# Condor Capital Reviews 2nd Quarter 2015

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With investors' eyes remaining focused on news headlines, the S&P 500 Index returned a meager 0.28% during the second quarter.

On the back of a skyrocketing Chinese equity market and dovish global central banking policy, international equities outperformed their domestic peers.

Domestic equities offer a compelling story considering the tailwinds being generated by an improving U.S. economy.

**July 2015**



Leading up to the final days of June, the second quarter of 2015 proved to be an interesting stretch, where domestic markets remained relatively muted as noteworthy macro events began materializing around the globe. Investors' eyes remained focused on daily headlines revolving around a variety of themes, such as an inevitable Fed rate hike, a slowing Chinese economy, and, of course, a possible Greek exit from the Eurozone as the Greek government resumed negotiations with its creditors. In the face of these concerns, the S&P 500 Index managed to muster a meager 0.28% return over the prior three-month period.

With momentum carrying some of the more volatile areas of the equity markets, small-cap growth names led the race for the quarter and bested their large- and mid-cap peers. On the whole, many large-cap value names were stifled by troubling macro news, while many small- and mid-cap companies benefited from soft, yet positive, domestic economic data. With robust merger and acquisition activity and expectations of a rate hike, the financial services sector was the top performer, with healthcare and technology following behind over the prior three months. Alternatively, rising rates negatively impacted most utilities names and the growing importance of content over more traditional sources of revenue for media companies hindered growth in the communication services sector. As a result, both utilities and communications were the worst performing sectors during the quarter.

Developed international equities outperformed the U.S. marketplace, with the MSCI EAFE Index returning 5.52%, on the heels of a European monetary policy program. Correspondingly, on the back of a strong rise in China's mainland equity markets, the MSCI Emerging Market Index posted a more modest 2.95% return during the second quarter.

With the release of encouraging employment figures and housing starts, many investors believe the U.S. economy continued to remain on track during the second quarter. With the domestic economy improving, the Federal Reserve's language has recently become more hawkish, indicative of a rate hike coming at some point during the second half of 2015. Elsewhere in Europe, the European Central Bank (ECB) continued its quantitative easing program and negotiations between Greece and its lenders became more and more disconcerting, providing ample ammunition for volatility in the global capital markets.

In the fixed income sphere, as many investors continued to factor in a rate hike, the U.S. 10-year Treasury yield began trending higher, beginning the period at 1.92% and ending at 2.35%. Likewise, in what bond manager Bill Gross coined the "short of a lifetime," yields on German 10-year Bunds expectedly skyrocketed to 0.76% from a near zero 0.18% at the beginning of the quarter. Unable to escape a rising rate environment, corporate bonds were also hurt, with the Citi Corporate Bond Index losing 2.90% during the period. Additionally, the Lipper Municipal Fund Index fell 1.06% as concerns over Puerto Rico's deteriorating financial health dragged the sector down. As these areas suffered, protection came in the form of high yield bonds, with the Credit Suisse HY USD Index rising 2.90% during the quarter.

Outlook – In the short term, investors will likely remain focused on negotiations between Greece and the rest of the European Union. That being said, we think a deal gets done at some point and a Grexit is averted, at least for now. The onus will be on the Greeks to pass and implement tough measures. If an exit does occur, we believe any impact on the global capital markets will be mitigated by action from the ECB. In the U.S., as long as the domestic economy continues showing signs of growth, particularly in employment figures and wage growth, we expect the Fed to begin raising rates in 2015, albeit slowly.

With that in mind, investors should not be surprised by yields continuing on their upward trajectory, with prices moving inversely. Despite the equity markets appearing, at times, to be fully priced, we continue to believe that improving corporate fundamentals and a U.S. economy on the verge of catching steam offer a compelling story for domestic equities and justifies our optimistic outlook for U.S. equities.


- *Low mortgage interest rates*
- *Less-stringent mortgage lending*
- *Low housing inventory*
- *Millennials are entering the market*

# What's New in the Housing Market for 2015?

Home buyers and sellers finally have reason to celebrate in 2015. After almost a decade of limping along toward recovery, it seems as though the housing market has finally hit a more comfortable stride. According to the S&P/Case-Shiller Home Price Indices, well-known gauges of the U.S. housing market, real estate is finally showing healthy signs of improvement.

Data released by Case-Shiller at the end of April indicates that home prices have continued to rise across the United States. (Source: S&P/Case-Shiller Home Price Indices, April 2015) And as it turns out, no one factor is responsible for the trend. Rather, a variety of factors are being credited for the recovery.

**Low mortgage interest rates**

This year, mortgage rates have remained at all-time lows. (Source: Freddie Mac U.S. Economic & Housing Market Outlook, April 2015) A slower-than-expected economic recovery may be partly responsible, with the Federal Reserve holding off on raising interest rates until the economy is on more solid ground. And while interest rates are expected to go up at some point (possibly later this year), home buyers are taking advantage of the historically low rates while they can.

**Less-stringent mortgage lending**

Obtaining a mortgage has gotten easier this year thanks to less-stringent lending requirements. (Source: Mortgage Credit Availability Index, March 2015) A number of changes are being credited for making mortgage lending more readily available.

Fannie Mae and Freddie Mac lowered their down payment thresholds this past December to as little as 3% of a home's purchase price, a boon for first-time home buyers and buyers with low down payment funds available.

In addition, the Federal Housing Administration (FHA) announced this past January that it will lower what it charges for annual mortgage insurance premiums. The 0.5% decrease, from 1.35% to 0.85%, is expected to reduce an FHA borrower's annual mortgage payment by $900 per year, on average. (Source: U.S. Department of Housing and Urban Development, HUD No. 15-001)

**Low housing inventory**

A low housing inventory frequently gives home sellers the advantage, since it often leads to an increase in housing prices. While inventory does vary by location, total unsold inventory was on the lower end, with a 4.6-month available supply. (Source: National Association of Realtors, News Release, April 2015)

**Buying a home is more affordable than renting**

According to Trulia's Rent vs. Buy Index, it was cheaper to buy a home than to rent one in all of the nation's largest 100 cities in late 2014. And nationwide, owning was 38% less expensive than renting, although the gap varied widely by location. (Source: Trulia.com, Rent vs. Buy Index, October 2014)

**Millennials are entering the market**

Despite living with high student debt and a tepid job market, millennials are finally entering the real estate market. In fact, adults age 34 and younger made up the largest percentage of home buyers in 2014, accounting for 32% of all home purchases nationwide. (Source: National Association of Realtors, Home Buyer and Seller Generational Trends study, 2015)

Of course, this doesn't mean that all millennials are buying homes. Those with the highest student loan debt may have trouble meeting the debt-to-income ratios required by lenders for a mortgage. Others are postponing starting a family, which affects their urgency to purchase a home.

*Do you and your employees know what to do following a disaster to minimize business disruption? When it comes to disaster planning, ensuring you have proper insurance coverage may be just the beginning.*

# Why Businesses Need a Disaster Preparedness Program

According to the Insurance Information Institute, 119 natural disasters occurred in the United States in 2014, totaling $25 billion in losses. But natural disasters represent just a portion of the crises that your business could face. Although you may not be located in an area prone to hurricanes, blizzards, tornadoes, floods, earthquakes, mudslides, and wildfires, you still need to consider the potential for power outages, civil unrest, terrorism (including cyberterrorism), fire, data breaches, and illness epidemics. What risks and hazards might your business face?

Approximately 40% to 60% of small businesses never recover from a disaster, reports preparemybusiness.org, a website created by the Small Business Administration (SBA) and Agility Recovery, an organization that helps businesses prepare for disasters and manage emergencies when they strike. For this reason, it is in the best interest of every business to identify potential risks and develop a plan to address them—before a crisis hits. Fortunately, many resources are available to assist business owners in developing a disaster preparedness program.

**Where to start**

Following are five steps that will help you create a disaster preparedness program, as outlined by ready.gov, a national public service campaign designed to educate Americans about preparing for and responding to natural and man-made disasters.

**Step 1: Program Management.** Although there are often minimum regulations that govern how certain businesses manage risk, as a business owner you will need to determine whether the minimums are enough. As ready.gov states, “Many risks cannot be insured, so a preparedness program may be the only means of managing those risks.” Management commitment to a preparedness program, as well as a written preparedness policy and oversight committee, may be critical to ensuring your business’s longevity.

**Step 2: Planning.** This step should include the creation of a “risk assessment” that identifies all potential risks and hazards for your business, with ideas for mitigating their impacts. It should highlight threats and hazards that are considered “probable,” as well as any that could cause injury, property damage, business disruption, or environmental impact. Another critical document is the “business impact analysis,” which details sensitive or critical processes, as well as the financial and operational impacts that would occur due to disruption of those processes.

**Step 3: Implementation.** In this step, committee members identify and assess resources, draft written plans, develop a system to manage incidents, and train employees as needed. Several key documents contribute to successful program implementation, including crisis communications, emergency response, and business continuity plans.

**Step 4: Testing & Exercises.** In order to evaluate the program’s effectiveness, including the success of employee training, management should run tests and drills to see what works and note opportunities for improvement.

**Step 5: Program Improvement.** During testing or an actual incident, weaknesses in the program are likely to be revealed. They should be documented, along with lessons learned and strategies for addressing such problems in the future.

**Other resources**

The Small Business Administration (sba.gov) offers a number of resources designed to help small businesses shore up their emergency preparedness, including links to templates and worksheets that will help you gather the data you need to put together the various written documents. At this website, you can also find links to information about the SBA’s own “Disaster Preparedness and Recovery Plan,” which provides details on assistance the SBA offers after a disaster strikes.

American Red Cross Ready Rating™ (readyrating.org) is a self-guided online program designed to help member businesses, organizations, and schools assess their level of emergency preparedness. The core of the program is a 123-point self-assessment that is used to gauge one’s level of preparedness. Members also have access to a variety of online tools and resources to help create and refine a disaster preparedness plan.

At preparemybusiness.org, the site mentioned above, business owners will find downloadable educational information, an archive of helpful webinars, and links to many of the other resources mentioned here.

Finally, the Insurance Institute for Business & Home Safety (disastersafety.org) offers a variety of resources, including research reports and an online tool that allows you to enter your Zip code and receive information about specific risks in your area.

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## What is the Roth IRA five-year rule?

Actually, there are *two* five-year rules you need to know about. The first five-year rule determines when you can begin receiving tax-free qualified distributions from your Roth IRA. Withdrawals from your Roth IRA—including both your contributions and any investment earnings—are completely tax and penalty free if you satisfy a five-year holding period *and* one of the following also applies:

- You've reached age 59 ½ by the time of the withdrawal
- The withdrawal is made due to a qualifying disability
- The withdrawal is made for first-time homebuyer expenses ($10,000 lifetime limit)
- The withdrawal is made by your beneficiary or estate after your death

This five-year holding period begins on January 1 of the tax year for which you made your first contribution (regular or rollover) to any Roth IRA you own. For example, if you make your first Roth IRA contribution in March 2015 and designate it as a 2014 contribution, your five-year holding period begins on January 1, 2014 (and ends on December 31, 2018). You have only one five-year holding period for determining whether distributions from any Roth IRA you own are tax-free qualified distributions (Roth IRAs you *inherit* are subject to different rules).

The second five-year rule is a little more complicated. When you convert a traditional IRA to a Roth IRA, the amount you convert (except for any after-tax contributions you've made) is subject to income tax at the time of conversion. However, your conversion isn't subject to the 10% early distribution penalty, even if you haven't yet reached age 59 ½.

But what the IRS giveth it can also taketh away. If you withdraw any portion of your taxable conversion within five years, you'll have to pay the 10% early distribution penalty on those funds that you previously avoided—unless you've reached age 59 ½ or qualify for another exemption from the penalty tax. This five-year holding period starts on January 1 of the year you convert your traditional IRA to a Roth IRA. And if you have more than one conversion, each will have its own separate five-year holding period for this purpose.

## What is the Roth 401(k) five-year rule?

The Roth 401(k) five-year rule determines when you can begin receiving tax-free qualified distributions from your 401(k) plan Roth account. While its similar to the five-year rule that applies to Roth IRAs, there are important differences.

Withdrawals from your Roth 401(k) plan account—including both your contributions and any investment earnings—are completely tax and penalty free if you satisfy a five-year holding period *and* one of the following also applies:

- You've reached age 59 ½
- You have a qualifying disability, or
- The withdrawal is made by your beneficiary or estate after your death

The five-year holding period begins on the first day of the calendar year in which you make your first Roth 401(k) contribution (regular or rollover) to the plan. For example, if you make your first Roth contribution to your company's 401(k) plan in December 2015, your five-year holding period begins on January 1, 2015, and ends on December 31, 2019. If you participate in 401(k) plans maintained by different employers, your five-year holding period is determined separately for each plan. But there's an important exception. If you make a direct rollover of Roth dollars from your prior employer's plan to your new employer's plan, your five-year holding period for the new plan will be deemed to start with the year you made your first Roth contribution to the prior plan.

For example, Beth made Roth contributions to the Acme 401(k) plan beginning in 2011. In 2015, she changed jobs and began making Roth contributions to the Beacon 401(k) plan. Her five-year holding period for the Acme plan began on January 1, 2011, and ends on December 31, 2015. Her five-year holding period for the Beacon plan began on January 1, 2015, and ends on December 31, 2019. In 2015, Beth decides to make a direct rollover of her Acme Roth account to Beacon's 401(k) plan. Because of the rollover, Beth's January 1, 2011, starting date at Acme will carry over to the Beacon plan, and any distributions she receives from her Beacon Roth account after 2015 (rather than 2018) will be tax free (assuming she's at least 59 ½ or disabled at the time of distribution).