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Money Matter\$



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Three Key Economic Themes for 2015

by Adam Sommers

Now that we are three months into the new year, we can talk about some of the economics happening around the world—and some ways we’re positioning client portfolios to make the best of the situations. There are currently three key economic themes that I am keeping in mind:

1. Rising interest rates in the United States
2. Quantitative easing and currency devaluation (currency wars) in both Asia and Europe
3. U.S. stocks are richly valued due to relatively strong economic growth and quantitative easing over the past six years

Let’s tackle them one at a time—and how I see each theme affecting our three investment buckets: Stocks, Bonds, and Alternative Investments.

The Federal Reserve Board has hinted at finally raising overnight lending rates above zero - which they have offered to member banks since late 2008. The key drivers they hoped to see before inching rates up are low unemployment, decent GDP growth, and inflation above 2%. It appears we’ve accomplished the first two, but there is still no evidence of inflation—as they calculate it. No doubt the price of oil falling 50% has helped keep inflation at bay. The Fed may raise rates this summer, this fall, or even wait until 2016.

The European Central Bank (ECB) and the Bank of Japan (BOJ) are both printing money in an ef-

fort to jump-start their economies à la Ben Bernanke. This should help lift asset prices of foreign stocks and bonds, but will ultimately damage the value of their respective currencies.

Given U.S. stocks are at historically high valuations (as measured by 10-year P/E ratios), is there more room to run after the 200% gain since the bottom in March of 2009? Our models suggest the average annual rate of return for stocks over the next 3-5 years could be less than 4%.

Bonds: We suggest avoiding intermediate term bonds, instead focusing on a barbell or ladder approach with your bonds. I like U.S.-dollar-denominated foreign bonds. We are also investing in floating rate notes, as the coupon payments will rise along with interest rates.

Stocks: We think foreign stocks should benefit from all three themes, as valuations overseas are much more reasonable. I also think dividend-paying U.S. stocks will have an easier time holding their value if stock prices stall.

Alternative Assets: We are currently utilizing option-income strategies, investing in energy-infrastructure, and employing hedge-fund-like strategies akin to managed futures, volatility, and long/short exposure.

Overwhelmed? Allow us to handle it for you.

“There is still no evidence of inflation—as they calculate it.”

3-Year Returns

Dow Jones Industrial 30

Average: 10.4 %

S&P 500 Large Company

Stock Index: 13.7 %

Russell 2000 Small Company Stock Index:

14.8 %

SPDR Gold Index

(GLD): - 10.0 %

iShares Aggregate Bond

Index (AGG): 3.1 %

SFM’s “NAKED ALPHA

FUND”: 10.3 %

ETF Extra – Vanguard Mid-Cap Index ETF—(VO)

The investment seeks to track the performance of a benchmark index that measures the investment return of mid-capitalization stocks. The fund employs an indexing investment approach designed to track the performance of the CRSP U.S. Mid Cap Index, a broadly diversified index of stocks of mid-size U.S. companies. It attempts to replicate the target index by investing all, or substantially all, of its assets in the stocks that make up the index, holding each stock in approximately the same proportion as its weighting in the index.

VO’s Notable Statistics

Dividend Yield:	1.45 %
Total Assets in the Fund:	\$ 10.9 Bil.
Expense Ratio:	0.09 %
Three-Year Return:	18.6 %
Max Drawn Down (last 3 yrs):	13.7 %



Model STOCK Portfolios

GROWTH-oriented portfolio

% Wt.	Symbol	Description	Div. Yield	1-year Return	3-year Return	Expense
21%	VYM	Vanguard High Dividend Stock ETF	3.26%	15.1%	18.8%	0.10%
17%	CSM	ProShares 130/30 Large Cap Core ETF	2.11%	16.7%	22.1%	0.45%
20%	VT	Vanguard Total World Stock ETF	2.45%	9.5%	12.8%	0.17%
22%	VIG	Vanguard Dividend Appreciation ETF	2.14%	12.3%	16.4%	0.10%
20%	IVV	iShares S&P 500 ETF	2.15%	15.4%	19.7%	0.07%

INCOME-oriented portfolio—average current yield: 4.0%

% Wt.	Symbol	Description	Div. Yield	1-year Return	3-year Return	Expense
16%	HSPX	Horizons S&P 500 Covered Call ETF	4.17%	6.4%	NA	0.65%
27%	VYM	Vanguard High Dividend Yield Stock ETF	3.26%	15.1%	18.8%	0.10%
18%	QDYN	FlexShares Quality U.S. Dividend ETF (dynamic vol)	3.46%	11.6%	NA	0.37%
18%	QDF	FlexShares Quality U.S. Dividend Stock ETF	3.51%	13.7%	NA	0.37%
21%	IQDE	FlexShares Quality Int'l Div. ETF (low volatility)	5.67%	-4.4%	NA	0.47%



Model BOND Portfolios

GROWTH-oriented portfolio

% Wt.	Symbol	Description	Div. Yield	1-year Return	3-year Return	Expense
19%	GSZAX	Goldman Sachs Strategic Income Fund	2.47%	-2.4%	4.2%	0.91%
20%	CSI	Cutwater Select Income Fund	6.83%	10.0%	6.4%	0.75%
20%	BSV	Vanguard Short-Term Bond ETF	1.14%	1.8%	1.4%	0.10%
20%	NFRAX	Nuveen Floating Rate Bond Fund	3.70%	2.1%	6.3%	0.98%
21%	BASIX	BlackRock Strategic Income Fund	2.30%	3.6%	5.0%	0.93%

INCOME-oriented portfolio—average current yield: 4.5%

% Wt.	Symbol	Description	Div. Yield	1-year Return	3-year Return	Expense
19%	CWB	SPDR Convertible Bond ETF	3.30%	6.5%	13.5%	0.40%
19%	NFRAX	Nuveen Senior Secured Floating Rate Note Fund	3.70%	2.1%	6.3%	0.98%
23%	CSI	Cutwater Select Income Closed-End Fund (CEF)	6.83%	10.0%	6.4%	0.75%
19%	JNK	SDPR High Yield Bond ETF	4.83%	1.0%	6.2%	0.40%
20%	OOSYX	Oppenheimer Senior Floating Rate Fund	3.94%	1.5%	5.0%	0.83%



Model ALTERNATIVE Portfolios

GROWTH-oriented portfolio

% Wt.	Symbol	Description	Div. Yield	1-year Return	3-year Return	Expense
18%	ALTS	ProShares Multi-Hedge Strategy ETF	3.19%	NA	NA	0.95%
23%	RWO	SPDR Global Real Estate ETF	3.43%	21.9%	14.6%	0.50%
18%	RYMSX	Guggenheim Multi-Hedge Strategy Fund	1.78%	9.4%	3.7%	1.52%
23%	VNQ	Vanguard U.S. Real Estate ETF	3.76%	30.2%	17.9%	0.10%
18%	PFF	iShares Preferred Stock ETF	5.10%	9.9%	7.9%	0.47%

INCOME-oriented portfolio—average current yield: 4.2%

% Wt.	Symbol	Description	Div. Yield	1-year Return	3-year Return	Expense
21%	PFF	iShares Preferred Stock ETF	5.10%	9.9%	7.9%	0.47%
16%	CVY	Guggenheim Multi-Asset Income ETF	5.64%	-4.9%	6.3%	0.84%
22%	RWO	SPDR Global Real Estate ETF	3.43%	21.9%	14.6%	0.50%
22%	VNQ	Vanguard U.S. Real Estate ETF	3.76%	30.2%	17.9%	0.10%
19%	ALTS	ProShares Multi-Hedge Strategy ETF	3.19%	NA	NA	0.95%