

MARKET COMMENTARY

US equities performed well once again in 2014. Both the Dow Jones Industrial Average (DJIA) and the S&P 500 indexes reached new highs, with the DJIA having daily record closes 53 times in 2014. Despite these records, it was a tough year for many investors. According to the *Wall Street Journal*, the average hedge fund had a 3.5% total return versus the S&P 500's 14% total return. At least 75% of hedge fund managers failed to meet their performance benchmarks.

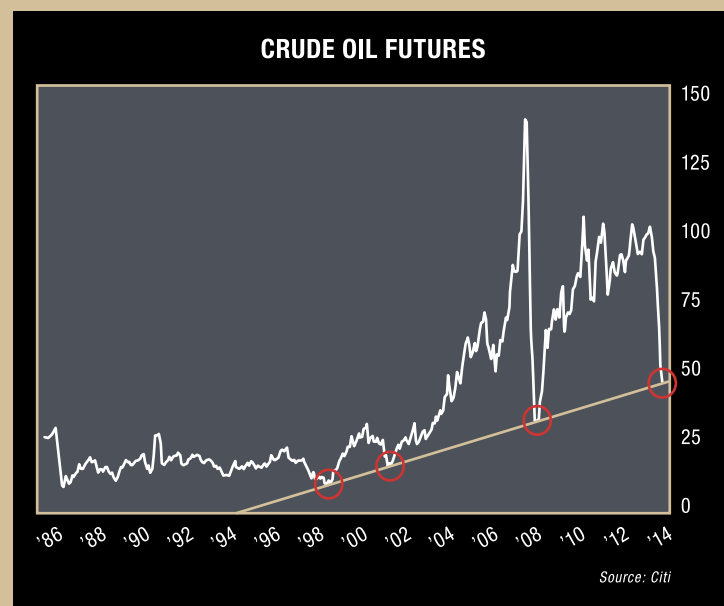
The best performing asset classes in 2014 were real estate investment trust (REITs) and large capitalization US equities. Emerging market equities struggled again in 2014, due to a reliance on commodity prices and geopolitical uncertainty. Nearly all commodity prices fell, most obviously oil, but also iron ore, copper, coal, steel, and gold. In turn, this sharp asset depreciation had negative pressure on the equities of materials producers and mining and construction equipment manufacturers.

Within US equities, the best performing sectors were utilities, healthcare, and technology. The worst performers were materials and energy. The underperformance by hedge funds is most likely due to managers making losing bets on asset allocation and/or sector concentration. In 2014, betting against US Treasuries or investing in some of the disappointing sectors such as energy resulted in surprisingly steep losses. According Jason Zweig of the *Wall Street Journal*, 48 of the 49 economists surveyed at the end of 2013 expected the yield on the 10-year Treasury note to average 3.52% for all of 2014. For most of the year, the 10-year yield was below 3% and closed 2014 at 2.2%. As a result, treasuries with long duration were a surprising outperformer for 2014, up 27% for the year.

When the S&P 500 dropped below its 200-day moving average this fall, many forecasters predicted a subsequent precipitous decline in the markets. The Ebola scare, ISIS, the Ukraine conflict, weakness in China and Europe, and soft commodity prices, all contributed to an uncertain investing environment. Instead of plummeting, the markets turned around, reaching new highs by the end of the year, aided by unexpectedly strong US GDP numbers. For the third quarter, US GDP climbed a remarkable 5.0%, after a weather related -2.1% start to the first quarter of 2014.

Perhaps the biggest event in 2014 was the rapid drop in the price of oil. As we discussed in our October *Market Commentary*, we expressed concern that a drop in the price of crude oil below \$85 per barrel would portend further price destruction. In the second half of 2014, crude prices fell 47% from over \$100 per barrel to just over \$50. While some of the price destruction can be attributed to slowing global oil demand, we believe much of the decline is due to the marginal increase in global supply. New technologies in fracking and the reluctance of OPEC to cut production are creating more supply than the global market demands.

The graph below shows the price of a barrel of West Texas Intermediate (WTI) crude from 1986 through 2014. The line at the bottom of the graph shows the long term trend in crude oil prices. Despite the wild spike in 2007 to nearly \$150 per barrel, oil prices remain close to long term support at approximately \$45 per barrel. If this long term trend holds, the price of a barrel of crude oil should bottom somewhere between \$40 to \$50 per barrel. Further deterioration in the price of a barrel of oil would lead to greater concern that global forecasts for oil demand are misguided.



Lower oil prices are both good news and bad news. The good news is that the consumer has more cash for discretionary consumption. According to David Rosenberg, a strategist at Gluskin-Sheff, for every penny that the price of gas falls, the savings to US consumers is about \$1.5 billion. These savings should track closely with US consumption spending, which is over 70% of US GDP. The bad news is that lower oil prices often signal a global slowdown. US employment in the energy sector is of particular concern. Most of the job growth during the recovery has occurred in states where shale oil and gas production have boomed, particularly Texas and North Dakota. According to David Hunter at Contrarian Macro Advisors, the shale states have created 1.36 million jobs in the past seven years, while non-shale states have lost a net 424,000 jobs. Significant cutbacks in new drilling plans are already happening, and it is likely that this will continue in the coming months. The decline in drilling activity will trickle down through the economies of oil-producing states, threatening job growth which is perhaps the greatest driver of economic activity.

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Despite the outlook for energy, economic conditions in the US seem well suited now for more growth. Weekly unemployment claims remain consistently below 300,000, and the unemployment rate has slowly improved to 5.6%. Auto production reached about 17 million cars - double that of 2009. Housing starts have not recovered to pre-recession levels, but are up 50% from the bottom of the recession. Corporate profits continue to show strong gains, and balance sheets can support increased capital expenditures. GDP growth has surprised most forecasters at 4.6% in the second quarter and 5.0% in the third. This strength was driven largely by personal consumption expenditures which happened before oil and gasoline prices dropped 50%, mostly in the fourth quarter of 2014.

In the coming months, we will closely watch weekly jobless claims for any weaknesses that may indicate economic fragility. With cheap oil giving extra cash to most Americans, rising unemployment could be an especially negative signal. However, most signs seem to suggest that if oil can find a floor and the Fed can skillfully and gradually begin returning to normal interest rates, we can look forward to another strong year in 2015.

401(k) CONTRIBUTION LIMITS

There are big advantages for 401(k) accounts over traditional IRAs.

401(k) ADVANTAGES OVER TRADITIONAL IRAS		
	401(k)	IRA
Annual limit per individual	\$18,000	\$5,500
Age 50+ catch-up amount	\$6,000	\$1,000
Roth income limit	None	\$131,000
Penalty-free access, if needed	Yes (via a loan)	No

CLIENTVIEW WEB PORTAL

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MARKET PERFORMANCE

	4Q 2014	2014
Dow Jones	5.2%	10.0%
S&P 500	4.9%	13.7%
Nasdaq	5.7%	14.7%
Russell 2000	9.7%	4.9%
MSCI EAFE	-4.6%	-8.1%
Barclays Agg	1.8%	6.0%

WHEN TO WORK WITH WINFIELD

PRIVATE INDIVIDUAL INVESTORS

- Manage accumulated wealth, inheritances and settlements to meet investment objectives

ENDOWMENTS AND FOUNDATIONS

- Manage assets with a long-term growth strategy while meeting investment policy requirements

BUSINESS OWNERS

- Customize investment portfolios to meet investment objectives and lessen risk of concentrated assets
- Defer taxable earnings in profit sharing plans
- Manage and advise 401(k) plans

BUSINESS PROFESSIONALS

- Customize investment portfolios, manage stock options and consolidate 401(k)/IRA plans to meet investment objectives and lessen risk of concentrated assets

RETIREES

- Customize investment portfolios to meet investment objectives with the option of drawing income
- Management of IRAs, trusts and taxable accounts

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www.winfieldinc.com

700 West St. Clair Avenue, Suite 404 • Cleveland, OH 44113

(216) 241-2575 • (888) 322-2575 • fax: (216) 241-4774