Greece Back in the Spotlight

Investors' fortunes reversed in May. Whereas April saw foreign investments and hard assets posting strong returns and prompted some investors to make significant changes to their portfolios in response, May was driven by the US markets yet again. This strong performance surprised some investors, after several economic data releases were soft in the month of May.

Analysts hoped that US economic data would follow a similar pattern to last year, when the harsh winter suppressed evidence of an ongoing economic recovery. In that case, the economic data improved dramatically as summer approached and boosted investor confidence. This year, that seems unlikely. Up to this point, none of the data indicates that the US economy is struggling. It is just starting to show that the recovery is losing steam. As a result, the strong performance of US stocks in May is largely due to the relative strength and safety of the US economy as compared to Europe, Japan, and emerging markets.

Last month, it looked like Europe finally found some momentum. The European Central Bank's stimulus program seemed to be having the desired effects and European stocks performed strongly. While this recovery started sooner than most analysts dared hope, it was encouraging. While US stocks increased in value dramatically in recent years, European stocks failed to keep pace. As US growth slowed in the early months of 2015, it looked like undervalued Eurozone assets were on the verge of a long-overdue recovery.

Unfortunately, the negotiations with Greece continue to weigh on the Eurozone economies. After months of back-and-forth and political grandstanding, the deadline for a deal is fast approaching. The European Central Bank and the International Monetary Fund maintain that Greece must agree to run significant budget surpluses, while it is paying down its debts. The Greek government contends that spending cuts and taxes that are required for those surpluses are stifling the Greek economy and perpetuating a deep recession. If the two sides fail to come to an agreement, Greece could leave the Eurozone. While European officials seem somewhat apathetic about that possibility, no one truly knows what the economic consequences will be for Greece or the Eurozone as a whole.

The economic news from China continues to improve, but it is failing to meet investor expectations. While those expectations seem to do little to impact investment in China itself, China's trading partners in emerging markets are suffering. As an example, its Purchasing Managers' Index (PMI) rose from 48.9 to 49.1, which shows an improvement from April's numbers. Unfortunately, any number below 50 indicates that the economy is contracting and that Chinese companies are placing smaller orders for materials. As long as Chinese demand for raw materials is slack, the emerging countries that supply those materials will struggle.

China's economy is currently on pace to grow by 7%, this year, but India overtook China as the world's fastest growing economy by posting a 7.5% figure. Obviously, none of this Chinese data is bad or indicating that its economy is unhealthy. In fact, any developed nation would be overjoyed with 7% growth. The difficulty is that investors and analysts expect China to maintain its world-beating trend and drive global growth, especially in emerging nations.

Market Movers

Investment returns in May were, once again, reminiscent of the last several years, as US stocks dominate virtually all other investments. However, year-to-date returns tell a different story with many investment areas outperforming the US markets. These returns change quickly and it is important to make considered decisions, when building and adapting your asset allocation. Our large allocations to various US markets served our investors well in May. Many investors were eager to take advantage of the European rally that seemed to kick-off in April, but we are patiently waiting for some clarification on the Greek issue before increasing our foreign holdings. Although May proved difficult for several investment areas, our strategies stood firm with most posting modest gains. Year-to-date, our higher risk strategies have outperformed US large cap stocks at reduced risk, while our lower risk portfolios were not far behind.

Asset Categories	May 2015	YTD
US Stocks	1.46%	4.43%
Foreign Stocks	-1.14%	8.60%
US Bonds	-0.26%	1.53%
Foreign Bonds	-2.06%	-3.05%
Hard Assets	-1.78%	-1.56%
Hybrids	1.23%	4.45%

- US Stocks saw modest increases in May with Small Caps (VB) leading the way at more than 2% for the month, which benefited our strategies. Returns from Large Caps (IVV) and Mid Caps (VO) were not far behind at more than 1% each.
- Now that the danger of a Greek exit from the Eurozone is an imminent possibility, Developed Large Caps (VEA) suffered a small loss. On the other side of the globe, China's woes pushed Emerging Large Caps (VWO) more than 3% into negative territory and our reduced allocation in this area was welcome. We expect there to be significant opportunities in these two asset classes before the end of the year.
- US Bonds were all near-zero in May. In general, longer-term bonds were slightly negative and shorter-term bonds were slightly positive. Our shorter-term focus across bonds provided added value.
- Foreign Bonds (BWX, PICB, PCY, WIP) struggled in May. Renewed concerns about the stability of Europe and China's recovery are making investors cautious when investing in foreign debt. In January, we reduced our exposure to Foreign Bonds and that is proving to be a positive decision for our portfolios.
- Commodities (DBC) and Master Limited Partnerships (AMJ) were driven lower when oil prices failed to continue their recovery. Until production declines further, we do not expect oil prices to rise significantly. Meanwhile, Precious Metals (GLTR) managed a nominal gain in the month of May.
- Hybrids continued their steady performance and contribute to our portfolio returns. Convertible Bonds (CWB) were the top-performing asset class in May and their year-to-date performance reached 6% by the end of the month. Preferred Stocks (PFF) saw a small gain in May, but they are up nearly 3% year-to-date.