

# HUDSON ADVISOR SERVICES, INC

## OUR VIEW OF THE MARKET

By William N. Hudson, Jr., David D. Burrows, William Hudson III, Evan Coppola, & Jeremy Hudson

We looked at the commentary we published in January and then in March. We explained that the market in 2015 would struggle to repeat its impressive performance in 2013 and 2014. We said the mixed economic news would keep the market in a narrow trading range. As the year unfolds, that prediction has turned out to be quite on the mark.

We did not specifically anticipate the distracting impact of the Greek crisis. The market was showing positive movement in April and May – but then hit the skids in June as the Greek leaders and their European creditors played brinkmanship. The July 5 referendum – in which 61% of Greek voters rejected further austerity – has caused more trepidation. No one knows what exactly will happen now and the uncertainty may keep markets unsettled for the period ahead.

We prefer to put the Greek situation in perspective. The crisis is really more political than economic. The gross national debt of Greece is about \$250 billion – only 1% of the European Union's total annual economic output. We simply do not believe European leaders will allow this problem to create widespread damage to the Euro currency or to the European Union itself. Some sort of compromise will be identified. At the same time, we are keeping a close eye on the Chinese financial markets, and the potential for slower growth. A major downturn in China's economy could have a significant impact on U.S. and global markets.

Thus, at Hudson Advisors, we are staying primarily focused on the U.S. economy. We will be watching all the signs that foretell future direction. Stock prices cannot move much higher until the earnings part of the P/E ratio shows more strength. Corporate earnings cannot improve until the trends of economic growth become firmer and clearer. In the meantime, the market should continue to move pretty much sideways.

### MARKET TRENDS

The accompanying chart summarizes stock and bond market prices in the first half of 2015. The stock market showed momentum for most of the second quarter -- after a flat performance in the first quarter – but then retreated in the face of the news from Greece. Meanwhile, the U.S. Treasury market suffered from the overall economic doubt.

Volume 64

July 2015

**Equity Market:** Stocks moved higher in April and reached record levels in May. These gains were then reversed in June as the Greece crisis worsened and the U.S. economic outlook turned more cloudy. The Dow Jones Industrial Average fell 0.29% for the second quarter and was up 0.03% for the year. The S&P 500 Index increased 0.28% for the quarter and was ahead just 1.23% for the year. In contrast, the Nasdaq Composite Index continued to win investor attention on the belief that technology's potential outweighs its risks. The index gained 1.46% for the quarter and was ahead 5.52% for the year. The Russell 2000 index was basically flat for the quarter – but held its first quarter gain and was ahead for the year by 4.75%.

**Fixed Income Market:** Many investors seem convinced the Federal Reserve will soon begin to increase interest rates – for the first time since 2006. This belief was reflected in a negative quarter for bond prices after five consecutive quarters of gains. The yield on the 10-year Treasury note – which moves inversely to prices – rose to 2.339% at the close of the quarter versus 1.930% three months earlier. Bonds in the Eurozone also were thrashed as investors perceived deflation there is ending and that inflationary growth looms ahead. The benchmark German 10-year bond finished the quarter at .77% after hitting a record low of .05% in mid-April.

### MAJOR MARKET INDEXES

|                               | 2Q Total Return | YTD Total Return |
|-------------------------------|-----------------|------------------|
| Dow Jones Industrials         | -0.29           | 0.03             |
| S&P 500 Index                 | 0.28            | 1.23             |
| Russell 2000 Index            | 0.42            | 4.75             |
| NASDAQ Index                  | 1.46            | 3.79             |
| EAFE Index NR                 | 0.62            | 5.52             |
| Barclays Aggregate Bond Index | 0.01            | 0.03             |

\*Total Return Includes Reinvested Dividends.

### THE OUTLOOK

**The Economy:** As indicated, our primary attention is on the U.S. economy. In March, we quoted the widespread view that annual growth in 2015 would be in the 2.5% to 3% range. That forecast is now generally believed to be somewhat below 2%. What explain this lower expectation? First, the demand from domestic consumers is wobbly. New job growth has jumped around in the last six months – averaging 236,000 per month – somewhat

lower than the prior six months. But, more significant, wage growth is not strong enough. Yes, the aggregate weekly wage of all U.S. workers in May was increased by 4.6% from a year earlier. But consumers show heavy inclination to be careful with their money. Second, multinational companies are affected by the still strong U.S. dollar and the still uncertain economies in Europe and Asia.

Unlike many market analysts, we are not obsessed with the future decisions of the Federal Reserve. We think the Fed will act with measured restraint. At most, they may decide to raise interest rates 25 basis points by year-end. But rates will remain historically low and the economic impact will be modest.

**The Market:** As always, the direction of the market is primarily influenced by how investors perceive stock valuations. Presently, the S&P 500 trades at 18 times the prior 12 months of earnings – up from a price/earnings ratio of 17.1 at the start of 2015. The 10-year average P/E for the index is 15.7. So, stock prices now are relatively rich.

As mentioned already, the earnings part of this equation is the key to watch. The aggregate outlook for corporate earnings is somewhat confused by the negative performance of the energy companies. Thus, stripping out the energy sector, all other companies in the S&P 500 are expected to show average profit growth of 2.2% for the second quarter over the prior year. That growth may be too low to push stock prices higher. However, the market could be moderately encouraged if actual earnings beat those expectations. There is reasonable hope for stronger-than-anticipated earnings in the health care, technology, and financial sectors.

On balance, we do not foresee the Dow Jones or S&P 500 showing much upward movement in the second half. In January we said those indexes might have potential for

4 to 8% increase in 2015. We now expect that year-end performance to be lower and just slightly positive.

## OUR STRATEGIES

**Asset Allocation:** For clients investing new money, same as last quarter, we recommend 55% allocation to equities and the remaining portion to cash, bonds with maturities under two years, and alternative investments. We suggest fully invested clients to trim equities to 55-65% depending upon time horizon and objectives.

**Preferred Equities:** We remain focused on large cap companies with strong balance sheets, sustainable cash flows, and credible business models. Companies that pay attractive dividends are central to our strategy. Some of the sectors we are like are similar to those indicated last quarter:

- **FINANCIALS:** The stocks of insurance companies and some banks have attractive value.
- **TECHNOLOGY:** Some technology companies have room for further growth – especially those with innovative consumer products.
- **HEALTH CARE:** We are attracted to some pharmaceutical companies because of new products coming to market.
- **INTERNATIONAL:** Emerging market stocks have been underperformers in recent years – and have not been our friend. But we anticipate them to rebound in the period ahead.

**Fixed Income:** We are gratified to see the market come around to accept our long-expressed aversion to long-term bonds. When the Fed does finally raise interest rates – even if the macro economic impact is limited – the effect on bond portfolios will be sharp and adverse. We think investors are correct finally to be moving towards our viewpoint.

### Dow Jones U.S. Sectors (Percent Change for YTD, Ending June 30, 2015)

|                        |              |                           |               |
|------------------------|--------------|---------------------------|---------------|
| <b>Oil &amp; Gas</b>   | <b>-3.98</b> | <b>Consumer Services</b>  | <b>4.71</b>   |
| <b>Basic Materials</b> | <b>-1.37</b> | <b>Telecommunications</b> | <b>3.79</b>   |
| <b>Industrials</b>     | <b>-0.34</b> | <b>Utilities</b>          | <b>-10.73</b> |
| <b>Consumer Goods</b>  | <b>1.23</b>  | <b>Financials</b>         | <b>0.49</b>   |
| <b>Health Care</b>     | <b>10.78</b> | <b>Technology</b>         | <b>0.85</b>   |

#### William Hudson, Jr., Jeremy Hudson, & Evan Coppola

4445 North Hwy A-1-A, Suite 233 • Vero Beach, Florida 32963 • (772) 231-8101  
237 Main Street, Suite 600 • Buffalo, New York 14203 • (877) 504-1964

#### William Hudson, III CFP®

6701 Democracy Blvd, Suite 300 • Bethesda MD 20817 • (301) 840-2071

#### David Burrows & Elizabeth Kisken CFA®

29 Hillside Drive • Greenwich, CT 06830 • (203) 302-3530

[www.hudsonadvisors.com](http://www.hudsonadvisors.com) • (877) 504-1964

**Hudson Advisor Services Inc.**  
**Market Data 2nd Quarter 2015**

**Bottom 15% Percentile YTD through 6/30/15 (US Listed stocks with am market cap over \$1 Billion)**

| RIC      | Company Name                       | Market Capitalization (USD, Millions) | Total Return, YTD (%) |
|----------|------------------------------------|---------------------------------------|-----------------------|
| BTU.N    | Peabody Energy Corp                | 608.34                                | -71.64%               |
| LL.N     | Lumber Liquidators Holdings Inc    | 560.85                                | -68.77%               |
| ALSE.PK  | Alseres Pharmaceuticals Inc        | 1,991.32                              | -67.50%               |
| APOL.OQ  | Apollo Education Group Inc         | 1,387.36                              | -62.24%               |
| CZR.OQ   | Caesars Entertainment Corp         | 885.54                                | -60.99%               |
| HMCP.PK  | Heritage Media Corp                | 703.58                                | -60.00%               |
| SSYS.OQ  | STRATASYS LTD                      | 1,781.99                              | -57.97%               |
| IEGHD.PK | leg Holdings Corp                  | 593.48                                | -57.69%               |
| CENX.OQ  | Century Aluminum Co                | 905.40                                | -57.25%               |
| SBLK.OQ  | Star Bulk Carriers Corp            | 643.67                                | -55.18%               |
| LE.OQ    | Lands End Inc                      | 793.48                                | -53.98%               |
| FPCG.PK  | First Physicians Capital Group Inc | 9,829.75                              | -51.92%               |
| ONDK.N   | ON DECK CAPITAL INC                | 805.03                                | -48.37%               |
| WIN.OQ   | Windstream Holdings Inc            | 643.26                                | -47.76%               |
| TRUE.OQ  | TrueCar Inc                        | 982.49                                | -47.64%               |
| MU.OQ    | Micron Technology Inc              | 20,376.22                             | -46.19%               |
| CEQP.N   | Crestwood Equity Partners LP       | 769.93                                | -45.62%               |
| ZU.OQ    | Zulily Inc                         | 1,610.12                              | -44.27%               |
| KORS.N   | Michael Kors Holdings Ltd          | 8,372.21                              | -43.95%               |
| I.N      | Intelsat SA                        | 1,054.50                              | -42.86%               |
| CHK.N    | Chesapeake Energy Corp             | 7,429.56                              | -42.03%               |
| HLX.N    | Helix Energy Solutions Group Inc   | 1,337.69                              | -41.80%               |
| LC.N     | LendingClub Corp                   | 5,491.63                              | -41.70%               |
| GMCR.OQ  | Keurig Green Mountain Inc          | 11,798.64                             | -41.47%               |
| ORIG.OQ  | Ocean Rig UDW Inc                  | 825.36                                | -40.62%               |

**Top 15% Percentile YTD through 6/30/15 (US Listed stocks with am market cap over \$1 Billion)**

| RIC     | Company Name                   | Market Capitalization (USD, Millions) | Total Return, YTD (%) |
|---------|--------------------------------|---------------------------------------|-----------------------|
| ROGP.PK | Royale Globe Holding Inc       | 3,384.12                              | 483.33%               |
| EGRX.OQ | Eagle Pharmaceuticals Inc      | 1,258.54                              | 421.68%               |
| NHTC.OQ | Natural Health Trends Corp     | 521.42                                | 262.88%               |
| HRTX.OQ | Heron Therapeutics Inc         | 1,095.17                              | 209.74%               |
| SGYP.OQ | Synergy Pharmaceuticals Inc    | 830.38                                | 172.13%               |
| COCP.OB | Cocrystal Pharma Inc           | 790.18                                | 171.43%               |
| RTRX.OQ | Retrophin Inc                  | 1,158.96                              | 170.83%               |
| HZNP.OQ | Horizon Pharma PLC             | 5,367.29                              | 169.51%               |
| EXEL.OQ | Exelixis Inc                   | 736.67                                | 161.11%               |
| ADPT.N  | Adeptus Health Inc             | 1,990.04                              | 153.98%               |
| ADXS.OQ | Advaxis Inc                    | 638.29                                | 153.81%               |
| PRTA.OQ | Prothena Corporation PLC       | 1,647.83                              | 153.71%               |
| ANAC.OQ | Anacor Pharmaceuticals Inc     | 3,387.81                              | 140.09%               |
| ZIOP.OQ | ZIOPHARM Oncology Inc          | 1,538.79                              | 136.69%               |
| IMGN.OQ | Immunogen Inc                  | 1,239.34                              | 135.74%               |
| HALO.OQ | Halozyme Therapeutics Inc      | 2,873.54                              | 133.99%               |
| RARE.OQ | Ultragenyx Pharmaceutical Inc  | 3,676.07                              | 133.34%               |
| AGEN.OQ | Agenus Inc                     | 712.04                                | 117.38%               |
| KYTH.OQ | KYTHERA Biopharmaceuticals Inc | 1,953.46                              | 117.16%               |
| ISLE.OQ | Isle of Capri Casinos Inc      | 736.89                                | 116.85%               |
| NBIX.OQ | Neurocrine Biosciences Inc     | 4,079.55                              | 113.79%               |
| CONN.OQ | Conns Inc                      | 1,445.49                              | 112.41%               |
| SRPT.OQ | Sarepta Therapeutics Inc       | 1,261.81                              | 110.30%               |
| RGEN.OQ | Repligen Corp                  | 1,355.81                              | 108.43%               |
| SUPN.OQ | Supernus Pharmaceuticals Inc   | 811.01                                | 104.58%               |

**Hudson Advisor Services, Inc. 2nd Quarter 2015 Focus List**

| Ticker  | Company Name                     | Sector                 | Ticker | Company Name                    | Sector                     |
|---------|----------------------------------|------------------------|--------|---------------------------------|----------------------------|
| NKE     | Nike Inc                         | Consumer Discretionary | GD     | General Dynamics Corp           | Industrials                |
| TIF     | Tiffany & Co                     | Consumer Discretionary | TYC.N  | Tyco International PLC          | Industrials                |
| foxa.o  | Twenty-First Century Fox Inc     | Consumer Discretionary | SWK    | Stanley Black & Decker Inc      | Industrials                |
| CMCSA.o | Comcast Corp                     | Consumer Discretionary | DE     | Deere & Co                      | Industrials                |
| DIS     | Walt Disney Co                   | Consumer Discretionary | BA     | Boeing Co                       | Industrials                |
| sbux.o  | Starbucks Corp                   | Consumer Discretionary | UTX    | United Technologies Corp        | Industrials                |
| tjx     | TJX Companies Inc                | Consumer Discretionary | LLL    | L-3 Communications Holdings Inc | Industrials                |
| UA      | Under Armour Inc                 | Consumer Discretionary | LMT.N  | Lockheed Martin Corp            | Industrials                |
| cbs     | CBS Corp                         | Consumer Discretionary | UPS    | United Parcel Service Inc       | Industrials                |
| VFC     | VF Corp                          | Consumer Discretionary | LUV    | Southwest Airlines              | Industrials                |
| MCD     | McDonald's Corp                  | Consumer Discretionary | GOOG.o | Google Inc                      | Information Technology     |
| TSN     | Tyson Foods Inc                  | Consumer Staples       | AAPL.o | Apple Inc                       | Information Technology     |
| SJM     | J M Smucker Co                   | Consumer Staples       | AVGO.o | Avago Technologies Ltd          | Information Technology     |
| STZ     | Constellation Brands Inc         | Consumer Staples       | mbly.n | Mobileye NV                     | Information Technology     |
| HAIN.o  | Hain Celestial Group Inc         | Consumer Staples       | fb.o   | Facebook Inc                    | Information Technology     |
| CVS     | CVS Health Corp                  | Consumer Staples       | MA     | MasterCard Inc                  | Information Technology     |
| PM      | Philip Morris International Inc  | Consumer Staples       | msft.o | Microsoft Corp                  | Information Technology     |
| PG      | Procter & Gamble Co              | Consumer Staples       | INTC.o | Intel Corp                      | Information Technology     |
| TAP     | Molson Coors Brewing Co          | Consumer Staples       | STX.o  | Seagate Technology PLC          | Information Technology     |
| PEP     | PepsiCo Inc                      | Consumer Staples       | CE     | Celanese Corp                   | Materials                  |
| MO      | Altria Group Inc                 | Consumer Staples       | lyb    | LyondellBasell Industries NV    | Materials                  |
| CL-N    | Colgate-Palmolive Co             | Consumer Staples       | DD     | E I du Pont de Nemours and Co   | Materials                  |
| VLO     | Valero Energy Corp               | Energy                 | IP     | International Paper Co          | Materials                  |
| XOM     | Exxon Mobil Corp                 | Energy                 | SHW    | Sherwin-Williams Co             | Materials                  |
| KMI.N   | Kinder Morgan Inc                | Energy                 | MPW    | Medical Properties Trust Inc    | REIT                       |
| AIG.N   | American International Group Inc | Financials             | SSS    | Sovran Self Storage Inc         | REIT                       |
| gs      | Goldman Sachs Group Inc          | Financials             | PSA    | Public Storage                  | REIT                       |
| MET     | Metlife Inc                      | Financials             | AMT    | American Tower Corp             | REIT                       |
| MTB     | M&T Bank Corp                    | Financials             | NLY    | Annaly Capital Management Inc   | REIT                       |
| COF     | Capital One Financial Corp       | Financials             | VOD.I  | Vodafone Group PLC              | Telecommunication Services |
| C       | Citigroup Inc                    | Financials             | VZ     | Verizon Communications Inc      | Telecommunication Services |
| JPM     | JPMorgan Chase & Co              | Financials             | t      | AT&T Inc                        | Telecommunication Services |
| GILD.o  | Gilead Sciences Inc              | Health Care            | APU    | Amerigas Partners LP            | Utilities                  |
| CELG.o  | Celgene Corp                     | Health Care            | SPH    | Suburban Propane Partners LP    | Utilities                  |
| BMJ     | Bristol-Myers Squibb Co          | Health Care            | D      | Dominion Resources Inc          | Utilities                  |
| ABBV.n  | AbbVie Inc                       | Health Care            |        |                                 |                            |
| BAX     | Baxter International Inc         | Health Care            |        |                                 |                            |
| ZTS     | Zoetis Inc                       | Health Care            |        |                                 |                            |