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FED-less

Markets provide glimpses and insight into the investor psyche when you watch them as much we do. Last week the headwinds created by higher interest rates and lower oil prices were strong enough keep stock markets from hitting new highs.

We are in one of the longest bull markets in history yet the crowd has ignored how actual economies are faring.

LONGEST STREAKS WITHOUT A 5% S&P 500 CORRECTION

Start Date	End Date	S&P 500 at Beginning	S&P 500 at End	S&P 500 Gain During Streak	Trading Days Without a 5% Correction
08/19/58	09/08/59	47.30	57.70	22.0%	266
01/04/61	01/09/62	58.36	69.15	18.5%	255
11/26/63	06/08/65	72.38	85.93	18.7%	386
10/12/92	03/28/94	407.44	460.00	12.9%	370
12/21/94	07/12/96	459.61	646.19	40.6%	394
06/28/16	07/11/17	2036.09	2425.53	19.1%	261

Source: LPL Research, FactSet 07/11/17

Logically, if markets are up, it would stand to reason that economies would have soared to new heights, wages would be higher than ever, business profits would be blossoming, and the middle class would have expanded. **Unfortunately, the reality just doesn't match up with the hype and that's when a combination of events – expected or unforeseen can swiftly and dramatically increase volatility.** We saw this in the past with the tech bubble, the housing bubble, and the debt bubble. Now, as in the past, during these periods of momentum and emotionalism, investors will herd into what is "hot," often with the assumption that they have entered a casino where everyone wins. This is what "bubble making" does to market psyches. **As unbelievable as it sounds, we are again at that moment today**.

In today's enormously unbalanced environment, is it safe to assume that stocks around the world will continue to go up forever without any consequence?

It may be tempting to put on the rose colored glasses, but it is important to not be swept away by the idea that stocks can go up forever from here.

Here is just one example of why we continue to advocate caution in this environment. An analysis of corporate earnings over the last five years tells us that earnings are barely keeping pace with inflation – with adjusted earnings averaging about 2% per year since 2012. They are essentially stagnating, even when using these optimistic adjusted earnings calculation methods, which allow companies to adjust for out-of-the-ordinary costs – opening a new plant, major infrastructure changes, etc. These adjusted earnings are what financial media – and the companies themselves – most often tout.

Even with earnings up only 2% per year for the last five years,
the stock market has risen 80% in the same period.

How can that be?

All that has occurred is that stocks have gone from 16x earnings to 23x earnings,
in effect driving stocks to all-time highs with some of the highest valuations in history,
not driven by profits, but rather by historically low levels of volatility and high levels of complacency .

And what will be the end result when the proverbial chickens come home to roost?

Even with such uncertainty, we are always watching and analyzing market conditions. As those conditions change and evolve, **we are looking to take advantage of opportunities as they arise**. Some may be short-term, while others may be longer-term, but all will be chosen carefully and with an eye toward safely growing principal. We are also careful **when** we tread, as occasionally the Federal Reserve sends out signals that they see some weakness in the markets. When this happens, we often see a short-term drop in rates, causing the market to celebrate, as happened on Wednesday the 12th of July. The party seldom lasts, though, as reality sets in and investors recognize that in signaling weakness, the Federal Reserve is confirming that conditions are not optimal and caution is advisable.

It is equally important to make sure that investment portfolios have an all-weather stance, in the event that interest rates temporarily drift higher. In our research, we test the whole of our portfolios for sensitivity to both interest rates and market declines. Other factors constantly come into play but for now these represent the two greatest risks. This year, we have integrated a series of bonds and mortgages to soften the blow of higher rates, while still offering good interest and upside potential, even with a rising stock market. It should be understood that there will be times when the highest quality bonds (i.e., treasuries, BBB corporate bonds, and GNMAs) will be chosen over yesterday's hot stocks. **The time will come when there is no longer a disconnect between fundamentals and fantasy**. It happened in 2000 prior to the S&P 500 losing 50% and it happened again in 2008 when the market lost more than 50%. The goal is to be prepared for that day of reckoning.

Economic data points are set to increase over the next few weeks as earnings season starts in earnest this week with the all-important balance sheets from big investment banking firms (Citigroup, JP Morgan and Wells Fargo) on Friday. It is very difficult to separate truth from fiction in a bank balance sheet but you can find nuggets of insight if you dig through them closely, as we do. At the same time we will also take hard looks at reports on Consumer Credit, Inflation, Inventories and Retail Sales.

As always, we will continue posting articles that we believe to be of great informational value on our website, under the "Great Articles" tab, which is linked here:

http://summitplan.com/cgi-bin/htmlos.cgi/great_articles.html.

Additionally, the "Summit Planning Financial Hour" will be live this week on Radio 570-WSYR at 10AM on Saturday. Don't forget to tune in for a recap of the week's events. If you cannot tune in, check out our radio show archive on our website at http://summitplan.com/cgi-bin/htmlos.cgi/radio_shows.html.

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6. The Dow Jones Industrial Average is comprised of 30 stocks that are major factors in their industries and widely held by individuals and institutional investors.
7. The Standard & Poor's 500 Index is a capitalization weighted index of 500 stocks designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries.
8. The NASDAQ Composite Index measures all NASDAQ domestic and non-U.S. based common stocks listed on The NASDAQ Stock Market. The market value, the last sale price multiplied by total shares outstanding, is calculated throughout the trading day, and is related to the total value of the Index.
9. The Russell 2000 Index is an unmanaged index generally representative of the 2,000 smallest companies in the Russell 3000 index, which represents approximately 10% of the total market capitalization of the Russell 3000 Index.
10. CBOE Volatility Index is a measure of the implied volatility of S&P 500 index options, calculated and published by the Chicago Board Options Exchange (CBOE).
11. The Dow Jones Industrial Average, the S&P 500, the NASDAQ, the Russell 2000 and the CBOE Volatility Index are unmanaged indexes which cannot be invested into directly.