SELECTOR
Real-Time Money Management

Monthly Commentary

March 17, 2015

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

This equity market is acting a lot like Nebraska weather… no matter what's going on right now, wait a week and you will be see the opposite extreme. We have had nine trend reversals in fourteen weeks averaging almost 93 points per reversal! Yet today the S&P 500 closed at 2074.28, 5.19 points lower than the December high of 2079.47. It has been a world-class, theme park rollercoaster ride. I have a couple of grandsons that love that kind of action, but most of us old-timers don't care for them one bit.

The redeeming factor is that during its February climb, the S&P 500 broke into new territory. A number of other domestic equity indexes, especially the growth style indexes, also went to new highs. It would have been nice if they had spent a little more time up there before correcting again, but this is the pattern that we are seeing thus far. I am calling it an accordion correction because that's how it looks on the charts. It's hard to be too critical because we are inching in the right direction, and the charts look much better than they did last October. The long-term trend is still distinctly positive.

Another positive development is that international equities have been breaking six to eight month downtrends. These breaks have not gone unnoticed by institutional investors who have been shifting significant capital allocations into selected international sectors, especially Europe. This effectively broadens the global landscape for equities, including domestic companies who do a lot of worldwide business. Emerging markets equities continue to lag as they remain captive to the very weak commodities markets. But international market action is definitely expanding.

Last month we discussed the sharp pullback in the utilities and real estate sectors. Initially, these pullbacks were consistent with a general institutional rebalancing, however they failed to adjust even when major equity markets began their own contraction within 'the accordion correction.' As a result, we received confirmed sell signals from both of these sectors in March. Real estate securities had been included in our portfolios long enough and were profitable enough to present us with very acceptable exits. Utilities were added during the fourth quarter of 2014 and presented smaller gains. Both had been useful, but it was obvious institutional attention was being focused elsewhere. Another persistent problem with the utilities and real estate sectors stemmed from their association as being interest-rate sensitive. The Federal Reserve has continued to be patient with the economy's slow growth and low inflation (thank you, oil prices), but institutional investors may have chosen to step back from these sectors earlier rather than later.

Speaking of interest rates, the star that continues to command all of the spotlight is the U.S. Dollar. Its strength continues to impress, as it effectively broke a downtrend that had extended all the way back to 2001/2002. The last remnant of that negative trend was soundly broken in the fourth quarter of 2014. While some economists have been lamenting the U.S. Dollar's rise, the reality is that its time has come and there is plenty of room for an advance that could extend for several years. In our opinion, betting against the U.S. Dollar at this juncture is foolhardy. And the best way to put your money on the U.S. Dollar is in U.S. stocks and bonds. There are even sophisticated methods to hedge the U.S. Dollar's strength with international equities that are attracting considerable attention.

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Accordingly, domestic bonds continue to represent dependable havens at this juncture. The question marks remain as to how they will adjust if/when interest rates rise and by how much. It is certainly no secret that everyone is tired of earning nothing on money markets and short term bonds. It's not in the Federal Reserves' long-term interest to continue to artificially suppress short-term rates, if you can pardon the pun. Intermediate and long term interest rates are not too far from their 'model' and we would be surprised to see dramatic impacts on these markets when the Federal Reserve readjusts their focus. Of course, it would be best if they didn't wait too long so it would appear that they were being responsible rather than reactive. Thankfully, that's not our job. Our job is to pay attention, and be responsive.

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Sources: Bloomberg, Marketwatch.com, StockCharts.com