November 17, 2015

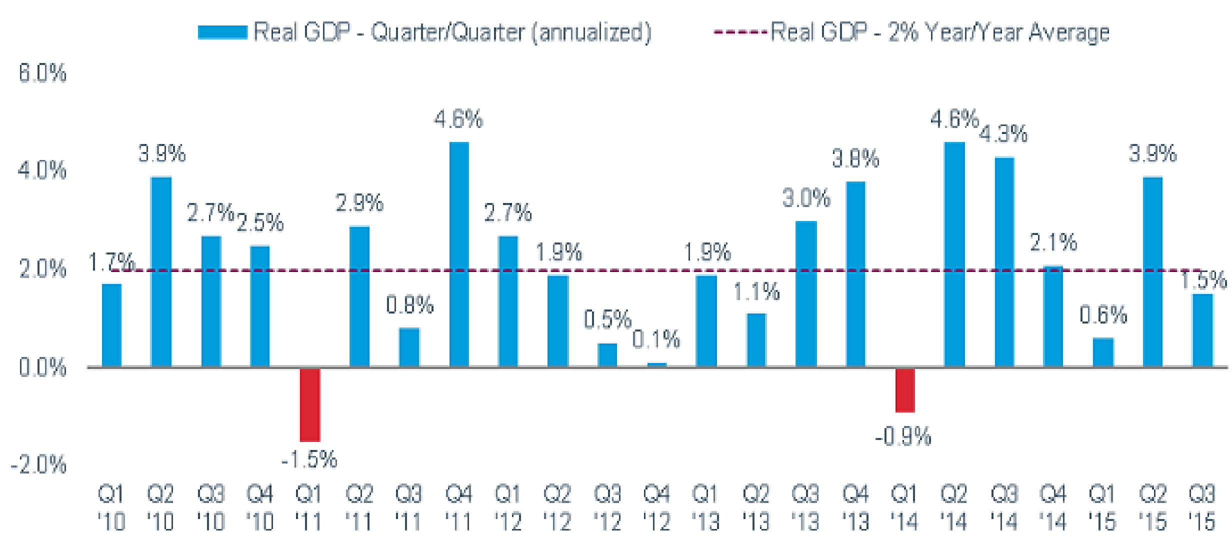
Market Insight: Inside the Chart Room…

As the world continues to swirl with uncertainty, it is appropriate to step into the chart room to refresh our perspective on the global economy and evaluate the financial footings. This edition of Market Insight is chalk full of charts covering key economic drivers, valuation, and performance. For those who enjoy pictures, it is a feast for the eyes. For those who don't like charts, here are the main themes:

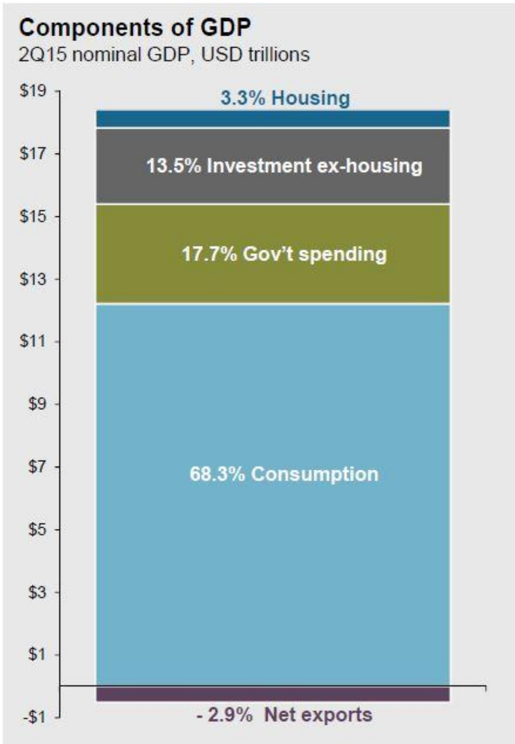
- Global Growth is modest but solid with manufacturing weak and consumption strong.
- 3rd Quarter earnings growth declined due to huge weakness in the energy sector and rising dollar. Both negative factors are likely to recede and will allow earnings to grow in upper single digits next year.
- Equity valuations are near their ten year average but remain cheap compared to level of interest rates.
- Market performance has been sporadic with volatility high and rapid leadership rotation across all asset sectors. Anticipation of Fed rate hike remains a stumbling block.
- Near term neutral view on market. Long term, stocks are still the best game in town, and should slowly grind higher.

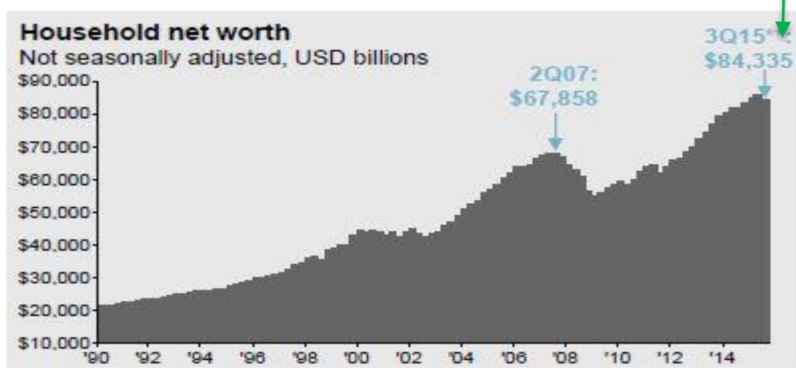
All charts below are from JPMorgan's Guide to the Markets unless otherwise noted.

Economy: **US economic growth is modest but solid:**
Since the end of the Great Recession, real GDP growth (net of inflation) has been volatile on a quarter-to-quarter basis, but has averaged exactly 2%. Long-run projections released at the FOMC's October meeting forecast both real GDP and inflation should average around 2%.

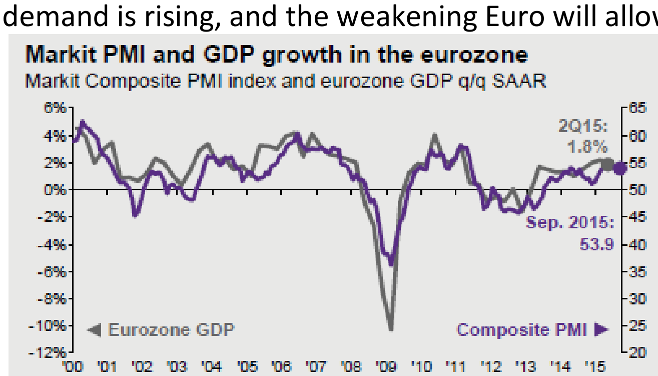


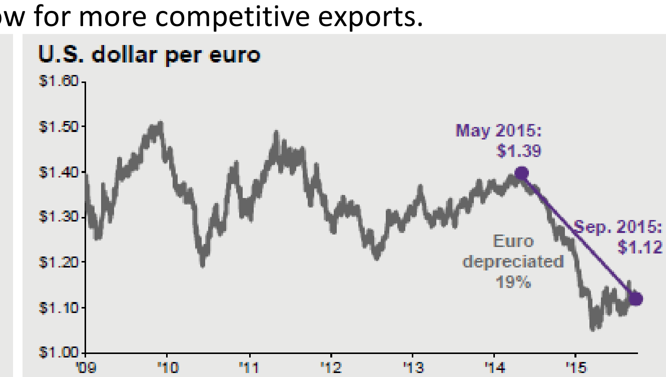
Consumption is the key driver of the US economy. Good news: Consumer's balance sheets have improved significantly. The debt service ratio is the lowest in 35yrs and net worth has now eclipsed the pre-recession high in 2007.

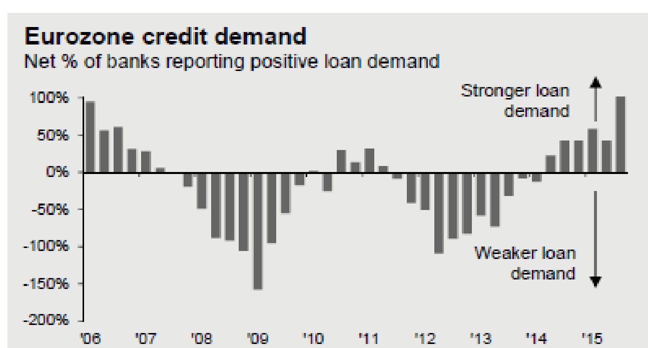




Europe growth continues to improve: GDP has risen to near 2%; Unemployment is falling; Credit demand is rising, and the weakening Euro will allow for more competitive exports.

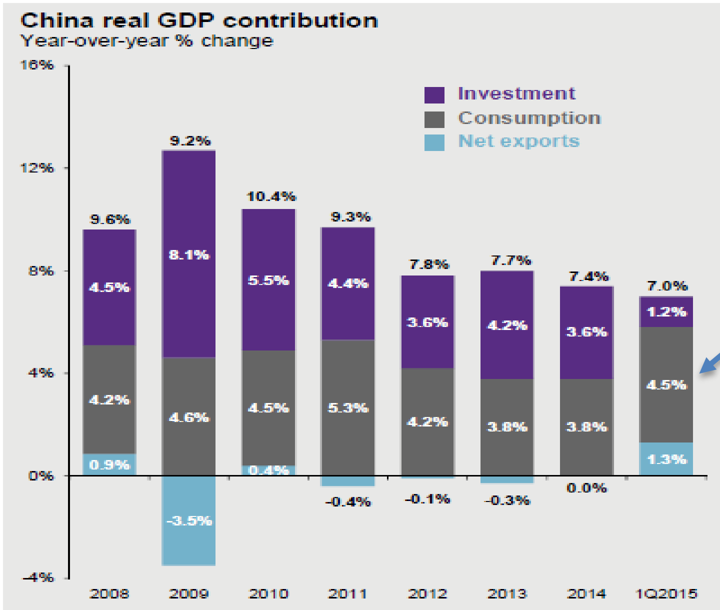






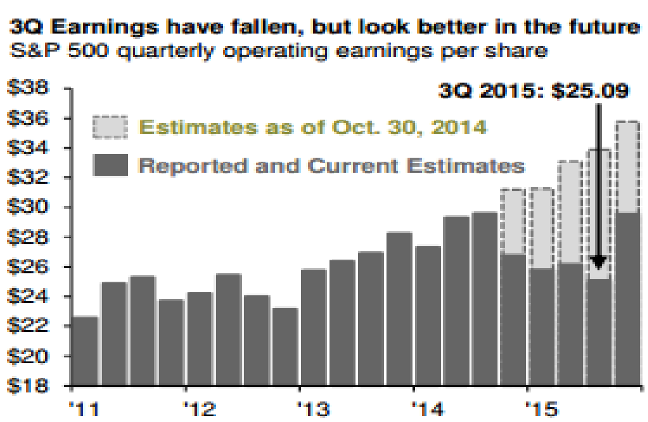
Source: FactSet, J.P. Morgan Asset Management, (Top left) Markit, (Top and bottom left) Eurostat, (Bottom right) ECB.
Guide to the Markets – U.S. Data are as of September 30, 2015.

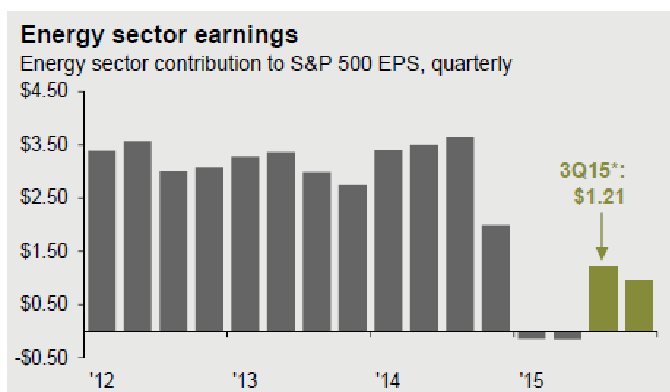
China's growth is slower but healthier as the composition of growth is changing from a government led to a consumption and export led economy. This is good news because growth will now be organic (real). As the rural population migrates into the suburbs, growth will be more stable and predictable.

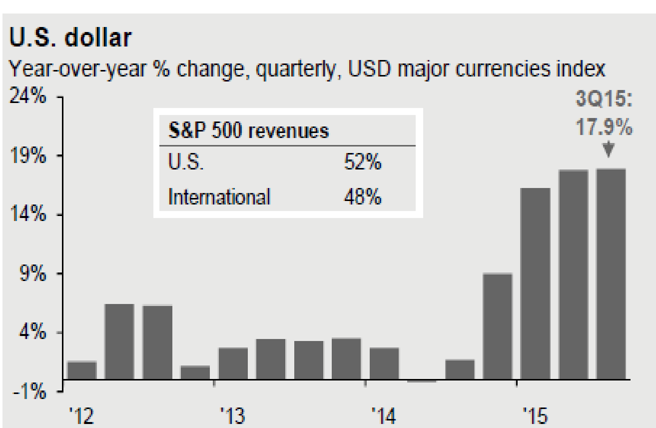


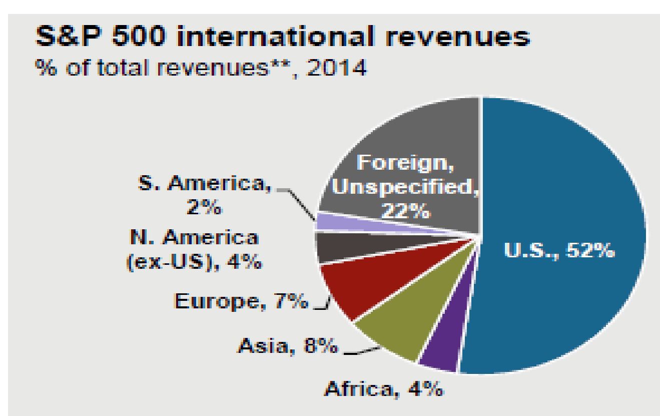
Consumption is main driver of growth

US Earnings: Third quarter earnings fell 15%yoy but rose 1.8% ex-energy. The rise in the dollar and fall in the energy sector earnings has been a major drag on S&P earnings. 48% of the total earnings of the S&P500 companies are generated outside the US.









Valuation remains at or below historical average with the **Growth sector** the cheapest.

Current P/E vs. 20-year avg. P/E

	Value	Blend	Growth
Large	13.9 / 14.2	15.1 / 17.1	17.2 / 21.1
Mid	15.3 / 14.4	16.7 / 16.7	18.4 / 22.1
Small	14.6 / 14.6	16.1 / 17.4	18.0 / 21.6

Current P/E as % of 20-year avg. P/E

	Value	Blend	Growth
Large	97.9%	88.1%	81.3%
Mid	105.8%	100.0%	83.3%
Small	100.2%	92.5%	83.3%

Performance: Every sector was hit hard in the 3rd quarter but there still remains a huge discrepancy in performance on a year-to-date basis between the **Value** and **Growth** sectors.

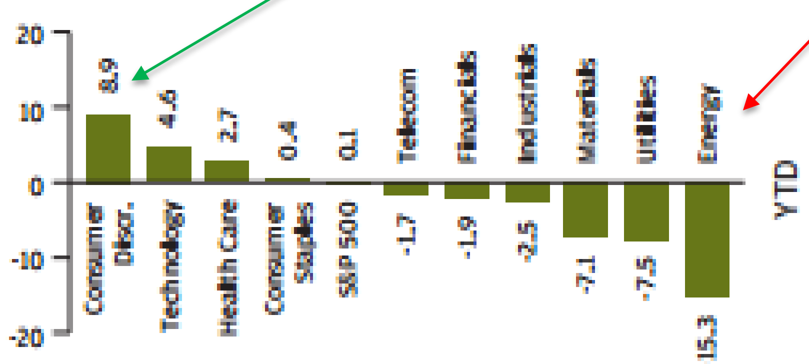
3Q 2015

	Value	Blend	Growth
Large	-8.4%	-6.4%	-5.3%
Mid	-8.0%	-8.0%	-8.0%
Small	-10.7%	-11.9%	-13.1%

% Year-to- Date (YTD)

	V	B	G
L	-4.3	0.1	3.9
M	-4.9	-3.0	-1.3
S	-6.4	-3.8	-1.1

Wide dispersion in sector returns for the year. Consumer Discretionary +8.0% verse Energy -15.5%**.**



High volatility is reflected in rapid rotation across asset sectors:

The chart below is often called the "**Quilt Chart"** and ranks each asset sector performance by month. This year has seen particularly high rotation of market leadership. For example, black line follows the Small Cap sector (bright blue box below) and shows how it has moved from low in January to high in May and June and back to low in September. <u>Net, this is a picture of a very unsettled market.</u>

Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sept	YTD*
REITs 6.8%	Commodities 6.5%	REITs 1.7%	Commodities 11.1%	US SmCap 2.3%	US SmCap 0.7%	REITs 5.6%	Int'l Dev Bonds 0.4%	REITs 3.0%	Core US Bonds 1.1%
Core US Bonds 2.1%	Int'l Dev 6.0%	US SmCap 1.7%	EM 7.7%	US Lg Cap [illegible].3%	Int'l Dev Bonds 0.1%	US Lg Cap 2.1%	Commodities 0.3%	Core US Bonds 0.7%	EM Bonds 0.3%
High Yld Bonds 0.7%	US SmCap 5.9%	EM Bonds 0.6%	Int'l Dev 4.1%	High Yld Bonds 0.3%	Commodities -0.1%	Int'l Dev 2.1%	Core US Bonds -0.1%	Int'l Dev Bonds 0.4%	High Yld Bonds -2.5%
EM 0.6%	EM 3.1%	Core US Bonds 0.5%	Int'l Dev Bonds 2.2%	EM Bonds 0.1%	Core US Bonds -1.1%	Core US Bonds 0.7%	EM Bonds -1.3%	EM Bonds -1.3%	REITs -4.3%
EM Bonds 0.5%	High Yld Bonds 2.4%	High Yld Bonds -0.5%	EM Bonds 1.8%	Core US Bonds -0.2%	EM Bonds -1.4%	EM Bonds 0.1%	High Yld Bonds -1.7%	US Lg Cap -2.5%	Int'l Dev Bonds -4.8%
Int'l Dev 0.5%	EM Bonds 1.2%	EM -1.4%	High Yld Bonds 1.2%	REITs -0.3%	High Yld Bonds -1.5%	Int'l Dev Bonds -0.1%	US Lg Cap -6.0%	High Yld Bonds -2.6%	Int'l Dev -5.3%
Int'l Dev Bonds -1.8%	Int'l Dev Bonds -0.8%	Int'l Dev -1.5%	US Lg Cap 1.0%	Int'l Dev -0.5%	US Lg Cap -1.9%	High Yld Bonds 0.6%	REITs -6.2%	EM -3.0%	US Lg Cap -5.3%
US Lg Cap -3.0%	Core US Bonds -0.9%	US Lg Cap -1.6%	Core US Bonds -[illegible].4%	Commodities -2.0%	EM -2.6%	US SmCap -1.2%	US SmCap -6.3%	US SmCap -4.9%	US SmCap -7.7%
US SmCap -3.2%	REITs -3.6%	Int'l Dev Bonds -2.1%	US SmCap -2.6%	Int'l Dev Bonds -3.0%	Int'l Dev -2.8%	EM -6.9%	Int'l Dev -7.4%	Int'l Dev -5.1%	EM -15.5%
Commodities -7.5%	US Lg Cap -5.8%	Commodities -6.8%	REITs -5.9%	EM -4.0%	REITs -4.6%	Commodities -14.1%	EM -9.0%	Commodities -6.3%	Commodities -19.5%

Source: Charles Schwab

Summary: The continued solid U.S. consumer spending, improvement in the European economy and stabilization in emerging markets are positive footings for equities. The negative effects of weak energy and strong dollar should wane in the year to come. However, political and monetary uncertainty around the globe is a drain on investor confidence and will continue to provoke market volatility**. Net, earnings growth should resume in the year to come, attaining upper single digits and which in turn should provide the impetus for stocks to resume their grind higher.**

Investment Strategy: In equities, there has been a small shift from Value to Growth. However, the portfolios remain broadly diversified to ride through the market volatility and to realize growth.

THANKSGIVING: I am thankful for the gift of freedom and to live in this magnificent country! May you and your family enjoy the many, many blessings of this THANKSGIVING!

Kind Regards,

Barbara

Barbara HS Huff

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