Views From The Heartland
Investment Perspective of Buena Vista Investment Management

Volume 14 Issue 1
March 2016

THE BULL MARKET THAT KEEPS GOING AND GOING
Along With Old Age Comes Increased Market Volatility

This appears to be a bull market that refuses to die. We just passed the seven year anniversary of this bull market that began March 9, 2009. At that time the S&P 500 was at 677 and now had risen to 2059. This is in spite of several pullbacks and numerous calls by forecasters that this bull market was done. In October 2011 the S&P 500 declined 19.4%. In August of 2015, there was a pullback of 12.4%. And on February 11, 2016 the S&P 500 declined to 1810 which was a 15.2% decline from its May of 2015 high. Yet in spite of these pullbacks the current bull market is still intact and has been the bull market that refuses to die.

It has been an amazing run these past seven years, and with the S&P 500 less than 4% from a new high, this could soon be the second longest bull market in history. This is potentially now the third longest in history at 84 months. I say potentially because the current market peak was 2134 established back in May of 2015. If we don't exceed that level before a 20% pullback occurs, then this bull market would have lasted 74 months. Either way, that is significantly longer than the average which is 3.8 years. Just as impressive as the length of this run, is the gain generated by this run. The table below compares the percentage price gain of this bull market with the 20 other bulls going back to 1900. As you can see, there have only been two other instances of a bull market lasting seven years. And this table shows the current bull run being nearly double the median price gain of 85.7%.

Bull Markets in the Dow Jones Industrials:
Distribution of Gains by Year

	Annual Bull Market Price Gain (%)								Total
	1 Yr.	2 Yrs.	3 Yrs.	4 Yrs.	5 Yrs.	6 Yrs.	7 Yrs.	8 Yrs.	Gain (%)
# Observations	21	16	10	8	6	4	2	1	23
Median gain	41.8	6.4	7.7	18.7	20.4	21.3	24.3	60.7	85.7
Average gain	46.6	8.3	12.3	20.1	22.6	22.2	17.9	60.7	133.9
March 9, 2009 gains	61.4	15.6	5.7	11.7	14.2	9.4	-5.5		158.1

One of the things we have seen more recently with this market is increased volatility. Since the start of 2016 we have seen intraday moves of 100+ points in the Dow on 46 of the first 53 trading days. At the end of January we saw the Dow lose 1143 points in a week, only to turn around and regain 1050 the next week. On February 11, the Dow moved drastically down in the morning, and then rebounded in the afternoon for a one day swing of 551 points. The ironic thing is that for all the volatility we've experienced in 2016, we are less than 1% away from where we started the year. Essentially you are seeing a sort of tug of war going on between the bulls and the bears. This seven year old bull market seems to be at an inflection point trying to determine if the next move will be to the upside, or the downside, which would then bring an end to one of the longest bull markets in history.

In order to get a sense as to where this market is likely to go in 2016, let's look at some of the factors that got us to this point. There are a number of factors that have contributed to this run from 667 to the current level of 2052 on the S&P 500 and 17,602 on the Dow. We're not going to examine all of them, but let's look at three major contributors.

(Over)

THE BULL MARKET THAT KEEPS GOING AND GOING (Continued)

The first factor is the Federal Reserve's quantitative easing program. The Fed Funds rate has been at zero percent since December 2008. In September 2012 we saw bond purchases by the Fed reach $85 billion per month. These policies injected a tremendous amount of liquidity into our financial system. This money needed to be put to work somewhere and a large amount of it ended up in US stocks. The overall consensus is part of the increase in stock prices has been due to low interest rates provided by the Fed. The question going forward is will the Fed policies continue to be a tailwind to stock prices or will they be a headwind?

The second contributing factor has been the large scale buybacks adopted by US corporations. In 2014 and 2015, US corporations authorized and/or bought over $1.87 trillion of stock repurchases, according to Birinyi Associates Inc. 2015's pace exceeded the record set in 2007 of $863 billion. Stock buybacks take shares out of circulation and, thus, have the effect of raising earnings per share and reducing the supply available to investors both of which drive up stock prices. Is this likely to continue at this pace in 2016?

The last factor to examine is corporate profits and profit margins. Profit margins have been rising steadily during this bull market run, rising from 9.4% in 2013 to a high of 10.2% in Q2 of 2015, which is the highest level in the last 55 years. That trend may be starting to fade. The estimate for Q1 of 2016 is 9.3% which would be the lowest net profit margin since Q4 2012. Again, we need to ask the question, are record setting profit margins going to continue to help propel this market upward?

Three primary factors that helped drive the market higher over the last seven years may have a reduced positive affect this year. Combine that with a market that has a forward Price to Earnings (PE) multiple of 16.5, which is above the 5- and 10-year average, and the expectations for this year may need to be somewhat muted. However, one factor that was a headwind in 2015 was the rise in the value of the US dollar. This hurts US corporations that do business internationally. So far in 2016, the dollar has dropped 4% based on the Bloomberg Dollar Spot Index. If the dollar continues to drift lower this year, that would likely be a positive for stocks.

While the absence of a tailwind provided by the Fed, stock buybacks and expanding profit margins may limit the gain in the S&P 500 this year, it doesn't spell doom and gloom. We still think we could see a modest single digit increase in the market. Currently, we have higher than normal levels of cash in most portfolios. Given our outlook for 2016, we will be looking to be opportunistic in putting that cash to work on market pullbacks.

For additional supporting data on this newsletter please see the "Communications" section of the Buena Vista Investment Management website.

BUENA VISTA INVESTMENT MANAGEMENT LLC

LONG-TERM MARKET INDICATORS

Buena Vista Conservative Buy/Sell Discipline:	Positive (turned positive – 03/2016)
Leuthold Major Trend Index:	Neutral (turned neutral – 03/2016)
InvesTech Negative Leadership Composite:	Neutral (turned neutral – 03/2016)
S&P 500 Stock Index:	2,059.74 (0.77% thru 03-31-16)
MSCI World Market Index:	1,648.11 (-0.88% thru 03-31-16)

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Ready For Year Eight?

When we began to worry about the bull's longevity a year ago (… and two years ago, and three years ago), we never imagined we might be updating the accompanying table of bull market anniversaries in 2016. But in early March, with the DJIA and S&P 500 pulling within 7% of their cycle highs, **we can't rule out the possibility that this bull might join an elite list of bull markets that lasted more than seven years**.

Assuming—only for the sake of argument—the bull remains intact, its seventh anniversary will mark a rare case in which the market was lower than at anniversary a year earlier.

- During the 23 cyclical bull markets since 1900, **there have been only four times in which the DJIA celebrated a bull market birthday at a level below the prior year's**. All of these cases occurred on either the bull's second, third, or fourth anniversary.

- The bull market's relative youth in each of those cases was likely helpful in overcoming the early setbacks. But today's "bull" (if it is, in fact, still intact) would rank as the third longest in history, undermining the chances for a comeback year.

Bull Markets In The Dow Jones Industrials: Distribution Of Gains By Year

	Annual Bull Market Price Gain (%)								Total
Bear Market Low	1 Yr.	2 Yrs.	3 Yrs.	4 Yrs.	5 Yrs.	6 Yrs.	7 Yrs.	8 Yrs.	Gain (%)
September 24, 1900	**Bull market lasted less than one year**								47.8
November 9, 1903	59.1	21.6							144.3
November 15, 1907	66.2	12.7							89.6
September 25, 1911	28.0								29.1
July 30, 1914*	84.5								110.5
December 19, 1917	24.9								81.4
August 24, 1921	56.0	-7.8	12.6	37.9	13.1	16.5	24.3	60.7	495.2
July 8, 1932	155.1	-7.6	26.1	27.5					371.6
March 31, 1938	**Bull market lasted less than one year**								60.1
April 28, 1942	44.4	1.5	51.3						128.7
June 13, 1949	40.1	10.4	7.4	-1.0	21.2	36.7			222.4
October 22, 1957	29.2	15.4	-7.7	22.2					75.1
June 26, 1962	32.3	17.2	2.8						85.7
October 7, 1966	24.8	3.0							32.4
May 26, 1970	43.6	7.2							66.6
December 6, 1974	41.8								75.7
February 28, 1978	9.0	5.6							38.0
August 12, 1982	52.2	3.0	7.9	39.7	45.4				250.4
October 19, 1987	22.9	25.5							72.5
October 11, 1990	26.2	5.1	14.6	7.9	22.1	26.1	34.8		294.8
August 31, 1998	43.6								55.5
October 9, 2002	32.9	3.9	2.4	15.2	19.5				94.4
March 9, 2009**	61.4	15.6	5.7	11.7	14.2	9.4	-5.5		*158.1*
# Observations	21	16	10	8	6	4	2	1	23
Median	41.8	6.4	7.7	18.7	20.4	21.3	24.3	60.7	85.7
Average	46.6	8.3	12.3	20.1	22.6	22.2	17.9	60.7	133.9

*Adjusted for closing of NYSE in second half of 1914.

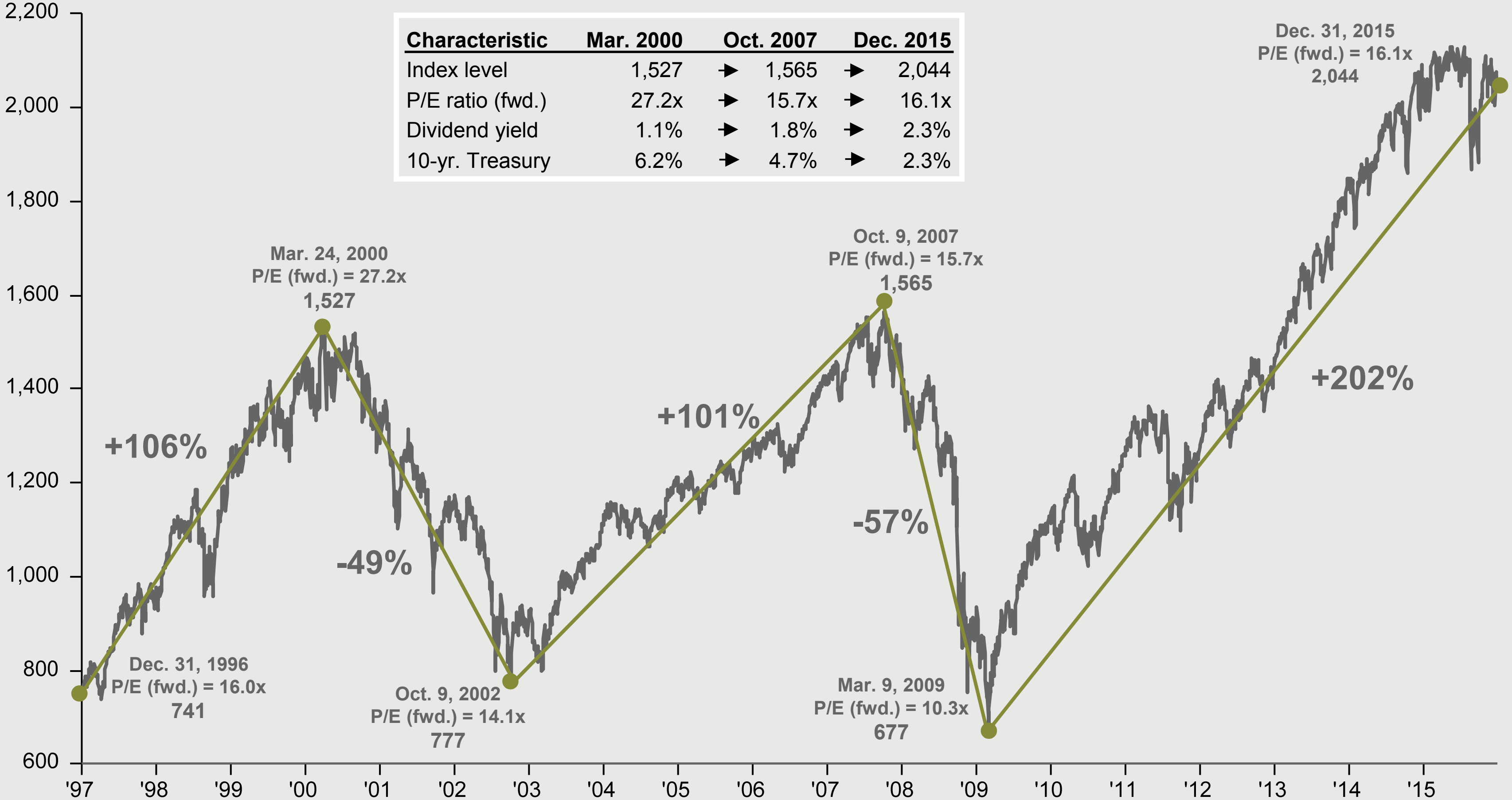
**Year 7 gain is through March 4, 2016 (...assuming bull market is still intact).

Equities

S&P 500 Index at inflection points

S&P 500 Price Index

Characteristic	Mar. 2000		Oct. 2007		Dec. 2015
Index level	1,527	→	1,565	→	2,044
P/E ratio (fwd.)	27.2x	→	15.7x	→	16.1x
Dividend yield	1.1%	→	1.8%	→	2.3%
10-yr. Treasury	6.2%	→	4.7%	→	2.3%



Source: Compustat, FactSet, Standard & Poor's, J.P. Morgan Asset Management.
Dividend yield is calculated as consensus estimates of dividends for the next 12 months, divided by most recent price, as provided by Compustat. Forward price to earnings ratio is a bottom-up calculation based on the most recent S&P 500 Index price, divided by consensus estimates for earnings in the next 12 months (NTM), and is provided by FactSet Market Aggregates. Returns are cumulative and based on S&P 500 Index price movement only, and do not include the reinvestment of dividends. Past performance is not indicative of future returns.
Guide to the Markets – U.S. Data are as of December 31, 2015.

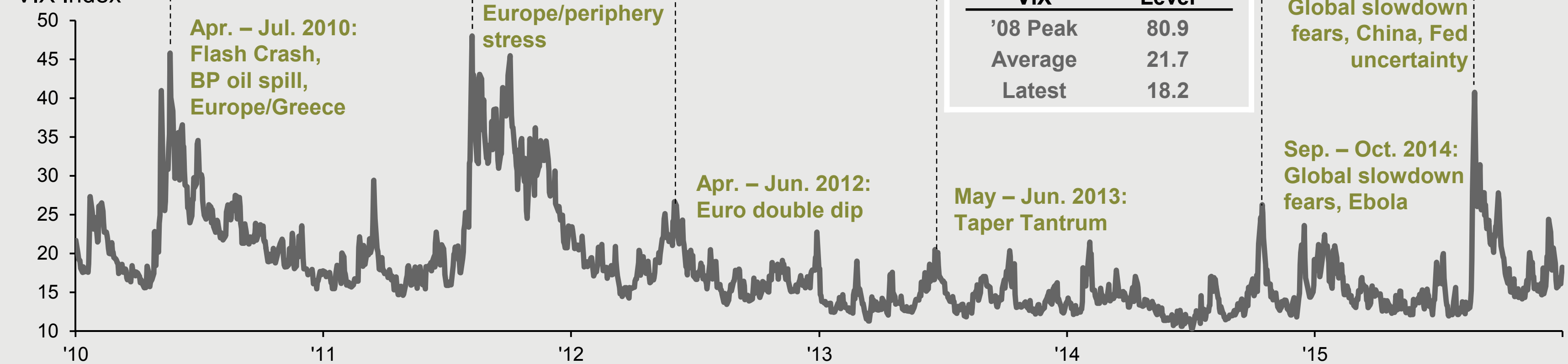
J.P.Morgan Asset Management

Major pullbacks during current market cycle

S&P 500 Price Index

Volatility

VIX Index



VIX	Level
'08 Peak	80.9
Average	21.7
Latest	18.2

Source: FactSet, Standard & Poor's, J.P. Morgan Asset Management; (Bottom) CBOE.
Guide to the Markets – U.S. Data are as of December 31, 2015.

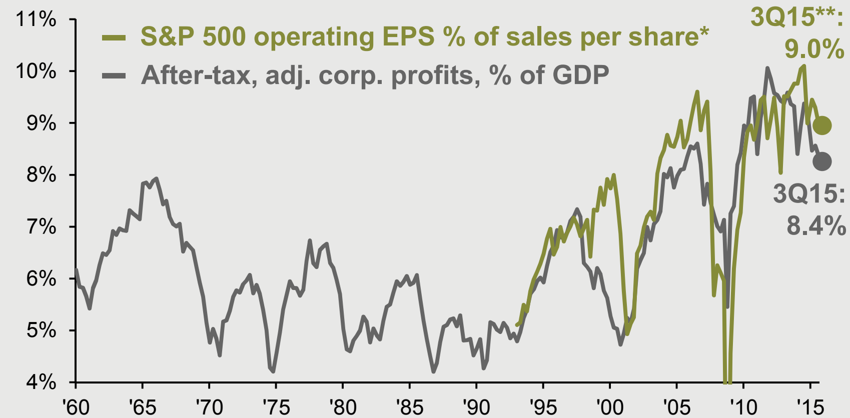
J.P.Morgan Asset Management

Equities

Corporate cash as a % of current assets

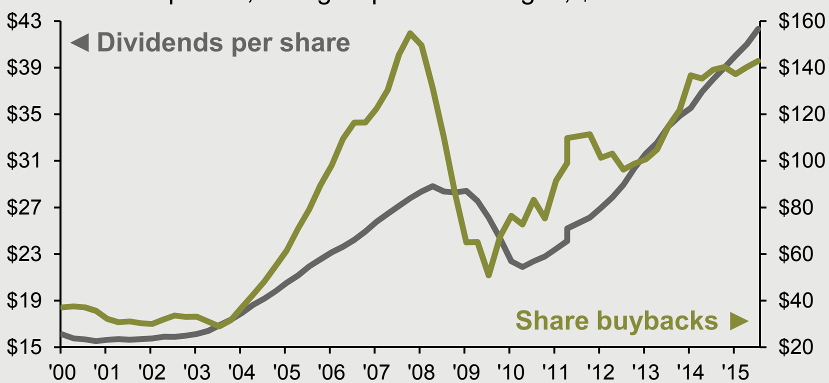
S&P 500 companies – cash and cash equivalents, quarterly

Profit margins



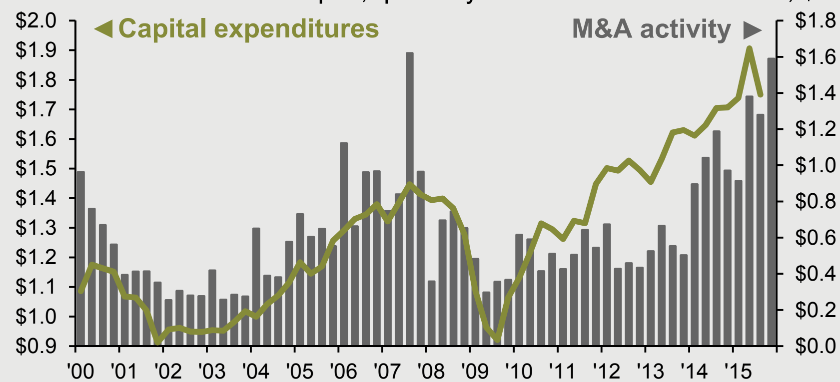
Cash returned to shareholders

S&P 500 companies, rolling 4-quarter averages, $bn



Corporate growth

Non-farm non-financial capex, quarterly value of deals announced, $tn



Source: FactSet, Standard & Poor's, J.P. Morgan Asset Management; (Top right) BEA, Compustat; (Bottom right) Bloomberg, FRB.
M&A activity is the quarterly value of officially announced transactions, and capital expenditures are for non-farm non-financial corporate business. *S&P 500 Operating EPS % of Sales per Share fell to 0% in 4Q2008 and is adjusted on the chart. **Most recently available data is 3Q2015, which is a Standard & Poor's estimate based on 99% of companies reporting.
Guide to the Markets – U.S. Data are as of December 31, 2015.

J.P.Morgan
Asset Management

InvesTech® Research

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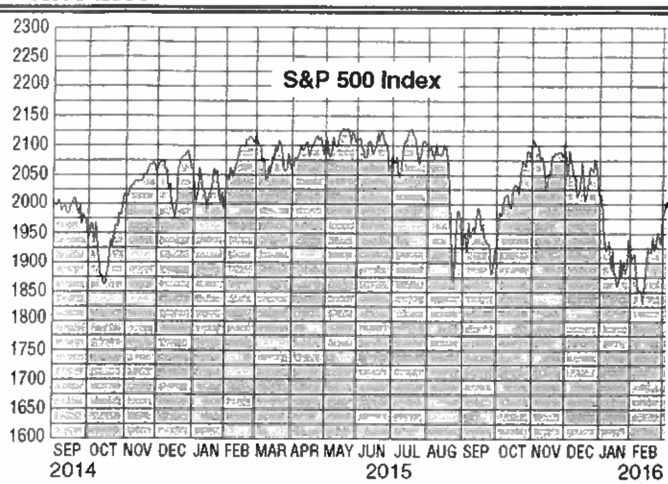


4 Weeks Ending March 4, 2016

	High	Low	Last
Federal Funds	0.40%	0.31%	0.38%
30yr T-Bonds	2.70%	2.49%	2.70%
Gold (London PM)	$1277.50	$1190.00	$1277.50

	High	Low	Last	200D M.A.
DJIA	17006.77	15660.18	17006.77	17182.04
DJUA	637.80	610.87	633.05	579.81
NASDAQ	4717.02	4266.84	4717.02	4889.45
S&P 500	1999.99	1829.08	1999.99	2023.06

S&P 500 P/E Current: 22.1 88 yr Avg: 17.0

Technical and Monetary Investment Analysis

TIPPING POINT?

Central banks have a knack for knowing when "things" are in trouble. They should – since much of the problem today is from miscued monetary policies that helped create bubbles of the recent past. And with European stock markets in bear market territory at the recent low (having fallen more than 20%), the European Central Bank just upped the ante this week in trying to thwart a global recession and possible deflation. ⟶

ECB cuts rates, increases assets buys more than expected
"FRANKFURT (Reuters) – The European Central Bank cut all three of its interest rates and expanded its asset-buying program on Thursday."
***Reuters** – 3/10/16*

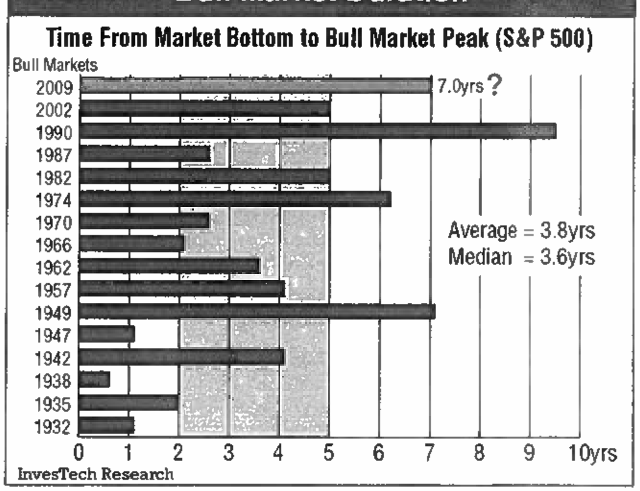
IS it my birthday?

So as U.S. stock investors ponder whether to celebrate a 7th birthday for the bull market, there seem to be more questions than certainties as to what lies ahead. After starting the year with a waterfall decline and the worst opening 6 weeks in Wall Street history, the subsequent 4-week rally has been impressive in both persistence and technical strength.

Unfortunately, the fact remains that even if the current bull market is still intact and new highs lie ahead, it is getting longer-in-the-tooth. In two months it would become the second longest bull market in U.S. history – surpassed only by the decade and Tech Bubble of the 1990s. While new highs seem achievable with the blue chip DJIA and S&P 500 Index less than 8% below last year's high, the more economically sensitive DJ Transports and broad small-cap Russell 2000 Index would have to gain over 21% to achieve new high status.

Inside this issue, we explore the residual risk in this aging bull(?) market, where warning flags are still flying today, and how to assess the strength of this recent rebound...

Bull Market Duration



FACTSET EARNINGS INSIGHT

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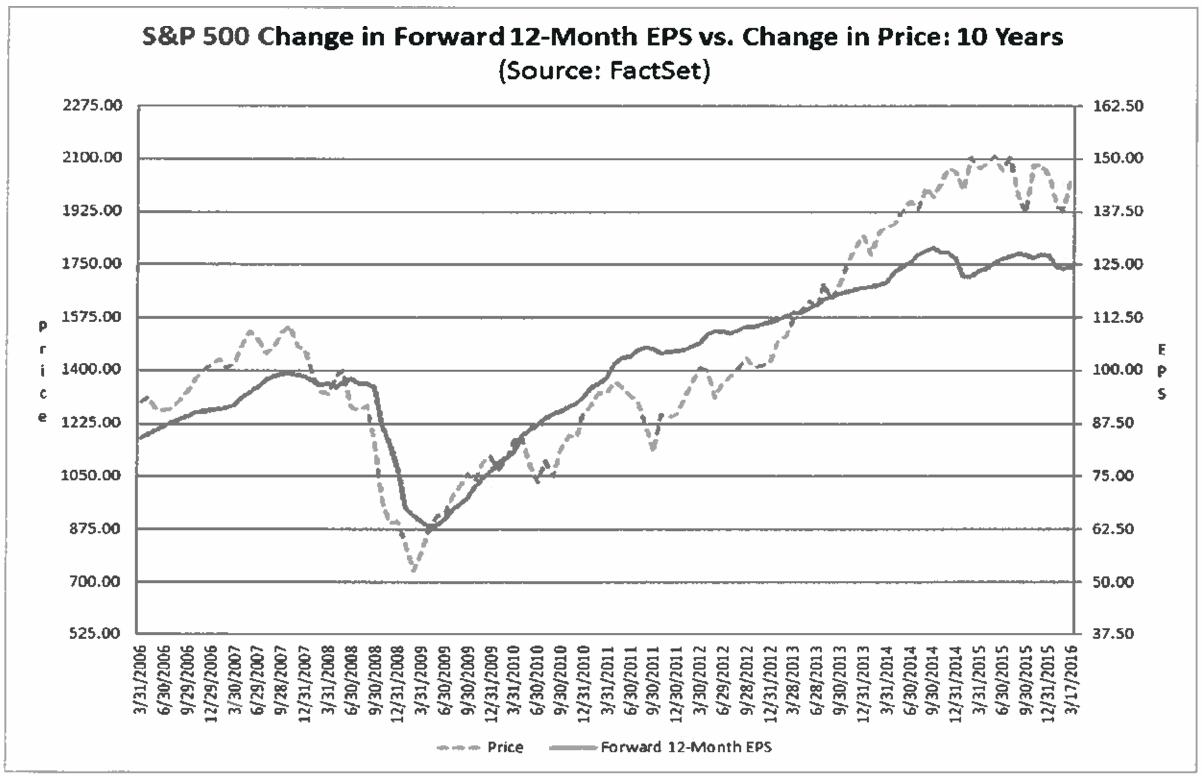
S&P 500 March 18, 2016

Key Metrics

- **Earnings Growth:** For Q1 2016, the estimated earnings decline is -8.4%. If the index reports a decline in earnings for Q1, it will mark the first time the index has seen four consecutive quarters of year-over-year declines in earnings since Q4 2008 through Q3 2009.
- **Earnings Revisions:** On December 31, the estimated earnings growth rate for Q1 2015 was 0.3%. All ten sectors have lower growth rates today (compared to December 31) due to downward revisions to earnings estimates, led by the Energy sector.
- **Earnings Guidance:** For Q1 2016, 92 companies have issued negative EPS guidance and 26 companies have issued positive EPS guidance.
- **Valuation:** The forward 12-month P/E ratio is 16.5. This P/E ratio is above the 5-year average (14.4) and the 10-year average (14.2).
- **Earnings Scorecard:** With 99% of the companies in the S&P 500 reporting earnings to date for Q4 2015, 69% have reported earnings above the mean estimate and 48% have reported sales above the mean estimate.



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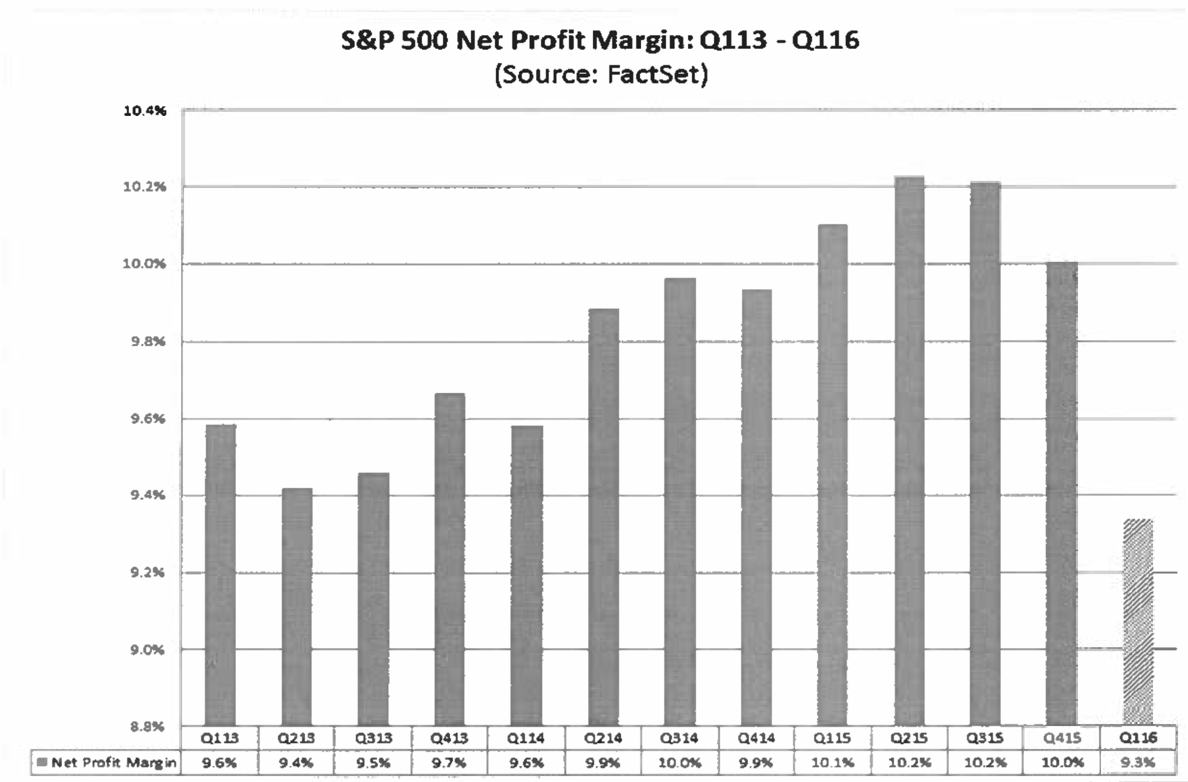
Topic of the Week:

Lowest Net Profit Margin (9.3%) Projected for S&P 500 since Q4 2012 (8.9%)

For Q1 2016, the estimated net profit margin for the S&P 500 is 9.3%*. If 9.3% is the actual net profit margin for the quarter, it will mark the lowest net profit margin for the S&P 500 for a quarter since Q4 2012 (8.9%). What is driving the weaker projected profit margin for the index relative to recent quarters?

Five of the ten sectors are projected to see lower net profit margins in Q1 2016 relative to the 3-year average for each sector, led by the Energy sector (0.1% vs. 6.5%). The estimated net profit margin of 0.1% for the Energy sector is based on estimated aggregate earnings of $263 million and estimated aggregate revenues of $182 billion for the quarter. Excluding the Energy sector, the estimated net profit margin for the S&P 500 would be 10.0%. However, this would also mark the lowest net profit margin for the index excluding the Energy sector since Q1 2014 (9.9%). Thus, other sectors are also contributing to the expected lower than average net profit margin for the index for Q1 2016. After the Energy sector, the other four sectors projected to report net profit margins below the 3-year averages for Q1 2016 are the Industrials (7.9% vs. 9.1%), Information Technology (17.2% vs. 18.0%), Consumer Staples (5.6% vs. 6.1%) and Consumer Discretionary (6.5% vs. 6.6%) sectors.

Based on current earnings and revenues estimates, however, the estimated net profit margin for Q1 2016 will reflect a low for the index. Over the next three quarters (Q2 2016 – Q4 2016), the estimated net profit margins for the S&P 500 are 10.1%, 10.5%, and 10.4%. Eight of the ten sectors are projected to see higher average net profit margins over the next three quarters relative to Q1, led by the Energy, Industrials, and Information Technology sectors.



**The net profit margin numbers published in the commentary and charts in this section of the report differ slightly from the net profit margin numbers published on page 22 of this report due to methodology differences in the calculations. However, both sets of numbers show similar trends in the net margins for the index. The net profit margin numbers in this section are calculated using of the same aggregate earnings and revenue numbers used to calculate the growth rates published throughout this report. The net profit margin numbers on page 22 are calculated using the bottom-up earnings per share (EPS) and sales per share (SPS) numbers for the index. The aggregate earnings and revenue numbers were used in the analysis in this section because ex-Energy net profit margin numbers can be calculated using these figures (but can't be calculated using the EPS and SPS numbers).*