# Southeast Asset Advisors, Inc.
# Lanigan Wealth Management
## Investment Management & Consulting

**TO:** Clients and Friends
**FROM:** SEA/Lanigan Wealth Management Team
**RE:** Newsletter – Commentary
**DATE:** April 2015

***"Did it ever occur to you that there's no limit to how complicated things can get on account of one thing always leading to another?"*** **- E.B. White**

## First Quarter 2015 Market Recap

- U.S. stock indices were slightly positive this quarter. In a change from recent periods, international stocks generally outperformed the U.S. – despite the effects of weaker currencies relative to the U.S. dollar.
- Interest rates declined slightly over the quarter resulting in core bond gains for the fifth consecutive quarter. Interest rates in other major global bond markets remain very low, or in some cases negative (hard to believe)!
- Global monetary policy has strongly influenced financial markets as central governments try to follow the U.S. lead to inflate the price of assets with low or even negative interest rates.
- Fall in energy prices hurt the energy sector and should help the consumer. However, lower energy prices have not yet resulted in increased consumer spending.
- Continued slow growth in the general economy may delay Fed interest rate increases.
- M&A activity and stock buybacks (many at overvalued prices) continue to add fuel to the fire, moving passive indices to stretched, if not bubble levels. This has created an environment favorable for good active "bottom up" value managers.

## Valuation Comments

- We continue to believe the equity markets are no longer inexpensive on the whole (see our prior quarter letter), and fundamental valuations of most major indices (if valued as one company) indicate very low returns over the next seven or so years from present levels.
- However, the alternative to equities (bonds) actually look "bubbly." Interest rates will eventually rise as the Fed unwinds its artificial stimulus, potentially causing major losses in intermediate and long bonds and other yield assets.
- Short-term bonds and money markets continue to provide almost no return. The Fed, by design, has pushed investors to equities, real estate, and other risk assets, inflating prices.

- We increasingly worry about a drop in "profit margins," or a reversion to the mean from a historic top in margins, as labor price increases outweigh any productivity gains for many businesses.
- Multiple expansion for the broad market index appears to be very limited as it will be difficult for interest rates to go lower from these low levels, and current cash flow yields are very low at ~ 4.7% (~ 21 x FCF).
- Our value hedge fund managers are finding many shorts but very few qualifying longs.
- Most "bottom up" value managers (VM) that we use are having difficulty finding qualifying investments. However, they feel their portfolios are far superior to general equity indices in regard to valuation metrics and qualitative measures (see prior quarter letter for further comments on passive vs. active.) We expect returns to be lower than the last five years for both indexes and these managers, but believe our VM can provide reasonable returns over the next cycle and outperform general equity indices.

## Asset Allocation Comments and Summary

We are again putting increased emphasis on ensuring our clients have adequate cash reserves to fund any short-term needs. Also, we are looking to opportunistically increase our cash reserves over the next few months. The amount of cash reserves, of course, depends on goals and objectives of the individual client. We continue to overweight active value managers that "get it" and allow them to look globally to find great investments. As you know, we love managers who default to holding cash if they cannot find qualifying investments. We also invest with managers that are aligned with us and our clients (i.e., have a lot of their own money invested alongside us).

We continue to keep bond durations very short and look carefully for fixed income alternatives, being mindful that "yield chasers" are creating a bubble in many alternatives. We are not optimistic about finding many yield qualifiers.

In summary, we are taking an increasingly cautious approach to our equity allocation, but continue to prefer great "bottom up" value managers, a few "fat pitch" special equity holdings to the "not so good - to awful" alternatives thereto. Level "3" continues to be our favorite "fat pitch special equity" and, even after a substantial price increase, looks very promising. We view it as a conservative way to participate in the "internet of things" future wave.

## Closing

We are off to Omaha next week for the annual Berkshire Hathaway meeting where we will meet with many likeminded investors and managers. Berkshire remains (as it has for many years) one of our largest holdings, and we view it as our enhanced active alternative to the general indexes.

We expect increased volatility, but with the right client temperament, our proven disciplined process, (and our selected managers) we are confident that we can achieve reasonable risk adjusted and good relative returns within a client's parameters and goals, even though valuations are substantially more expensive than in late 2008.

As always, thank you for your confidence and trust. We are working hard on your behalf. Please contact any of our team if you desire to schedule a personal conference at any time.

Your Investment Team,

Bernard Lanigan, CPA
Chairman & CEO

Brad Jackson, CPA, CFA
President

Mark Saussy, CPA, CFP, CIMA
Executive V.P. & COO

***"Preparation, patience, discipline, and decisiveness – one without the other is useless."*** **– Author Unknown**