July 2015

regent atlantic

Investment Outlook Report

The 2015 3rd Quarter Outlook:

Summer is usually a quiet time of year for financial markets. Traders, policy makers, and CEOs alike use this time of year to take their annual vacations, which tends to lead to fewer big news items, less volatility and an all-around calmer environment for stocks and bonds alike. This summer may be different.

The season is already more eventful that normal due to headlines coming from Greece and its long term status in Europe, and it may become more eventful still as the markets shift their focus to the U.S. Federal Reserve and what the central bank might do later in the fall with our monetary policy.

We believe these developments are definitely worth watching. Worries about Greece have the power to move markets, though we do not see it as a big risk economically or for Europe's banking system anymore. Likewise, if the Federal Reserve hikes rates for the first time since 2006 it will create a fair amount of anxiety for investors. In our view, though, the Fed has already begun tightening monetary policy indirectly. More importantly, a rising fed funds rate has historically been associated with rising, rather than falling, stock markets.

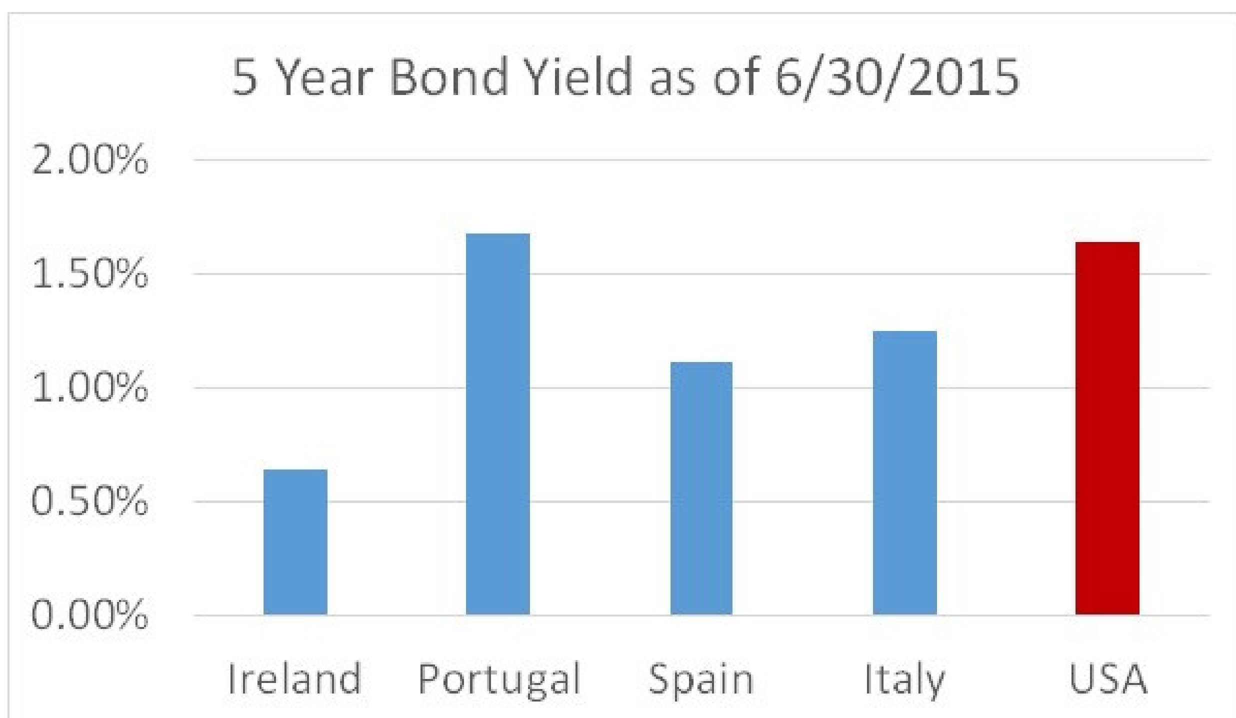
Ongoing Drama in Greece

One of the biggest news items of June and July was the ongoing drama in Greece. The acrimonious negotiations between the Greek government and its European partners came to a head in the final week of June, when Greece walked away from the bargaining table without a new bailout deal. This led to a run of stock market volatility lasting well into July. The S&P 500 saw its biggest one day drop in a year on June 29th, after Greece stopped negotiating.

These are some of the biggest up and down moves in the markets that we've seen in some time, but let's not let the day-to-day price changes and political maneuvering take our focus away from the fundamentals. Greece is likely to stay in the news for some time to come, but not because it is a major macroeconomic risk to the rest of the world. The Greek economy is only about the size of Louisiana's and the Greek stock market represents less than 0.1% of global market cap.

Nor do we believe that Greece is any longer a risk to the global financial system. When its fiscal troubles first became apparent in 2010, there were many banks and other financial institutions holding Greek debt. In the five years since then, the major market players have had ample time to reduce their exposure to Greek debt. As of 2015, the biggest holders of Greek debt are public institutions like the IMF and the European Central Bank. In fact, Greece already defaulted on its debts once in 2012, without that event leading to material financial market repercussions.

If the risk is neither macroeconomic nor financial, why then is Greece grabbing headlines and moving markets? Markets may be responding to a different risk – contagion. If Greece falls, or exits the Euro, what happens to the other troubled countries in Europe? The market has a way to gauge this risk – the yield on government bonds. This number is a proxy for the perceived safety of a country's debt, and hence a good sign of whether investors expect a domino effect from Greece or relative stability. So far, the markets have expressed confidence in the stability of other European countries, with the yields on government bonds issued by Spain, Portugal, Italy and Ireland all close to or below the rates that U.S. bonds command! This was not the case in 2010-2012, when there were periods where investors demanded a yield of 7% or more on bonds issued by these countries.



The situation in Greece is one worth watching. It has the potential to drive markets both higher and lower depending on the outcome. Day to day newsflow and changes in headlines may make for larger price swings than we've seen so far this year. However, fundamentally Greece is unlikely to have drastic effects on the global economy or on financial markets. Greece's potential to create a domino effect among the weaker countries in Europe is not large and investors have expressed confidence in other Eurozone economies.

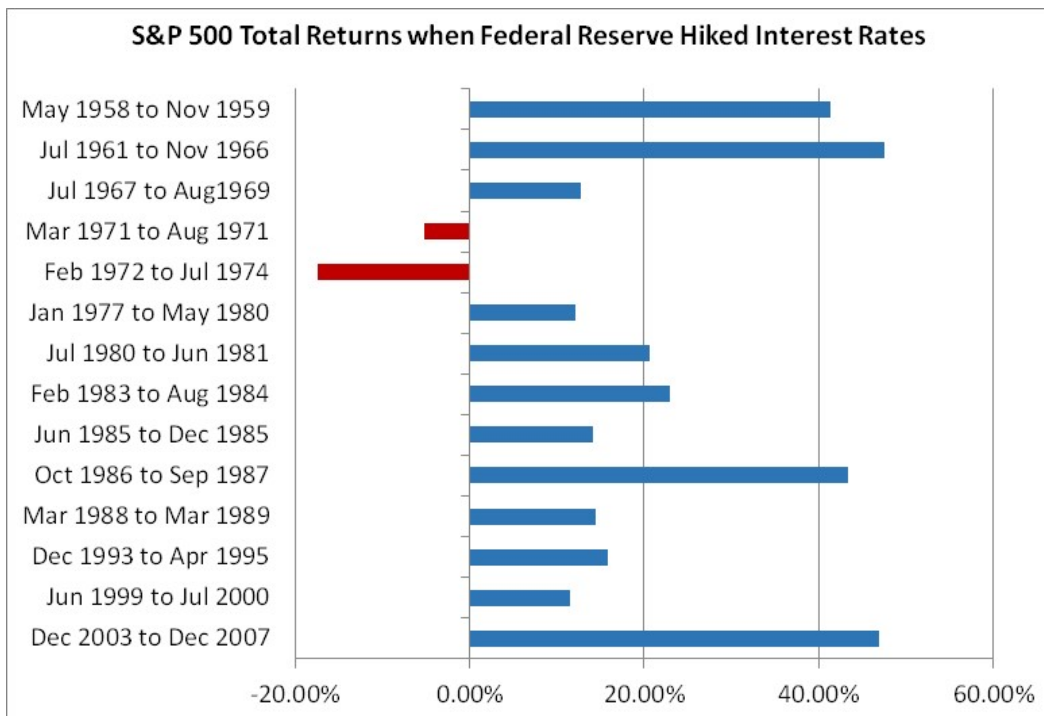
Federal Reserve – What's Next for the U.S. Economy?

The Federal Reserve is likely to be on any investor's radar for the rest of 2015. Since 2008, the central bank has taken multiple unprecedented actions to try and support the U.S. economy. The actions ranged from taking short term rates down to very close to 0%, to buying billions of long term bonds each month in a bid to reduce borrowing costs and helps both homeowners and companies to fix their balance sheets. The next potential step that has investors' attention is the potential for an interest rate increase later this year. This would be the first increase in the Federal Funds rate since 2006.

Investors may worry about this development. It is important to keep this in perspective though. While this may be the first interest rate increase in some time, it would not be the first step back towards normal. In fact, the Fed has been getting us back on track since mid-2013, when the Fed chairman first began to suggest that the billions of dollars of bond purchases would eventually stop. It has followed through on that promise and its bond purchasing program tapered off in the Fall of 2014. This rate hike is the next logical step in the process. It is not the beginning of a tight monetary regime where the Fed is trying to slow the economy. It's the continuation of the policy that has been two years in the making.

Many investors worry about the potential impact of interest rate hikes on the stock market. If borrowing costs rise, isn't it expected that company profits and their stock prices might fall? While that makes sense, it's important to remember that the Fed does not act in a vacuum. The Federal Reserve tightens monetary policy and raises interest rates in response to a stronger economy – one that has a healthy corporate sector, low unemployment, and a good outlook for growth. In fact, prior environments when the Fed raised interest rates have actually been associated with rising stock markets, rather than losses.

RegentAtlantic. A better way.



The summer of 2015 is already off to a boisterous start and developments both at home and abroad may occupy headlines in an otherwise quiet period for the markets. We believe that the situation in Greece does not have the potential for a domino effect, so while it is important to watch Europe we do not expect contagion to affect other European economies. Likewise, while the Fed's expected rate hike will grab much media attention, it may not be bad news for markets over the long term.

RegentAtlantic

1200 Mount Kemble Avenue - Morristown, NJ 07960-6797

973-425-8420 - Fax 973-425-8434

www.regentatlantic.com

Important Disclosure Information

Please remember that different types of investments involve varying degrees of risk, including the loss of money invested. Past performance may not be indicative of future results. Therefore, it should not be assumed that future performance of any specific investment or investment strategy, including the investments or investment strategies recommended or undertaken by RegentAtlantic Capital, LLC ("RegentAtlantic") will be profitable. Please remember to contact RegentAtlantic if there are any changes in your personal or financial situation or investment objectives for the purpose of reviewing our previous recommendations and services, or if you wish to impose, add, or modify any reasonable restrictions to our investment management services. A copy of our current written disclosure statement discussing our advisory services and fees is available for your review upon request. This article is not a substitute for personalized advice from RegentAtlantic. This article is current only as of the date on which it was sent. The statements and opinions expressed are, however, subject to change without notice based on market and other conditions and may differ from opinions expressed in other businesses and activities of RegentAtlantic. Descriptions of RegentAtlantic's process and strategies are based on general practice and we may make exceptions in specific cases.

The index returns shown above show the total return for various investment indices and include the impact of the reinvestment of dividends. A comparison to indices may not be a meaningful comparison. Comparisons to benchmarks have limitations because benchmarks have volatility and other material characteristics that may differ from the performance of a client's portfolio. The investments in a client's portfolio may differ substantially from the securities that comprise each index and are not intended to track the returns of any index. One cannot invest directly in an index, nor is any index representative of any client's portfolio. Actual client accounts will hold different securities than the ones included in each index. The index returns are gross of applicable account transaction, custodial, and investment management fees. The actual investment results would be reduced by such fees and any other expenses incurred as an investor. Please below for definitions of the indexes used.

S&P 500 Index - The S&P 500 is an index consisting of 500 stocks chosen for market size, liquidity and industry grouping, among other factors. The S&P 500 is designed to be a leading indicator of U.S. equities and is meant to reflect the risk/return characteristics of the large-cap universe. Each constituent in an index is weighted by its market-capitalization, as determined by multiplying its price by the number of shares outstanding after float adjustment. The price return of an index is a measure of the cap-weighted price movement of each constituent within the index.

Source for all data in this article: Bloomberg