Market Update

June 30, 2015

During the second calendar quarter of 2015 market indices provided small negative returns. The S&P 500 was down 0.4%, the Dow Jones Index was down 0.9%, mid-cap stocks were down 1.2%, small cap stocks were down 0.6%, international developed markets were down 1.1% and international emerging markets were down 1.3%. NASDAQ, with its blend of large and small cap stocks and with a greater exposure to the Technology sector, was up 1.8%. All in all, nothing to get excited about.

U.S. real Gross Domestic Product surprised most by contracting during the first quarter. However, recent reviews of the seasonal adjustment mechanisms used by the government seem to be skewed towards reducing early year economic data and inflating later quarters. This same pattern was observed in 2014, however the Bureau of Labor Statistics promised that a new set of seasonal adjustments would be released this July. These revisions will probably provide smoother estimates of quarterly economic activity but the end result will most likely show 2015 as another year of 2.0-2.5% real growth in U.S. GDP.

Interest rates rose modestly during the second quarter with the ten year U.S. Treasury Note yielding 2.4% on June 30. Initially, rates rose in anticipation of an increase in the Federal Funds rate of 0.25%. The Federal Reserve decided to defer that increase based on relatively weak economic data. At present, market participants are divided roughly 50/50 between those who expect a rate increase in September and those who expect a rate increase in December.

For the third time in the past five years, the European Union is dealing with a debt crisis with Greece. However, over the past five years much of that country's $270 billion in debt has been transferred from the European banks to the European Central Bank and the International Monetary Fund. Consequently, the danger to the European banking system is greatly diminished and the European Union is taking a much tougher stance during these negotiations. If Greece decides to leave the Euro and return to the Drachma, the ensuing devaluation and explosive increase in inflation would be cataclysmic to Greece, but of only moderate impact to its creditors.

Corporate earnings, excluding the energy sector, appear to be reasonably good for U.S. based companies. U.S. employment figures are positive, inflation is running at less than a 1% rate, and the federal budget deficit is stable, in short a continuing lukewarm recovery.

We anticipate the economy and the stock market will improve during the second half of the year and we believe equities will fare better than bonds.

Raymond A. Beplat, CFA
Chief Investment Officer