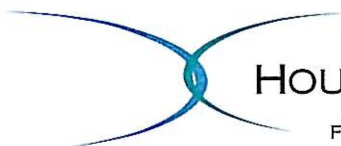

HOULIHAN FINANCIAL RESOURCE GROUP, LTD.
FINANCIAL PLANNING & INVESTMENT MANAGEMENT

1st Quarter 2015

As we begin 2015, many of the same macro trends from last year persist.

Global Concerns: Slower global growth, particularly in Europe and China, has contributed to recent volatility. China is in the process of transitioning from an export based economy to a consumer centric economy. During this shift, growth may slow but more sustainable organic growth for the Chinese economy may be a positive in the long term. The European Central Bank (ECB) has just implemented the first round of quantitative easing with the intention of spurring growth and investment.

Demographic Changes: There is additional worry that an aging population may have a negative impact on developed economies. Birth rates in developed Europe are low and the population growth in the US has been declining for decades. In Japan, low fertility rates combined with longer life expectancies has led to an older and steadily declining population. The taxable wage base decreases as people leave the workforce. Additionally, more people drawing Social Security and other government benefits has the potential to strain already stretched government budgets. While these trends may cause a new normal of slower growth, we believe changing demographics also presents opportunity for investment. In contrast, higher birth rates and increasing life expectancy in emerging markets are long term trends that may facilitate increased economic growth in these economies.

Decrease in Oil Prices: The duration and severity of the decline is still to be determined. Supply is high; OPEC has refused to cut production and, as a result of fracking, production in the US continues to increase. Compounding the issue, demand is decreasing as the global economy slows. The threat to the economy is that the oil and gas industry has been a major contributor to job creation so a slowdown in drilling and exploration domestically may hurt job growth. However, the consumer sees the savings from lower gas prices at the pump which is a potential tail wind for the economy.

Monetary Policy: If job growth continues and wages increase, the Fed is expected to begin increasing interest rates this year. While this may contribute to market volatility in the short term, the Fed is signaling that economy is healthy enough to begin returning to a more normal interest rate environment. Over the past few years, low interest rates have encouraged investment in risky assets and allowed companies to refinance and issue new debt. Conversely, savers have been punished as yields on fixed income investments have been well below historical norms. As we enter 2015, especially in light of ECB quantitative easing, we anticipate that, in addition to the Federal Reserve, demand for US Treasuries from foreign investors will have and impact on interest rates. The expectation that the Fed will increase the Federal Funds Rate influences the short

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end of the curve while demand for longer dated US Treasuries from abroad kept rates on the long end of the yield curve down in 2014.

Strengthening Dollar: This could be a headwind for American based multinational companies since US exports become less attractive and earnings from abroad, when converted to dollars, are worth less. Conversely, European companies who export or earn revenue from abroad may benefit from a weaker Euro (another benefit of ECB quantitative easing).

Emerging Markets: 2014 was not a good year for emerging markets. As we mentioned above, long term positive trends such as increasing share of global GDP and favorable demographics persist. However, the strong dollar, geopolitical concerns and the potential for money to earn more if rates increase in the US were all factors causing performance to lag in 2014.

Active vs. Passive Management: In bull markets, passive management tends to outperform active management. Low cost passive index funds and exchange traded funds (ETFs) give broad based exposure to different indices and, when the market goes up, so do these funds. While we believe that index funds are an important part of a well diversified portfolio, we employ a semi-active management philosophy, using a combination of both index funds and actively managed mutual funds. When we screen for active managers we do so with a focus on performance in down markets. Many of you have been to the office and have seen examples of different metrics we use when selecting managers. One of these is the Drawdown Metric which measures the depth (how deep), duration (how long) and the frequency (how often) of a funds negative return in down markets. We believe it is important to look for mutual fund managers who have a long track record of protecting on the downside. By not digging deep holes, we can more easily participate in up markets. While the prolonged bull market has made it easy to lose sight of the value of stock selection, we believe skilled managers have and will offer superior long term performance.

We greatly appreciate the opportunity to work with you and look forward to an exciting new year. We love to hear from you so please feel free to contact us if you would like to set up a meeting.

Patti, Ryan, Carlton, Sean and Kristal