George M. Hiller Companies L.L.C.
INVESTMENT MANAGEMENT, TAX, ESTATE & FINANCIAL COUNSEL

Financial & Investment Newsletter

September 2015 Edition

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Market Outlook

As of September 2, 2015

The bull market, which began in March 2009, (almost 6 1/2 years ago) stumbled in August. The stock market entered correction territory (defined as a drop of at least 10 percent), but so far the market has refused to stay in correction, emotionally swinging up and down with volatility. The stock market has been influenced by fear derived from events in China (the second largest economy in the world) that may play out without significantly affecting the U.S. economy.

Our view is that recent market moves do not appear indicative of an ongoing bear market. There are underlying signs of strength in the U.S. economy that may translate into improved stock market results as we move toward the year-end and beyond.

Even though the market has dropped there has been an uptick in demand for stocks as both traders and longer-term investors have sought to take advantage of lower prices and better values. Evaluation of market supply and demand measures indicates a recent move toward greater market strength. Because of this increase in demand our intermediate market outlook (weeks to months) has changed from negative to positive.

Our longer-term market outlook (months to years) continues to remain positive with one notable exception. Our longer-term outlook for the category of Resources and Materials is negative.

Resources and Materials typically include investments in chemicals, oil, metals, timber, and other commodities. The longer-term outlook for Resources and Materials is not favorable. However, our longer-term outlook is favorable for the following categories:

- US Equities
- International Equities
- Real Estate
- Bond/Fixed Income

Please remember that no market outlook or indicator is foolproof or guaranteed to accurately forecast future market conditions. Observed historical trends are not guaranteed to occur in each and every year nor in any given year or time period.

Year-to-date the Dow Jones Industrial Average is down -8.26%, the S&P 500 Index is down -5.34%, while the NASDAQ is up 0.29% as of September 2, 2015 (source money.cnn.com). Please note that the Dow, S&P 500, and NASDAQ are all equity indexes.

Most diversified investment portfolios are not invested 100% in equities. Also, while it is possible to invest in various equity index funds, it is not possible to invest directly in the indexes themselves.

Our market snapshot (taken daily) is as follows:

-- U.S. Equities	***Positive outlook for past 1,314 days***
-- International Equities	***Positive outlook for past 1,118 days***
-- Resources & Materials	***Negative outlook for past 40 days***
-- Real Estate	***Positive outlook for past 2,210 days***
-- Bonds/Fixed Income	***Positive outlook for past 551 days***

Currently, the top 3 performing sectors (based upon our assessment and ranking methodology) are:

- **Cash (1-3 month T-Bills)**
- **Utilities**
- **Consumer Cyclical**

Consumer Cyclical is a category of stocks that tend to fluctuate with business and economic cycles. Typically, companies in the auto industry, retail, housing, restaurants, and entertainment are considered consumer cyclical stocks. When the economy is not doing well these stocks tend to suffer because consumers tend to cut back on purchases in these areas when times are tough.

Consumer Non-Cyclical is a category of stocks that tend to not fluctuate as much when business and economic cycles change. Typically, companies in areas of essential items such as toothpaste, soap, food, power, water and gas tend to hold up well in troubled times because consumers tend to purchase these items regardless of the business or economic climate.

In addition to the top three sectors listed above Consumer Non-Cyclical and Healthcare have above average rankings. This suggests that these sectors are also above average investment candidates. Currently the worst performing sectors are Basic Materials and Energy.

It is interesting to note that in terms of relative rankings Real Estate has continued its rise in our rankings.   Real Estate ranks above average compared to many other investment categories.

Real Estate is also showing strength.   According to the Federal Reserve in its recently released Beige Book on economic activity, "Existing home sales and residential leasing widely improved, with home prices moving up in most areas." The Fed also stated that commercial real estate was "mostly positive."

Auto sales (a consumer cyclical) have been exceptionally strong. Strong auto sales is an indication of increasing consumer confidence. Auto sales are at a seasonally adjusted annual rate of 17.7 million light vehicles, the best auto sales figure since July 2005, (source, "The Wall Street Journal," September 1, 2015).

Strength in auto sales and real estate points toward strength in the underlying economy. It also gives the Federal Reserve favorable data on which to base a decision to increase interest rates.

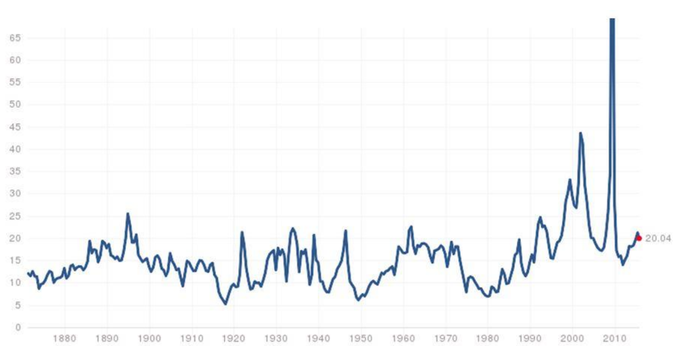
Right now, several economic and business signs we review are bullish, but there will come a time when that changes. We recently changed our longer-term outlook on Resources and Materials from bullish to bearish. Currently, we remain generally bullish on U.S. Equities, International Equities, Real Estate and Bonds/Fixed Income.

Stock Market Valuation Indicators

There are indications that the stock market may be overvalued. This does not mean that the market will not continue to move up. As noted above, our longer-term market outlook remains positive although we have concerns.

The S&P 500 price to earnings ratio (PE) now stands at 20.04 (source multpl.com). This is well above the long-term mean of 15.55. The S&P 500 PE ratio is based upon the current price divided by the earnings over a 12-month period.

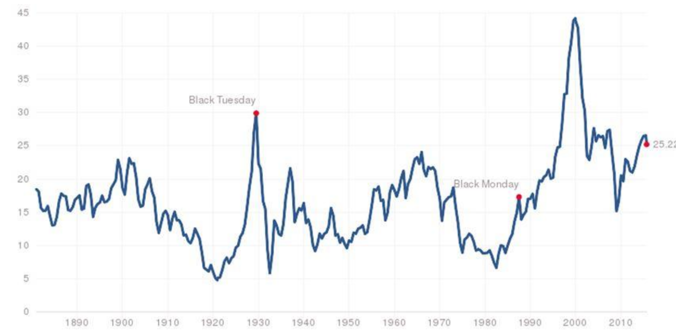
S & P 500 PE Ratio (1880 to August 30, 2015)



Shiller PE

The Shiller PE ratio also known as CAPE is based upon cyclically adjusted price to earnings (CAPE) over a ten-year period. Currently the Shiller PE ratio or CAPE is at 25.22. The long-term mean average of the Shiller PE ratio is 16.62.

Shiller PE Ratio (1881 to August 30, 2015)



These two stock market indicators are at historically higher than average levels, suggesting that stocks are expensive relative to the long-term averages of these indicators. The Shiller PE in particular suggests that the stock market may produce lower returns over the next ten years than what might otherwise be expected. In fact, since 1881, the average annual returns for all ten-year periods that began with a CAPE at this level have been just 3% per year (source, The Sherman SITREP).

Another stock market valuation indicator is called the Market Capitalization of Equities to GDP ratio, also known as the Buffett indicator due to the fact that Warren Buffett has referred to this data as the single best indicator of relative stock market valuation. As of September 2, 2015 the Total Market Index is at $20,206.1 Billion, which is 114.1% of the latest reported GDP. With the correction that has occurred over the last few weeks, stock market valuation has improved. At this level the market is graded as modestly overvalued (source, GuruFocus.com).

Precious Metals Outlook

Our precious metals outlook is negative. That does not mean it may not be a good time to buy or add to precious metals. It simply means that the current trend in precious metals is negative and has been negative for an extended period of time. Gold is under pressure from the strong dollar and from expectations of a Fed rise in interest rates.

Gold recently hit a 5 year low. The price of one ounce of gold has dropped for the last 4 years. As the chart below shows the price of gold is below its price level of 5 years ago.

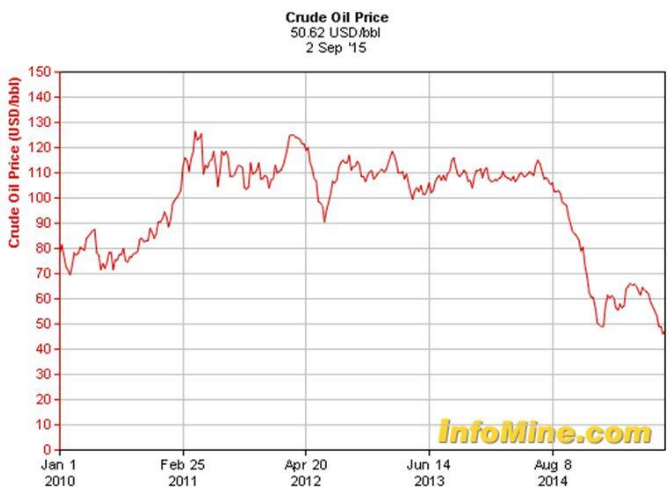
Our long-term planning perspective suggests that precious metals should be considered in asset allocation strategy. With a federal deficit over $18 Trillion it is likely that the purchasing power of the US dollar over time will be worth less than it is today, while gold and silver are likely to retain a significant storehouse of value under different economic scenarios.

Precious metals represent a form of catastrophic financial insurance in the event of a huge devaluation of the dollar or other world-shaking event. Now may be a good time to begin precious metals investments or add to existing positions in order to achieve a certain target within an overall asset allocation plan.

There are many different ways to make investments in precious metals. Some ways are better than others. If you have questions about how to invest in precious metals and what role gold and silver investments should play in your investment portfolio, please call our office for guidance.

Energy Outlook

Our energy outlook is negative. It is negative even though oil recently posted its biggest 3-day gain in 25 years. The following day, after achieving this result, oil dropped about 8%. The chart below shows the crude oil price from January 1, 2010 through September 2, 2015. For almost three years from 2011 to August 2014 crude oil was trading in a range of about $110 per barrel. It is now at $50.62 per barrel, a decline of 54%.



The Economic Environment

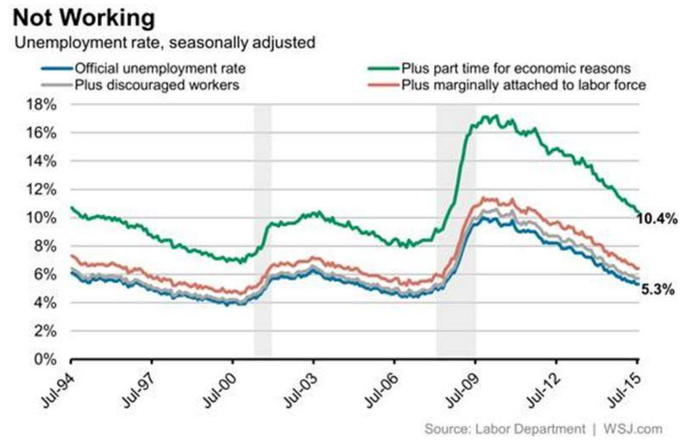
Second quarter GDP was revised upward to a surprisingly strong 3.7% annualized. First quarter GDP increased 0.6% (source, Bureau of Economic Analysis).

The unemployment rate remained at 5.3% in July 2015 (source, Bureau of Labor Statistics). The unemployment rate is now at a seven year low. The drop in the unemployment rate indicates gaining strength in the economy and more confidence on the part of employers to add jobs.

Among the labor force that is employed, there are a large number of people who are underemployed working part-time or are "marginally attached workers" that want to work, but have given up hope of ever finding a job.

The Bureau of Labor Statistics has a term that measures this group called the U-6 rate, which in July was 10.4%, ticking down from 10.5% reported in June. This is sometimes referred to as the true unemployment rate. The continued drop in the U-6 rate shows modest improvement.

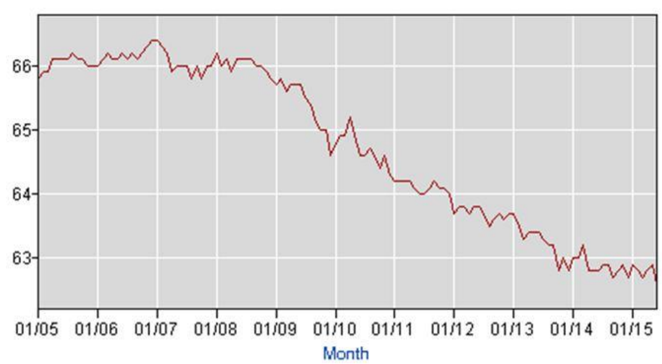
Below is a chart of the official unemployment rate, plus discouraged workers, plus marginally attached to labor force, plus part time for economic reasons, from July 1994 to July 2015. As reported above it shows that the official unemployment rate is 5.3% and the U-6 rate (or true unemployment rate) is 10.4%.



The Labor Department's JOLTS (job openings and labor turnover summary) report in June indicated 5.2 million job openings across the country. This is down a bit from May numbers of 5.4 million, the highest level of job openings in 15 years.

The labor force participation rate remained unchanged at 62.6% in July. This means that among the total labor force in the US, the percentage that is either employed or looking for work is at a low 62.6%. Below is a chart of the labor force participation rate over the last ten years (source, Bureau of Labor Statistics).

Labor Force Participation Rate (2005 to 2015)

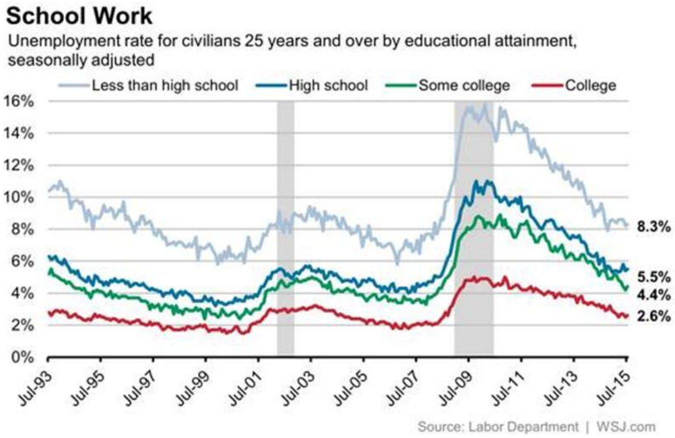


The labor force participation rate is now at its lowest level in 38 years. This means that despite all the new jobs that have been added to the economy and the record number of job openings created, many hundreds of thousands of people are leaving the workforce.

Nearly 94 million people in the USA are neither employed nor are they looking for work. This low labor force participation rate is a drag on the economy that will extend over many years into the future.

The Link Between Education and Unemployment

There is a direct link between education and the unemployment rate. Participants in the labor force that have higher levels of education also experience lower levels of unemployment. The following chart shows the unemployment rate from July 1993 to July 2015 broken down into four different categories.



As you can see the July 2015 unemployment rate for civilians 25 years and over ranges from a high of 8.3% for those who have less than a high school education to a low of 2.6% for those who have a college degree. The lesson here is that higher levels of education result in lower rates of unemployment.

Asset Allocation

In reviewing investment portfolios one of our concerns is that many investors do not have a portfolio that is prepared for today's challenging and changing investment environment. There are times when market and economic conditions suggest a need for changes in the relative weightings or components assigned to an asset allocation portfolio. This process of changing asset allocations based upon changes in the market (such as market anomalies or identifying strong market sectors) and in economic data and trends is called tactical asset allocation. Investors have an opportunity to improve investment performance over time through proper implementation of tactical asset allocation.

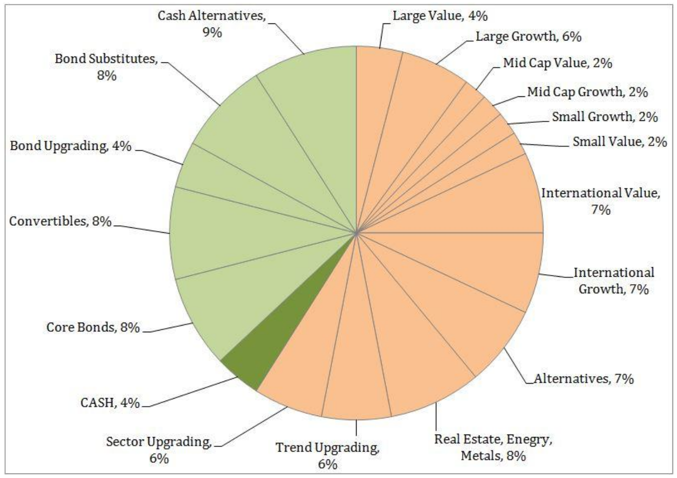
The United States is one of the best places to invest in the world. With recent market corrections, stock market valuation measures have become slightly more favorable even though U.S. stocks as a group are still overvalued compared to historical averages. Given our favorable market outlook for the US and recent market turmoil in China and other areas it makes sense in our view to maintain or increase exposure to U.S. investment assets and reduce exposure to international investment assets.

Due to the fact that our outlook for Resources and Materials has turned bearish we suggest reducing holdings in Resources and Materials including chemicals, oil, metals, timber and other commodities. Reductions in Resources and Materials should allow increases in US investment assets.

The following asset allocation pie chart is an example of tactical asset allocation. The pie chart shows a reduction in the segment comprised of real estate, energy and precious metals, reflecting a reduction in resources and materials, but not real estate. The asset allocation pie chart shows a slight reduction in cash reserves and cash substitutes compared to a previous asset allocation pie chart and a relative overweighting in U.S. stocks compared to global capitalization weightings. These changes are based upon an ongoing assessment of U.S. stock market valuation indicators and the evaluation of supply and demand data and performance data using in part our proprietary tracking and ranking methodology.

We also recognize and evaluate certain economic data and trends in developing tactical asset allocation strategy. Changes in investment data and economic data occur regularly and can in turn lead to changes in asset allocation at any time.

Example of Asset Allocation Pie Chart



In summary the asset allocation pie chart above expresses tactical asset allocation strategy in pursuit of the following broad investment themes:

- **Relative Overweighting to US Investment Assets**
- **Reduced Exposure to Resources and Materials**
- **Reduced Exposure to International Assets**
- **Slight Reduction in Cash**

This asset allocation example is for educational and informational purposes only. It is not representative of any particular client account. Each person, family, or account has different facts and circumstances, so no single investment allocation can fit all situations. In addition, changes in an individual's time horizon and risk tolerance as well as various economic, financial and market factors can lead to changes in the asset allocation of an investment portfolio for any particular investor.

Comings and Goings

Our Director of Portfolio Operations, Russ Hiller, and I traveled to New York City this past July. While there we visited with three New York based investment firms: Marketfield Asset Management, Gotham Asset Management, and Baron Funds. We met with the following people to discuss investments:

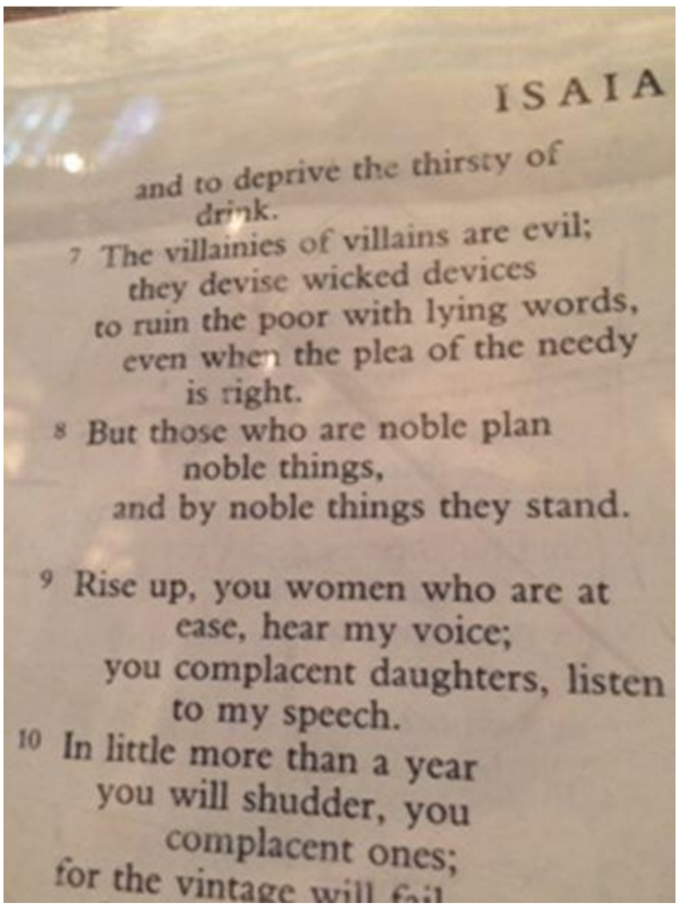
- **Michael Shaoul, Chairman and CEO of Marketfield Asset Management**
- **Kaityn Lucia, Associate Director Investment Relations, Gotham Asset Management, LLC**
- **Robin Chafetz, Investment Specialist, Baron Funds, and Andrew Peck, Portfolio Manager, Baron Asset Fund**

Meetings like these help us to foster relationships in the investment community and better understand and evaluate investment opportunities for our clients.

While we were in New York we visited Trump Tower for lunch and happened to see Donald Trump being interviewed by Anderson Cooper of CNN. A few weeks later I was reviewing financial disclosure information that Donald Trump released to the public as part of his campaign for president of the United States. I noted with interest that Donald Trump had invested millions of dollars in the Baron Funds.

In August, I traveled with George Hiller, Jr. to London and surrounding areas. George took me to visit Winchester Cathedral, Canterbury Cathedral, and the church of Saint Bartholomew the Great, the oldest surviving church in London established in 1123.

While visiting Canterbury Cathedral, where Thomas Becket was murdered on December 29, 1170, I happened to spot an open Bible on a lectern in the middle of the cathedral. The Bible was opened to Isaiah 32 and I took the following photograph of the words of scripture.



My attention was directed to verse 8 above of Isaiah chapter 32. "But those who are noble plan noble things, and by noble things they stand." I have been thinking a lot about that verse and its relevance to our clients and the work we engage in at the George M. Hiller Companies, LLC as financial planners, wealth managers, and stewards of our client's financial plans and investments. Our clients are noble, and we are grateful for the opportunity to serve you in your noble plans.

It is our mission to provide high quality professional and objective financial counsel in the areas of investment management, estate and personal financial planning designed to help our clients improve their financial condition and achieve long-term financial goals.

Sincerely,

George M Hiller Companies, LLC Investment Team

More Resources on our Website

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