Chapel Hill Investment Analysts, Inc.

"Cup of Joe"

A lot has happened since our last email blast. If you have been watching TV or listening to the radio, the focus has been on a couple key items – noticeably interest rates; oil; Europe and the rapid rise of the dollar. The goal, as always, is to inform our clients of any pertinent portfolio moves and to shed light on which direction we feel the market is headed.

First, the most significant discussions relate to interest rates and when the FED will start to tighten their monetary policy. In other words, when the Federal Reserve feels that the economy is on solid footing and hitting certain data points (wage growth, inflation, etc.), they will begin to raise rates. Remember, this is good news! The FED will not do this until they feel confident that the "training wheels" can come off and our economy can grow on its own. Our opinion is that the FED will remain cautious and accommodative in deciding when to raise these rates. Regardless, when they decide to do this, volatility will follow. The market does NOT like change! However, keep in mind that when rates rise, bonds will lose money, creating a big reason why equities are still the way to go. Stocks continue to look like the only game in town.

Another popular topic of discussion has been oil, which remains at depressed levels. In the long term, this is great news! However, due to the increased emergence of energy firms in the S&P, as oil currently remains low, so does the market. We feel that once the oil market has reached equilibrium, these companies will start to rebound and the market will start to realize that the consumer is benefitting tremendously from saving money at the pump. With the consumer making up over 70% of the GDP, this is GREAT news! A number of experts have said they believe oil will never again reach $100 per barrel. If this is true, it will provide a permanent boost to growth for the entire world, and especially to the nations that import oil (India, Japan, Europe, etc.).

Lastly, we want to touch on both Europe and Japan, along with the rise of the dollar and decline of the Euro and Yen. As discussed in the previous email blast, Europe has embraced quantitative easing, or monetary stimulus! This entails injecting money into the economy by purchasing bonds, which in turn drive down the price of the Euro, decrease interest rates, and make European exports more appetizing (cheaper goods for the US). Interest rates in Europe are currently negative, meaning banks are now charging their depositors interest to hold their money. This forces consumers to spend their money instead of hoarding it in banks in a desperate attempt to fight deflation. Japan has also been implementing the "3-arrow approach" to boost their economy by injecting money, lowering rates, and devaluing their currency to make their exports more attractive. The only bad news to come from this is the emergence of currency wars. When the U.S. raises rates (tightens), the price of the dollar will rise even more, creating a headwind for U.S. multi-national companies relying on selling products overseas. The foreign exchange imbalance is one reason experts are encouraging the FED to hold off raising rates so the U.S. won't feel a significant impact to our economy.

The great news for you, our client, is that your portfolios are extremely well-diversified and have been exposed to Europe and Japan for quite a while now. We just rebalanced the portfolios and increased our exposure to the areas where we see the most growth in the future. Moving forward, we feel that the U.S. will continue to grow at a steady pace (with some volatility) in the early part of the year. Europe and Japan should continue to do well as a result of having the support of their respective central banks. Interest rates will rise, but only when the FED feels comfortable that we are on solid footing.

As always, thank you for reading our comments, as well as for your ongoing referrals and loyalty throughout the years. And remember - keep funding your 401(K), IRA and Pension Plan!

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