BRIAN D. LOWDER, INC.

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FINANCIAL MARKET OVERVIEW

The broad U.S. stock market finished the first quarter about where it started. The Dow Jones Industrial Average was down 0.3%, the S&P 500 was up 0.9% and the overall total market index was up about 1.5%. January performance was flat, February performance was up nearly 3% and March stock market performance nearly erased all of February's gain.

The big turnaround during the first quarter of this year was the positive performance of international and emerging markets. Both categories outperformed U.S. stocks by a wide margin ranging between 2% and 5.5% gross returns compared to U.S stocks meager -0.3% to +1.6% returns.

First quarter performance varied within the U.S. stock market. Growth stocks outperformed value stocks. Small-company growth stocks ended the first quarter with the best gains averaging 6.4% while small-company value stocks averaged only 1.5% gain. Likewise, mid-size company stocks outperformed large-company stocks by 3.5% versus less than 1%.

First quarter financial market performance was positive for nearly all basic investment categories except for the 30 stocks in the Dow Jones Industrial Average and large-company value stocks – both had slightly negative performance. Biotech shares posted the strongest first quarter performance and International stocks advanced more than 5% following negative performance in 2014. The prices for gold and silver barely moved at all.

Once again, interest rates *declined* during the first quarter with the 10-year U.S. Treasury Note falling from a 2.17% yield on the last day of 2014 to 1.93% at the end of the first quarter of 2015. Although interest income dropped slightly, the *value* of Treasuries increased (when interest rates fall bond values increase), thus intermediate-term bonds gained about 2.5% during the first quarter.

The value of the U.S. dollar compared to six other major currencies continues to rise – up over 10% during the first quarter of 2015. Crude oil prices have settled into a range of $43-$50 per barrel.

Real estate (REITs) values (investment real estate – not homes) continue to outperform most other asset categories and posted an average 4.7% gain during the first quarter. This gain follows the nearly 30% advance during 2014. The following chart displays sample returns of various asset categories during the first quarter of 2015:

1st Qtr. 2015	**Index Return (*includes dividends reinvested*)**
- 0.26%	**Dow Jones Industrial Average (^DJI)**
+ 0.88%	**Standard & Poor's 500 Index (^GSPC)**
+ 1.65 %	**DJ U.S. Total Stock Market (VTI)**
+ 3.46%	**Large-company stock-Growth (IWF)**
- 1.26%	**Large-company stock-Value (IWD)**
+ 5.04%	**Mid-Size Stocks – Growth (IWP)**
+ 2.03%	**Mid-Size Stocks – Value (IWS)**
+ 6.44%	**Small-company stock- Growth (IWO)**
+ 1.50%	**Small-company stock- Value (IWN)**
+ 5.47%	**International (EFA)**
+ 2.14%	**Emerging Markets (EEM)**
+ 4.71%	**Real Estate Investment Trusts (VNQ)**
	Fixed Income
+ 0.58%	**Short-term U.S. Treasury (SHY)** *(includes appreciation)*
+ 2.59%	**Intermediate U.S. Treasury (IEF)** *(includes appreciation)*
	Alternative Investment Category
+ 0.07%	**Gold (GLD)**

ECONOMIC AND FINANCIAL MARKET OUTLOOK

Once again, the overall U.S. stock market continued advancing into the first quarter of 2015; however the increase was minimal.

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While some sectors of the economy perform better than others during any particular time period, overall U.S stocks were up less than 2% during the first quarter. Our low-interest rate environment has been a major factor (along with foreign investment flooding into our markets) in propelling U.S. stock values higher than they would normally be based solely on economics. Now we have company. Foreign stock prices have just begun outperforming the U.S stock market.

U.S. investors might think our interest rates are very low – such as the **1.98%** yield on a 10-year U.S Treasury Note, however the interest rate on a 10-year German government bond is **0.183%**, the rate on a 10-year government bond in Japan is **0.4%**, and the yield on a 10-year U.K. government bond is **1.58%**. Now, capital is beginning to flow away from the U.S. and back into the stock markets of other foreign countries that have lower rates than the U.S. The thought or bet is their equity markets are very cheap compared to the U.S. and will experience higher valuations due to very low interest rates - just as our stock market responded over the previous three years. During the first quarter of 2015, foreign and emerging-country stocks out-performed the U.S equity market by more than double.

Also, the strong U.S. dollar continues to impact the financial markets as well. A strong U.S. Dollar does attract foreign investment to both our stock and bond markets, but it also has a negative impact on our corporate earnings. U.S. goods and services become more expensive world-wide when our currency is strong. A strong U.S. dollar lowers foreign demand (exports) for our goods and services – a strong dollar makes our exports more expensive and adversely impacts corporate profits.

Further, with substantially lower energy prices, oil companies' profits have declined - which further reduces expected overall U.S. corporate profits (first quarter estimate of earnings growth is actually negative). Basically, this means our stock market is further out on a "high valuation" limb than it was last year – not worthy of dire predictions, but just a plain fact. We think this beginning trend (money moving away or back to foreign markets) is logical and will continue. Without considering unpredictable global events, foreign markets should perform equal to, or more likely, better than the U.S. market over the near term.

After nearly 6 years of positive stock market returns - following the ugly 37% decline in 2008, U.S. stock prices are more than fully valued. Renewed interest in foreign stocks may be the catalyst that shifts capital flows away from our markets.

Another hint that leadership is about to change is volatility. Simply stated, volatility in stock prices means the conviction of investors is fragile and subject to change.

During each of the three months in 2015, there have been several days of significant up and downward adjustment in stock prices. If stock price volatility is moving in one direction, conviction is strong. Wild swings in daily stock prices in both directions are evidence of a lack of investor confidence.

Over the near-term, we expect to increase our clients' exposure to U.S. equities only during market weakness. The truth is, both U.S. stocks and bonds are more than fairly valued at this time. This observation doesn't mean there must be an imminent market correction, it simply means adding to U.S. stocks or low-paying bonds at this time are less attractive compared to foreign or international stocks. Expect lower returns in the U.S. stock and bond markets in 2015. We do expect to increase exposure to foreign and emerging market stocks carefully over the next 6 months.

Our biggest concern is the impact of an inevitable increase in interest rates. Everyone has been wrong on the timing of rate increases – it should have occurred years ago. But, the Federal Reserve has purposely kept interest rates artificially low to protect our rather weak economy from stumbling back into a recession. Now, other countries around the world are doing the same. So, interest rates may continue to stay low for some undetermined length of time. And, it just means that the transition to higher rates (when it does come about) and the impact on income-oriented investments will be more pronounced.

Nearly all asset categories will be affected when interest rates rise – stocks, bonds, REIT's, and any dividend or income-paying investment. REIT's, water stocks, bonds, and most dividend-paying stocks are currently priced at the high end of the valuation range. Conservative investors who favor income over growth in share price will be forced to make a decision to minimize the price decline of income-paying securities when interest rates rise and consider growth stocks where price appreciation is less certain or predictable than dividend income.

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UNDERSTANDING VOLATILITY

The financial definition for volatility is a measure for the variation in a price of a financial instrument (in our case stocks) over time. There are both historical and implied definitions, which as the names suggest, are based on the data that is utilized to compute them. Also, there is the Merriam-Webster definition for volatility as the likely change in a very sudden or extreme way. If the latter definition is more common, then this explains why investors are getting nervous.

Recently, there has been a lot of news regarding the increase in volatility. So why is it important? The chart below shows the relationship between the S&P 500 (SPX stock market index) and Volatility (VIX) the measure of the price change mentioned earlier. It should be obvious that there have been historical "spikes" in the VIX which were inversely (VIX or volatility up, SPX or stocks down) correlated to the SPX. For example, in late 2008 we had a large spike in the VIX which was the result of a large drop in the SPX (U.S. stocks). Subsequently, we had two additional spikes (May 2010 and August 2011) with corresponding pull backs.

Currently, the VIX is around 15 to 16 , which is a far cry from the high of 80.86 which was followed by the drop in the S&P 500 in 2008 to 2009. If the measure of volatility is currently say 16 and the Bear market was fully realized at 80, then at what level of VIX should there be concern? Once again, referring to the chart below – we can see that when the level of the VIX increases above 30…there is real concern. Starting around 1998, we can see the VIX increase and stay at or around the 30 level. Then in August 2000, the Bear market began and wouldn't relinquish its hold for almost three years. Each stock market decline over the past decade was accompanied by a spike in volatility. So, when the VIX is below 30, volatility is low and that's "good", although below 30 and heading lower is best. When volatility or VIX is rising, that suggests caution, and when the VIX is above 30 and rising, that rise implies danger.

So why is all the attention on the VIX? Well, for starters it tells us that there has been a lot of up and down movement in stock prices. Overall, the S&P 500 was down in January approximately 3% , up in February by 5.6% and then back down in March by 2.6%. Included in these returns are several days that had market movements of greater than 1%. However, if you left your home December 31, 2014 and went a on a camping trip in a remote location (no contact with data) then came home on March 31, 2015 and promptly checked the news you would notice that the stock market (S&P 500) was up around .9% and you would say to yourself "Geez, the stock market hasn't done anything". However, the exact opposite is true.

What causes the volatility? Here's where we need to be very cautious about trying to pinpoint the single headline or the variable associated with unusual price movement. It's in our nature as humans and the media's ticket to the show to discover "the reason of the day". It has been our experience that the headlines don't match the factual (questionable) content and market movements could be completely unrelated to the media's reason of the day.

So what are some of the most recent reasons for increased volatility? For starters, there has been uncertainty regarding the Fed policy and when the interest rates will begin to adjust upward. The U.S. recession fears are a past concern; therefore our artificially low interest rates must eventually adjust upward as the economy continues to grow. But economists, analysts and Wall Street gurus still don't have a consensus of when the increase will occur as most of us expected rates to increase over the past 15 months and it hasn't happened yet.

Maybe it's the stronger dollar and lower oil prices that are adversely impacting U.S. corporate profits of multi-national companies. Or, increased volatility may be a reaction to our Bull market that's getting long in the tooth at 73 months versus the average Bull market of 63 months.

Regardless of the reasons, increased volatility in both directions is a cause for concern. If volatility is low or simply disappears – that would be a good sign and adds stability to the financial markets. If it doesn't, continued volatility in stock prices should not be ignored. You don't necessarily have to figure out what is causing the increased volatility, you just have to understand and be prepared to act when volatility increases – it means something is about to change.

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COPIES OF 2014 INCOME TAX RETURNS

Please send paper or electronic (email) copies of your 2014 income tax returns to our office at your earliest convenience. Our investment decisions, income tax management and retirement planning strategies are greatly improved when we have your most recent income tax returns in our files.

ANNOUNCEMENTS

We haven't had any changes to our team of advisors and staff for over 14 years. But Remette Martinson, who has been our office manager for 18 years, has decided to join her husband Jay in retirement effective June 2015. We are truly sad to see our office mother retire and a bit jealous. Remette has made a definite imprint on our team and she will be missed. However, Remette's pending departure also brings good news. Jennifer Finley has joined the firm as our new office manager and has been "shadowing" her mentor, Remette for the past several weeks.

Jennifer has over 20 years of experience as office manager, operations manager and portfolio administrator with several investment advisors as well as maintaining the books and records for several private clients. We have all the confidence that the transition will be a short one and Remette will quickly transition into retirement with a smile on her face.

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Best regards

Brian Lowder | Clinton Winey | Michael Kinnear | Remette Martinson | Pam Priest