SEBOLD CAPITAL
WEALTH MANAGEMENT

September 2015

Market Update

Markets saw a jump in volatility in August. Investors showed particular interest in China, driving market swings based on emotion and momentum rather than fundamental analysis. Global noise and skittish trading forced a 10% decline in Large Cap stocks for the first time since 2011. After a rebound, the S&P finished the month dropping only 6% in August and 2.9% year-to-date. Small Caps fared similarly, down 6.3% on the month, and down 3% on the year. Global equities declined 7.6%, and the biggest drop came from emerging market specific equities- falling 9% in August riding the sharp drops in the Chinese market. Providing a bit of protection in volatile times, bonds were mostly flat- domestic fixed income dropped 0.1%, while global holdings gained 0.1%.

August Benchmark Returns

Domestic Benchmarks	Aug	YTD
Large Cap: S&P 500	-6.0%	-2.9%
Small Cap: Russell 2000	-6.3%	-3.0%
International Equity Benchmarks		
Developed: MSCI EAFE	-7.6%	-2.2%
Emerging: MSCI EM	-9.0%	-12.6%
Fixed Income Benchmarks		
Domestic: Barclays Aggregate	-0.1%	0.5%
Foreign: Barclays Global Aggregate	0.1%	-0.8%
Other Benchmarks		
Municipal: Barclays Municipal Bond	0.2%	1.0%
High Yield: ML High Yield Bond	-1.9%	0.4%
Commmodity: Dow Jones UBS Commodity	-0.9%	-12.8%
Real Estate: FTSE NAREIT All REITS	-5.8%	-6.5%
Risk Free: US Treasury CD 3 Month	0.0%	0.0%

Change

It's what you get at the grocery store when you hand over a $20 bill to the clerk when you are buying a candy bar. It is what you get when your current employer thinks that there is a better way to do things. It is when your software provider decides it is time for an upgrade. It's when your hardware is so slow that you have no alternative but to buy new.

We all know change has to happen, but boy we don't like it. It changes our routines; the way that we have grown accustomed to doing things. Our early morning coffee gets interrupted when the coffee store closes. Great, now what? I have to drive 10 minutes out of the way to go to a different coffee shop, and it isn't even that good.

It is that time in the markets. We are in the process of upgrading our software. It is painful in that it is taking us out of our routines and into new ones. The Federal Reserve is changing its policy on interest rates. What is really making a mess out of this process is the length of time it is taking for us to move on in the change cycle. Imagine an upgrade out of Microsoft that was in the works for eight years and when the time comes to upgrade, it gets postponed, again; and again; and again. Each FOMC meeting we have been expecting an interest rate hike, only to find it has been postponed. The challenge, very much like software, is that that the market really doesn't know if it will be an honest to goodness upgrade, or a real stinker.

Volatility is the outgrowth of our angst about change. Some people think that the change will be great. After all, if they raise the interest rates, that must mean that the economy is doing well and we do not need to be in a state of emergency monetary policy now. Savers will finally get some interest that they have in the bank. On the other hand, if they raise interest rates, that will cause problems. Mortgage interest rates will go higher, slowing down the only bright spot in the economy. Borrowing rates will go up and that will slow an already tepid economy.

These are the stories that are playing out in the markets on a market cycle that is currently evolving around the Fed. Admittedly there is too much talk already. In reality a .25% change in the Fed Funds rates will have very little impact on the economy. At this point, it will also have very little impact on interest rates. The only thing that it is impacting is the market participants who can't stand change. They need to be able to predict it, use it, and then move on. This really long roll out of a new policy is getting maddening to them.

So we will put this on the table, the Fed will raise rates eventually. It could be this year, it might be next year. It will have very little impact on the economy as a whole. If the Fed raises rates and the economy grows, then it was the right decision. If the Fed raises rates and the economy slows, then it was the wrong decision. The reality is that there is little to no causal relationship between the two, as much as the market might try to tell you differently.

This is, however, what is causing the volatility. If you want it to slow down a bit, then you might consider penning a note to Chairperson Janet Yellen and telling her to get on with it already. It won't make a difference. I doubt, however, that it would have much impact, but you may feel better.

If we could get this out of the way, the market might begin to behave normally. It might not do what we want, but it will be normal again. What the real issue behind the Fed decision is a confirmation about what other economists think of the economy. After all, if they raise rates, there must not be a fear of recession. The Fed would never raise rates if that was imminent. You might view the Fed as the teacher and the market as the students. The students might know more than the teacher, but they always want to make sure that the teacher isn't hiding any information that they don't know about.

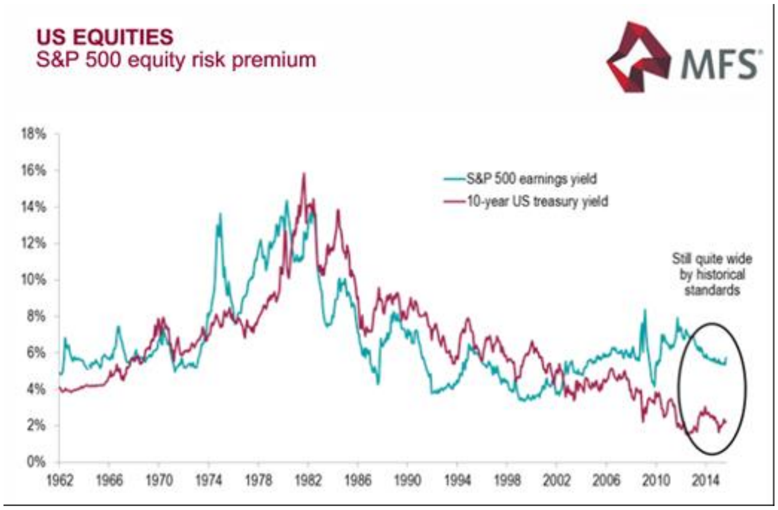
What was different about this month's Federal Reserve Statement was that they, for the first time, went beyond their explicit mandate of U.S. price stability and full employment. Janet Yellen in her press conference explained that they did take into consideration the most recent global events and the potential slowdown in China into consideration as they decided on a rate hike. If a global slowdown persists, a strengthening dollar would continue to put pressure on US manufacturer and could then impact the Feds' mandated positions.

The recent economic data out of China suggests that they are not growing at the 7% stated growth rate. In addition, the Yuan was devalued 2% in one day. While neither of these events taken by themselves tend to mean much, if you put them into context, they tell a story of global slowdown. The markets have reacted in so much.

It appears from our perspective that the reaction, once again, has gone a bit too far. Consider the exposure to China and other EM countries that the US has: less than 1% of GDP for China, and less than 4% GDP for China and all EM combined. So while we agree with the general slowdown, the impact of the slowdown will be muted moving forward.

From a portfolio perspective, we have yet to see any data that contradicts our overall risk/return assumptions. We are, however, actively looking at portfolios both from a tax perspective and from a rebalancing perspective to add value to individual accounts. This activity will have more of an impact on those portfolios with cash flows either in or out.

Overall we continue to see the US markets muddle through this corrective slump over the next several months. While the news cycle would seem to put the market turmoil at crazy, corrective levels, as of this writing, the S&P 500 is down less than 5% on the year. This puts it quite nicely in our range of expected levels, even though we are not expecting outsized returns from the domestic side in the next couple of years.



On a comparison basis, stocks still look very favorable to the fixed income side, as this chart from MFS suggests. While the current volatility is scaring some investors away, long term investors will be well served by holding equities over bonds. This was a consistent story over the past several years that investors have forgotten about.

As always, thank you for your continued support.

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