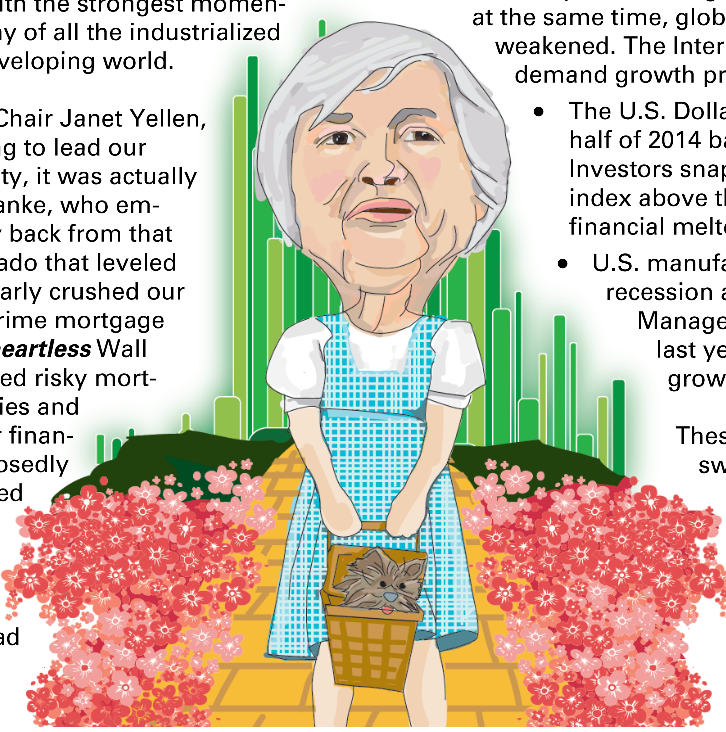
Investment Watch

4th Quarter, 2014

No Place Like Home

"There's No Place Like Home" not only in Kansas, but throughout the United States. While the rest of the world seemed to falter in the greyness of slower growth or even the darkness of recession in 2014, here at home U.S. economic growth broke out of the doldrums and burst into Technicolor, just like in Oz. The U.S. Commerce Department's final revision of 3rd quarter GDP revealed a surprising surge of 5.0%. This, coupled with the 2nd quarter's 4.6% expansion, produced the strongest back-to-back quarters since 2003 and the most reliable evidence yet that our recovery may finally be on solid ground.

Most believe that the expansion cannot keep up this torrid pace facing headwinds of lackluster global growth due to the struggles of Europe and Japan, the slowdown in China and the chilling effect of plunging commodity prices in the developing world. Macroeconomic Advisors predicts a more modest gain of 2.8% for the 4th quarter's GDP. Even so, the U.S. enters the new year with the strongest momentum and healthiest economy of all the industrialized nations and most of the developing world.



Although Federal Reserve Chair Janet Yellen, imitating Dorothy, is striving to lead our economy to the Emerald City, it was actually her predecessor, Ben Bernanke, who embarked on our long journey back from that devastating economic tornado that leveled our housing market and nearly crushed our financial system. The subprime mortgage crisis was precipitated by ***heartless*** Wall Street wiz kids who packaged risky mortgages into complex securities and sought assistance from our financial gatekeepers. The supposedly erudite rating agencies doled out top rankings on these low quality securities making them seem as safe as a Treasury Bond, ultimately proving that they had ***no brains*** at all.

Fed Chairman Bernanke, like "*The Great and Powerful Oz*" didn't have any magic, but he did have the ***courage*** to unleash the most daring financial rescue plan in our history. Bernanke, a student of the Great Depression, used that knowledge to coax the US economy out from the Great Recession. This fiscal experiment of near-zero interest rates, reinforced with direct cash injections and three rounds of quantitative easing, held interest rates down at historically low levels.

Two years ago Janet Yellen took the helm of the Fed and was immediately charged with the difficult task to unwind these easy money policies while trying to keep our nation on the yellow brick road to a self-sustaining economy. Her first job was to eliminate the behemoth $85 billion per month bond buying of **QE3**. Beginning just over a year ago, the bond purchases were slowly scaled back and were finally concluded in October. **QE3** fulfilled its goal and kept longer-term rates low. Experts predicted and feared a substantial rise in longer-term interest rates would derail our economy. Astonishingly long-term interest rates not only didn't rise, they tumbled as demonstrated by the yield on the 10-Year Treasury Note plunging from 3.03% to 2.17%.

2014 finished the year with many other economic surprises:

- The nation added 2.7 million jobs through November, its best year of employment growth since 1999. The current 5.8% unemployment rate and declining new applications point to sustained improvements, while the growth in average wages portend more meaningful jobs.
- Oil prices collapsed from over $100 a barrel at the end of June to under $55 and many predict the global oil glut will get much bigger before it's over. Unchecked supplies due to technological advances from U.S. shale production and deep well drilling will keep the supply flowing, while at the same time, global oil demand unexpectedly weakened. The International Energy Agency cut its oil demand growth projections by 22%.
- The U.S. Dollar skyrocketed over 12% in the last half of 2014 based on the WSJ Dollar Index. Investors snapped up greenbacks pushing the index above the level not seen since the 2008 financial meltdown.
- U.S. manufacturing had its best year since the recession according to the Institute for Supply Management. The PMI averaged 55.8 for last year and began 2015 with new orders growing and inventories contracting.

These unexpected, dramatic economic swings have caused disruptions in the financial markets and present a quandary for our Federal Reserve. With the slowdowns in Europe, China and Japan, their central banks are embarking on new monetary easing measures while Yellen's second job is to tighten credit by raising the short term Federal Funds interest rate from the current near-zero level. The Fed has assured us that in this process they will be "patient."

With more purchasing power from the dollar's rise and lower gas prices putting more money in our pockets, the American consumer will be better off in the new year. The road ahead may not be smooth, but for right now -

"There's No Place Like Home".

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