicating that there is still room for economic expansion.
9. NAHB/Wells Fargo Housing Market Index (HMI), which measures the level of builder confidence for new homes rose to 49 in June, close to the threshold for "good builder confidence". New home sales jumped in May to 18.6% to a 504,000 unit annual rate, the highest level since June 2008. This increase, the largest since January 1992, suggests that economic growth can continue at a moderate pace into 2015.
10. Housing starts came in at about \$1 million in May, above the 12-month average of 950,000 units. This, the best annual rate since October 2008, bodes well for sustainable economic growth.
11. Leading Economic Indicators and Coincident Economic Indicators continue to increase indicating sustainable economic growth.

In sum, we expect continued, although moderate, advances in stock prices over the next six month or longer. We may still have that 10% correction and therefore continue to be cautious in committing new money into equities, but we believe that the trend continues upwards and are positioned accordingly. However, our globe seems to be on a precipice of something bad. We can't ignore the negative events surrounding us. Each could hold the potential to ignite disaster. We need higher order collaborative thinkers and peacemakers at the table of policymaking. Let's work to place only such people into leadership positions. We remain positive that good will prevail, but also keep an open eye to the possibility that our better angels could be knocked for a loop.

As always thank you for your business, confidence and your time to read our commentary.

