Commentary

April 20, 2015

The Markets

It's a topsy-turvy world.

In the United States, during the last quarter of 2014, about seven million (13 percent) of all mortgaged residential properties were underwater, meaning the mortgage loan amount was at least 25 percent higher than the estimated market value of the property, according to *RealtyTrac.com*. That's a significantly lower number than the 12.8 million that were underwater early in 2012. Regardless, it's an unhappy situation for the homeowners who may wish they lived in Spain.

Why Spain? Well, as has been mentioned before, negative interest rates have been sweeping across Europe and affected mortgage rates. *The Wall Street Journal* explained:

"In countries such as Spain, Portugal, and Italy, the base interest rate used for many loans, especially mortgages, is the euro interbank offered rate, or Euribor… Banks set interest rates on many loans as a small percentage above or below a benchmark such as Euribor. As rates have declined, sometimes to below zero, some banks have faced the paradox of paying interest to those who have borrowed money from them."

In fact, at least one bank – the seventh largest in Spain – has been paying some of its mortgage holders' interest! It just deducts the interest amount from the principal amount the borrower owes. It may be safe to say European banks' expenses have increased since, in addition to paying interest on some loans they've issued, banks also have been "compelled to rebuild computer programs, update legal documents, and redo spreadsheets to account for negative rates."

In addition to a confounding interest rate environment, Europe is also contending with issues related to Greek debt, which triggered a sell-off in stock markets late last week. U.S. markets fared no better. Major markets lost value last week on concerns about Greece leaving the Euro, the potential for weaker-than-expected earnings results, and new trading regulations in China.

Data as of 4/17/15	1-Week	Y-T-D	1-Year	3-Year	5-Year	10-Year
Standard & Poor's 500 (Domestic Stocks)	-1.0%	1.1%	11.6%	14.4%	11.7%	6.2%
Dow Jones Global ex-U.S.	0.3	7.0	0.6	6.4	3.3	3.8
10-year Treasury Note (Yield Only)	1.9	NA	2.7	2.0	3.8	4.3
Gold (per ounce)	-0.3	0.3	-7.4	-9.7	1.2	10.9
Bloomberg Commodity Index	2.4	-2.4	-26.0	-9.7	-5.2	-3.9
DJ Equity All REIT Total Return Index	-0.8	1.4	17.8	13.0	14.4	9.1

S&P 500, Dow Jones Global ex-US, Gold, Bloomberg Commodity Index returns exclude reinvested dividends (gold does not pay a dividend) and the three-, five-, and 10-year returns are annualized; the DJ Equity All REIT Total Return Index does include reinvested dividends and the three-, five-, and 10-year returns are annualized; and the 10-year Treasury Note is simply the yield at the close of the day on each of the historical time periods.
Sources: Yahoo! Finance, Barron's, djindexes.com, London Bullion Market Association.
Past performance is no guarantee of future results. Indices are unmanaged and cannot be invested into directly. N/A means not applicable.

IS CREATIVE DESTRUCTION ACCELERATING? In the middle of the last century, economist Joseph Schumpeter presented the idea of creative destruction which causes current ideas, technologies, equipment, skills, and more to become obsolete. He wrote creative destruction "incessantly revolutionizes the economic structure from within, incessantly destroying the old one, incessantly creating a new one. This process of Creative Destruction is the essential fact about capitalism."

Globalization appears to have hastened the pace of creative destruction in ways Schumpeter may not have imagined. The current issue of *PWC's Strategy + Business* pointed out:

"Business operates today in a world of accelerating change. In the United States, it took 76 years for half the population to own a telephone. The smartphone achieved the same penetration in less than a decade. It took France 100 years to double the share of its over-60 population within the labor force, from 7 to 14 percent. China, India, and Brazil will make the same leap in less than 30 years. Due to the whirlwind pace of global forces, a phenomenal amount of value can be created or destroyed more quickly today than at any other point in history."

Strategy + Business suggested most companies will face disruptions during 2015 as the ways in which they reach customers and the products and services they provide to customers evolve. The magazine pointed out seven industries that are on the cusp of significant change including automobile manufacturing (where brand is less important than it once was), shipping (which will be competing with 3D printing), healthcare (where consumers are becoming more influential), and telecommunications (where companies are being challenged by nimble and responsive rivals).

Change may open new investment opportunities and, sometimes, may make companies which have been good investments less attractive.

Weekly Focus – Think About It

"What we need to do is always lean into the future; when the world changes around you and when it changes against you – what used to be a tail wind is now a head wind – you have to lean into that and figure out what to do because complaining isn't a strategy."

--Jeff Bezos, Founder and CEO of Amazon

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* The Standard & Poor's 500 (S&P 500) is an unmanaged group of securities considered to be representative of the stock market in general. You cannot invest directly in this index.
* The Standard & Poor's 500 (S&P 500) is an unmanaged index. Unmanaged index returns do not reflect fees, expenses, or sales charges. Index performance is not indicative of the performance of any investment.
* The Dow Jones Global ex-U.S. Index covers approximately 95% of the market capitalization of the 45 developed and emerging countries included in the Index.
* The 10-year Treasury Note represents debt owed by the United States Treasury to the public. Since the U.S. Government is seen as a risk-free borrower, investors use the 10-year Treasury Note as a benchmark for the long-term bond market.
* Gold represents the afternoon gold price as reported by the London Bullion Market Association. The gold price is set twice daily by the London Gold Fixing Company at 10:30 and 15:00 and is expressed in U.S. dollars per fine troy ounce.
* The Bloomberg Commodity Index is designed to be a highly liquid and diversified benchmark for the commodity futures market. The Index is composed of futures contracts on 19 physical commodities and was launched on July 14, 1998.
* The DJ Equity All REIT Total Return Index measures the total return performance of the equity subcategory of the Real Estate Investment Trust (REIT) industry as calculated by Dow Jones.
* Yahoo! Finance is the source for any reference to the performance of an index between two specific periods.
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* Consult your financial professional before making any investment decision.
* Stock investing involves risk including loss of principal.

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