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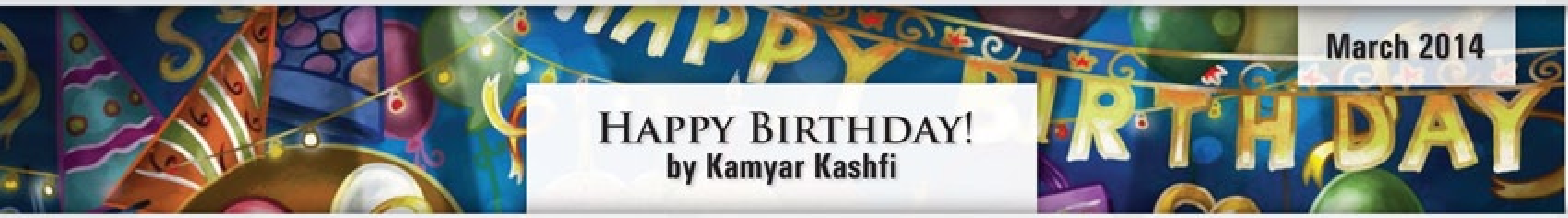
MONTHLY NEWSLETTER



March 2014

HAPPY BIRTHDAY!

by Kamyar Kashfi

On March 10th, this current bull market celebrated its fifth birthday. The S&P rose a cumulative 178% in price from 3/7/2009 through 3/7/2014 and is now 20% above its prior bull market peak. That was the second best bull market return since 1945. Of the 6 bull markets during that time that lived to see their fifth birthday, 3 lived to see their 6th birthday with an average price gain of 26%.[1] When will this bull market end? What will derail it? Will it be the weather? Will it be the next crisis in Crimea? Will it simply be earnings? The answer is not an easy one and a subject of much debate. While it is difficult to predict what will cause a meltdown, it is useful to look at the positive things that are occurring in order to gauge whether or not you believe things are getting worse or maybe even getting better. If things are getting better, the bull market has a better chance to endure.

On the technical front, you would be hard pressed to find a major index that is not currently biased to the upside. The Dow 30, S&P 500, the Wilshire 5000 and the Nasdaq Composite have all broken out to the upside or on the cusp of breaking out to the upside after some recent selling and consolidation.[2] Neither the recent cold weather or recent crisis in Crimea have had an enduring effect on the market. One could argue as the weather warms and this latest crisis abates, any short term effects on markets or productivity and earnings will soon reverse themselves.[3] As markets break out to the upside, often new highs beget new highs. Before I would worry too much about declining prices or worse yet a bear market, I would say that the market would first need to experience a full-fledged 10% correction. At present, this is not happening. Bull markets have endured many corrections and they have often been viewed as a healthy point of price consolidation which can set the stage for further gains. Before you have a new bear market, quantified as a decline of 20%, you must first have a correction. At present, I would say that technically speaking it's a bit early to start worrying about when this bull market will end and the bias is still to the upside. Declines can and do happen but until the technical damage is done, it can be a very expensive habit trying to outguess the market. The trend is often your friend. That being said, a prudent investor should always assess gains and losses, perhaps take profits, rebalance and reallocate. This is a proactive approach rather than a reactive one. With so many stocks doing so well, selling winners and reinvesting in potential overlooked opportunities can help mitigate losses. Selling high flyers and buying things that haven't left the ground yet can leave a portfolio with a shorter distance to fall.

Fundamentally, as we approach the end of the current earnings season, 64% of S&P 500 companies have beat earnings estimates. This compares favorably to the 62% average. S&P 500 earnings are on track for another record quarter.[4] Recent events in Crimea and unusually cold weather have led to some declines in earnings projections for 2014 as well as some hints of slowdown in economic reports. If projections come down further, expectations and confidence may also decline and investors may begin selling. I believe that investors will first wait and see if these short term factors are causing recent weakness in economic reports or if there is something more meaningful behind the slowdown. Stock prices appear to be giving the market the benefit of the doubt. That being said, with a current P/E multiple of 17.26, investors might become cautious as the market P/E approaches 20. P/Es greater than 20 have often signaled markets that are priced to perfection. The economy does appear to be improving along with housing and unemployment. If earnings rise, then a further rise in prices can indeed be justified.

Will this bull market live to see its 6th birthday? Obviously only time will tell. Things do seem to be improving. While there are always things to worry about, many investors are only still getting over the hangover of the last financial crisis in 2008. Diversification and periodic rebalancing are a powerful means by which to prepare for the end of this bull run. Let's review your portfolio and take a proactive approach.

1. http://advisor.marketscope.com/SP/msa/index.html
2. http://stockcharts.com/freecharts/candleglance.html?[MARKO]
3. http://advisor.marketscope.com/SP/msa/index.html#historyId0
4. http://advisor.marketscope/SP/msa/index.html

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