Schaper, Benz & Wise
INVESTMENT COUNSEL
Trusted Advisor for Generations

18 Jewelers Park Dr., Suite 200 | P.O. Box 628
Neenah, WI 54957-0628 | 920.727.1137

Economic & Market Summary
July 2015

Entering 2015 we expected relatively robust domestic economic conditions resulting from continuing consumption growth and stronger levels of residential and business investment. The current economic expansion, however, continues to be largely driven by consumption while investment remains uneven. Employment is trending higher which will lead to additional consumption growth, while supply shortages of skilled workers appear to be pressuring wages. To be fair, business investment has improved modestly in this recovery, yet we continually see share repurchases favored over investments in plant and equipment. Relatively subdued investment is likely leading to below-average productivity growth. An increase in merger and acquisition activity suggests risk aversion is abating to some degree. Meanwhile, housing has slowed during the last year as prices firmed, financing remains challenged, and consumer preferences have shifted toward rental and multigenerational arrangements. Yet it is clear underlying demand exceeds supply, particularly in the context of a growing birth rate. The U.S. is on pace for 2015 GDP growth of 2.5%.

A recent sell-off in the bond market has created modest buying opportunities. This reflects rising inflation data and a predicted Federal Reserve interest rate hike in September. The Fed's justification for a rate hike is inflation data, employment data, and unnecessarily accommodative policy. Importantly, market forces will likely move interest rates more than Federal Reserve policy, especially for intermediate and long-dated maturities. The probability for a larger sell-off in the bond market remains elevated.

Internationally, the specter of Greece leaving the European Monetary Union is leading news headlines. The outcome will have little real effect on the global economy. Fiscal leaders across the globe should take notice: Poorly designed and funded defined benefit programs along with rising debt levels can lead to asset devaluation and economic hardship. While markets have experienced heightened volatility, it is difficult to make the case for contagion outside of Greece. In fact, European economic growth has improved this year. Additionally, Japan's economy has seen some resurgence with a return to growth after annualizing last year's tax increase. Capital outflows resulting from a strengthening dollar is a risk in emerging markets, while relatively good equity performance has gone somewhat unnoticed.

The S&P 500's YTD 2015 total return was 1%. Earnings growth has been flat as a strengthening dollar and weak performance in the oil/gas sector have offset margin improvement and share repurchases. U.S. multinationals will continue to experience dampened revenues and profits if the dollar stays at current levels. One potential offsetting factor from a return perspective would be a higher P/E multiple as capital becomes attracted to assets held in a stronger currency. For the year, consensus earnings estimates are $115 per share, down slightly from 3 months ago and resulting in a P/E ratio of 18x. At current valuation the market is susceptible to downward pressure, but note markets tend to overshoot in both bull and bear markets, leaving open the potential for a higher P/E ratio. This year's negative domestic equity fund flows and falling earnings estimates offer some explanation as to relatively subdued S&P 500 returns. The universe of publicly-traded high quality businesses remains bountiful, but valuations are not nearly as attractive as just a few years ago.

Thomas H. Rippl, CFA

To request our SEC Form ADV Part II, please contact Michael L. Wise, Chief Compliance Officer, at the address above.