SELECTOR
Real-Time Money Management

Monthly Commentary

April 17, 2013

"Good investors gather information, put that information into current and historical context, then make sound decisions."

It has been a good year for equity markets so far. We are now experiencing just the second correction in fifteen weeks. The first correction was a very brief 2% pullback the end of February. It was over as quickly as it started, being totally contained in a single week. Our current equity market correction started on Tax Day, the 15th, and was accelerated by the atrocious attack during the Boston Marathon. We are still in the 'cone of confusion' but will know in short order how much further markets will exhale. But at this writing, equity markets are enjoying a very good year.

Bond markets have been relatively quiet in 2013, with only minor price movements. This is significant because in such a low interest rate environment, price can be a major contributor to total returns, such as we saw in 2012. When price fluctuations are removed from the equation, bonds have to rely more heavily on either their interest rate or their ties to the equity markets, which can be seen in high yield and convertible bonds. The majority of capital flows this year have not been into the bond markets, but into the burgeoning equity markets.

As good as equity markets have been, gold has stolen the spotlight with its largest single day plunge (-10%) in thirty years on Monday. Gold plays many roles in our society and in our investment community. Most obvious is its role in the jewelry world. Jewelry is the most common way gold reaches consumers and approximately 78% of gold consumed each year is made into jewelry. India has the greatest demand for gold jewelry, consuming 27% of world demand, followed by China at 26%. The U.S. consumes about 5% of the world's gold jewelry demand. In the financial world, gold takes on a different role and is generally regarded as a hedge against traditional financial investment vehicles. Some feel that foreign governments such as Japan or China may be involved with gold's decline, as they seek to manipulate their own currencies. But the fact remains that gold prices are under severe pressure.

Working our way back to equity markets, the best performances of the year thus far are being seen in the health care sector. The utilities sector is also putting up good numbers and retaining strong technical pictures. Both of these sectors are generally regarded as defensive in nature, which is beginning to characterize the equity market advances seen to date. Large cap equities have a definite edge on the mid cap and small cap equity sectors. Earlier in the year the advance had been quite broad, however we are now seeing more definition and separation between these cap weighted equity sectors. While it is not uncommon to see more defensive sectors and cap weights in the lead for short periods of time, this is not the type of action we normally see over extended periods of time. This means that either we will have to be more patient for the leadership to broaden once again, or that markets are in the midst of a transition.

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Either way, more data is required to develop either scenario and we remain diligently attentive to the potential outcomes. It is still early in the year, and there is no calendar pressure. With the declines in gold and the flat affect in bonds, equity markets seem to be a logical landing place for new capital, with domestic equity markets holding a clear advantage over international equities. That being said, we have already seen very nice gains year-to-date and there is certainly room for equity markets to continue to exhale and extend our current short-term correction. Increasing performance separation between the primary equity market sectors also creates opportunities for additional sector rotation.

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Sources: Bloomberg, iShares.com, Marketwatch.com, Stock Trader's Almanac 2012, StockCharts.com.