CEP FINANCIAL

INVESTMENT NEWSLETTER

CEP FINANCIAL, LLC March 31, 2016

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The overall US Equity Markets was up 1.2% for the 1st three months of 2016

Large Cap Stocks - +1%
Mid Cap Stocks - +2%
Small Cap Stocks - +1%

Foreign Stocks

Developed Economies - -4%
Emerging Markets - +5%

Fixed income interest rates continued to drift downward remaining at historically low levels.

Short/term rates – +0.01%
Long Term rates - +1.8%

Real Estate was up 5% for the quarter.

Commodities reversed their dramatic decline to finish up 5% for the quarter.

The Investment Letter is mailed periodically to our clients and friends. This letter was prepared from material provided by Bob Veres , Morningstar, The Wall Street Journal, and other sources that we believe to be reliable).

1st Quarter 2016: Bumpy Ride But It Ended Better Than It Started.

The first quarter of the new year has brought us small positive returns in many of the U.S. market indices, which means that investors survived—for now, at least—the worst start to a calendar year ever for the U.S. stock market.

US Equity Markets Summary

The Wilshire 5000 Total Market Index--the broadest measure of U.S. stocks and bonds—was up 1.2% for the first three months of 2016. Considering that the index was down more than 10% by the second week of February, a small gain feels pretty good. . The comparable Russell 3000 index has gained 1.0% so far this year.

Large Companies-
The Wilshire U.S. Large Cap index gained 1.3% in the first three months of 2016. The Russell 1000 large-cap index was up 1.2%, while the widely-quoted S&P 500 index of large company stocks posted a gain of 0.8% in the first quarter of the year.

Midsize Companies - The Wilshire U.S. Mid-Cap index gained 2.2% for the quarter. The Russell Midcap Index was also up 2.2%.

Small Companies Small company stocks, as measured by the Wilshire U.S. Small-Cap index, gave investors a 0.9% return during the first three months of the year. The comparable Russell 2000 Small-Cap Index was down 1.5%, while the technology-heavy Nasdaq Composite Index lost 2.8% for the quarter.

Foreign Equity Markets

The markets of developed countries, other than the US, are not off to a good start. The broad-based EAFE index of companies in developed foreign economies lost 3.7% in dollar terms in the first quarter of the year, in part because Far Eastern stocks were down 6.1%. In aggregate, European stocks lost 3.2%, and are now down more than 10% over the past 12 months.

Emerging markets stocks of less developed countries, on the other hand, did much better, gaining 5.4% for the quarter.

Commodities and Real Estate

Real estate investments, as measured by the Wilshire U.S. REIT index, were up 5.2% for the first quarter. Commodities, as measured by the S&P GSCI index, gained 3.8% of their value in the first quarter, largely because of a modest 3.5% rise in oil prices since the end of last year.

Interest Rates

Meanwhile, interest rates have continued their downward drift, leading to gains in bond portfolios. Treasuries continue their long trend of paltry returns to investors; 3-month notes yielded 0.2% at the end of the quarter, while 12-month bonds were yielding just 0.6%. Go out to ten years, and you can get a 1.8% annual coupon yield.

Is there a way out of this low interest rate environment? Bill Gross thinks so. He told Barrons magazine:

The way out is a little bit of pain over a relatively long period of time…. It means raising interest rates and returning the savings function to normal. In today's world, normalization would mean a 2%, fed-funds rate, a 3.5% yield on the 10-year bond, and a 4.5% mortgage rate. He believes that the Fed will raise interest rates this year, as long as the stock market permits it. Would this create some pain? Of course. Housing prices probably would stop rising, and might fall a bit.

Outlook - Sort of Bearish

There was temptation at the beginning of the year to bail out of the markets. The markets were declining and many, perhaps most, analysts predicted the start of a painful, protracted bear market. Some analysts were talking openly about another 2008-9 drop in share prices. But 10% market declines are simply a part of the market's normal turbulence, and anyone who spooks as soon as they see a month of bearish sentiment is likely to miss out on the subsequent gains. Since hitting their 2016 lows on February 11, the S&P 500 index has gained roughly 13% in value.

That doesn't guarantee that there will be gains going forward, however. The Market Watch website reports that half of the S&P 500 sectors are reporting declines in earnings per share this quarter over the same period last year, and a poll by the FactSet analysts suggests that seven out of the ten sectors will end the earnings season reporting declining earnings.

Part of the wind at the backs of stocks this past six weeks has come, yet again, from the U.S. Federal Reserve Board, which had originally signaled that it planned to raise interest rates four times this year. After its most recent meeting, the Fed is projecting just two interest rate hikes this year, and Fed Chairwoman Janet Yellen has clearly indicated that the Fed will remain cautious about disrupting the markets or the economy as it unwinds its various QE initiatives.

Another tailwind was provided by the falling dollar. In the first three months of the year, the dollar's value against a basket of six major currencies fell 4.2%. A weaker dollar makes U.S. exports more price-competitive against goods and services sold in other currencies, potentially leading to higher top-line revenues for companies that do business overseas.