Eideard Group
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Market Commentary *Spring 2014*

A Time to Reflect

Following what was an extraordinary year for equity returns in 2013, the natural inclination for many investors was to continue to pile in and to expect more of the same in 2014. For others of the more conservative persuasion, the first four months of 2014 was a perfect time to reflect on last year's surprise growth in their stock portfolios and to be equally appreciative, perhaps even respectful of the market's current respite. There are several reasons to reflect positively. First, S&P earnings grew by just over ten percent last year but the market gave us thirty percent, so we've got to be thankful. Second, no one was prescient enough to have called 2013's outsized gains, so it truly was a surprise. And finally, despite a rough start to 2014, the market recovered and through April has largely preserved its rather lofty levels despite adding another four months to an already mature five year bull run.

We remember the parting words we authored in our January commentary following the market's torrid pace last December: "We hope the stock market will level off for a bit or in the worst case it takes a modest dip on the front end of the year. This should allow an expanding economy the chance to catch up." So far, that early prognosis has rung true.

You'll also remember that last year our principal concern was the fifty-five or so new stock market highs and, arguably, the lofty valuations that had accompanied them through year-end. We opined at length on corporate America's top line revenues and earnings growth rates, both of which had begun to moderate from their historic peaks despite increasing valuations. Notwithstanding the lack of current media attention, and already a third into this new year, we have experienced very little change in valuations. Hence, the current trading range should be considered fortuitous and what is needed to mitigate an unwanted correction and otherwise sustain the market's longer run health.

Ok, so while the market seems to be range bound, how is the economy doing on catching up? To that question, we can either cite the arsenal of weekly and monthly published statistics or we can simply focus on the most recent indications offered by the US Citi Economic Surprise index. This "one over the US" index measures macroeconomic data relative to forecast. The index rises when economic data exceeds economists' expectations. So too, it falls when economic data falls short of consensus. On that count, the index was biased to the downside during the most severe of our recent winter months, which suggests that economic activity will likely come in flat in Q1. That said, the index appears to have troughed, and reversed itself in early April, suggesting that the economy should once again be on the rebound and begin pulling its own weight.

But for now, today, irrespective of how the economic expansion plays out, as long as we remain in this near zero interest rate environment, we should embrace real equity returns even in the single mid-digit range particularly when banks offer us zero or investment grade bonds provide just a couple hundred basis points more. We'll take that difference to the bank every time.

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