Financial Services Advisory
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Make Sure Your Tray Tables are in the Upright and Locked Position!

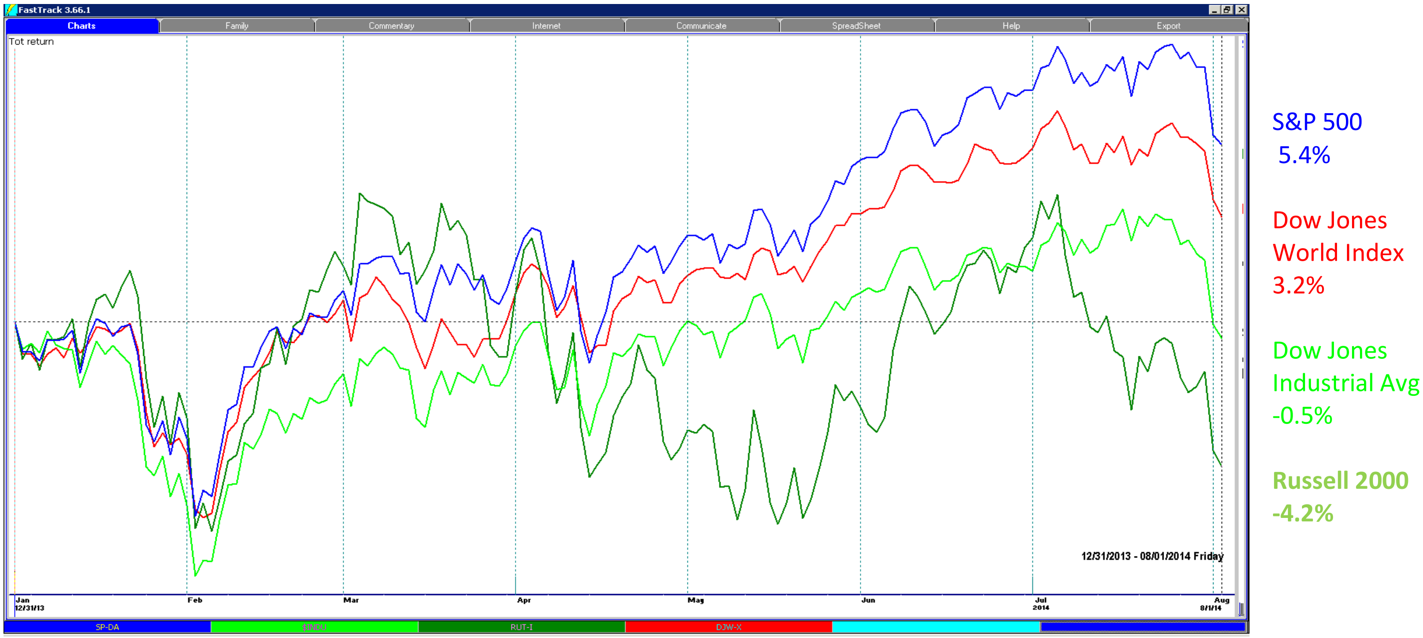
July Market Review From Your Portfolio Management Team—August 12, 2014

On any US flight, you will hear the flight attendant utter those words before take-off and landing. It always reminds me that I should expect some turbulence in the near future as the plane either accelerates into the air or returns to earth at the end of the flight. Either way, things are going to get more choppy.

We believe that is a fair assessment of the current market environment as well. Stocks have been on a fairly consistent uptrend for the past two years, without even a 10% correction, though, historically, we should expect such a correction once a year. However, July came to an abrupt end as the market's performance in the last week was the worst for stocks in six months, and July is now in the books as the first negative month for the S&P 500 since January.

As expected, high quality bonds have behaved quite well during this recent period, offering a shelter from the increased choppiness in the stock markets. And true to their nature, high yield bonds have suffered somewhat alongside stocks during this time. High yield bonds tend to move more in line with stocks over time, rather than high quality bonds; however, they are usually less volatile than stocks which is why we like to use them during periods when the environment for stocks becomes more uncertain.

The chart below shows the year-to-date performance of several indexes we track. While the S&P 500 index (in blue) seems to be performing just fine, it is being driven primarily by the performance of only three sectors—energy, technology, and health care—masking the fact that the average stock, both here and abroad, is having a difficult time keeping its head above water. Case in point, the Russell 2000 index of small cap stocks, typically the 'canary in the coal mine,' is negative for the year.



Source: Fasttrack; Data covers the period from January 1 – August 1, 2014. The Russell 2000 index tracks the performance of smaller companies. Past performance is no indication of future results.

What's Ahead

There are a number of global and economic issues keeping investors on edge right now. Foremost is the ongoing tension in Ukraine, but there is also unease about the conflict in Gaza, as well as Iraq and even Afghanistan. In addition, as the Federal Reserve continues to taper its purchases of government and mortgage bonds, investors are fretting about what could happen once the Federal Reserve is no longer supporting the stock and bond markets.

Given the strong returns from stocks over the past 5 years, and especially given the complacency among investors over the past year, it should come as little surprise that anxiety has picked up. At this point, it is nothing more than anxiety; there has been no serous break of trends among any major stock index. And high quality bonds continue to trade at or near all-time highs, as they distance themselves from the losses they suffered last year.

It has been a pretty smooth ride for stocks over the past 2 years, so it should not be a surprise to anyone that volatility has picked up. We plan to monitor our positions on a daily basis and as they trip through the FSA Safety Nets®, we will cut back and eliminate them. With the exception of small-cap funds and some foreign funds, most of our stock and balanced funds are behaving just fine. With the tray tables up, we are braced for more volatility, but as you know, in most cases the trip ends and everyone makes it to their destination in good shape.

We wish everyone a pleasant remainder of the summer.

Ronald Rough, CFA
Director of Portfolio Management