Second Quarter 2016

# GALECKI FINANCIAL MANAGEMENT FINANCIAL SENSE

| | LAST MONTH | LAST 3 MONTHS | YTD |
|---|---|---|---|
| **S & P 500 Index** | 6.78% | 1.35% | 1.35% |
| **Russell Midcap Index** | 8.19% | 2.24% | 2.24% |
| **Russell 2000 Index** | 7.98% | -1.52% | -1.52% |
| **Dow Jones Industrial Average** | 7.22% | 2.20% | 2.20% |
| **Morgan Stanley EAFE Index** | 6.51% | -3.01% | -3.01% |
| **MSCI US REIT Index** | 10.42% | 6.31% | 6.31% |
| **DJ UBS Commodity Index** | 3.82% | 0.42% | 0.42% |
| **Barclays Aggregate Bond Index** | 0.92% | 3.03% | 3.03% |

## INDEX RETURNS

The markets in the first quarter took investors on a wild ride. The first six weeks of the year brought solid corrections among most indexes. The S&P 500 experienced an 11% correction, while small cap stocks were down 16% and the MSCI EAFE index had a 12% drop. Around February 11, the price of crude oil bounced off $26 per barrel, and began a nice recovery. Stocks have largely followed suit since that point.

U.S. Large cap stocks ended the quarter up 1.35% after going through the 11% early decline. The strong recovery in large cap stocks coincided with the stabilization of oil prices. This stabilization should help earnings recover, especially in the energy sector.

Mid-cap and Small-cap stocks also experienced a lot of volatility in the first quarter. Although mid-cap stocks are now positive on the year, small cap stocks as measured by the Russell 2000 are down 1.52% year to date.

The bond market had a big quarter with the Barclays Aggregate Bond Index increasing 3.03% over the first three months. Even Emerging Market bonds increased 5.34% in the first quarter.

## ECONOMIC REVIEW AND OUTLOOK

The economy grew at a 1.0% annualized rate in the fourth quarter of last year. This followed the 2.0% growth rate in the third quarter. This means that the economy grew 2.4% in 2015 which was equal to the 2.4% rate in 2014. In both cases, the first quarter was negative, while the last three quarters were positive. We believe this will again be the case in 2016. The first quarter GDP number is likely to be slightly negative again. The key will be generating the same strong comeback in the second quarter like we have seen the last two years.

GALECKI FINANCIAL MANAGEMENT
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25
YEARS

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The Leading Economic Index increased 0.1% in February to 123.2 following a slight decrease in January. The index has risen 0.3% over the last six months suggesting that the economy should continue to grow at a modest pace. Industrial Production decreased 0.5% in February after increasing 0.8% in January and the Capacity Utilization rate dropped to 76.7 percent. This is 3.3 percentage points below the historical average over the last forty years and suggests that there will not be much pricing pressure in manufacturing over the next few quarters.

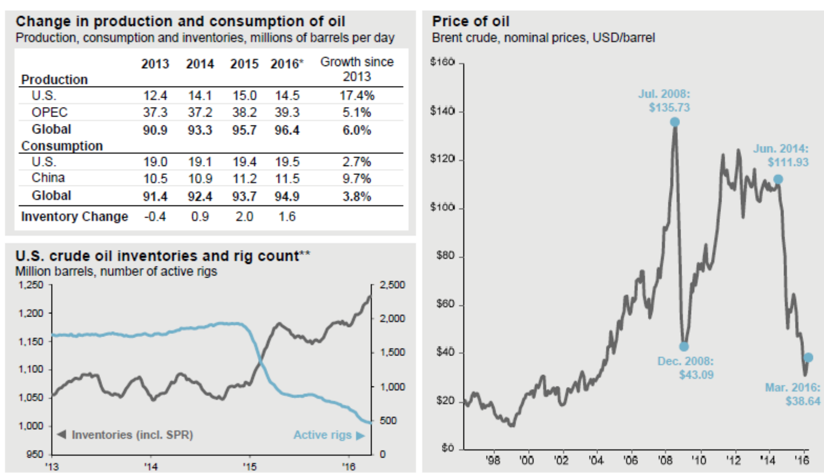
Non-farm payrolls increased by 215,000 in March and the unemployment rate is 5.0%. This suggests that the economy is near full employment. Initial weekly unemployment claims were 267,000 for the week ending April 2. According to the JOLTS survey, there were 5.4 million job openings in February.

Manufacturing saw a jump in March as the ISM PMI index moved to 51.8% which is back in expansion territory for the first time in six months. The ISM Non-Manufacturing index came in at 54.5% in March. This index continues to show solid growth for the service sector, which is roughly 88% of our economic output.

Global economies are beginning to show some strength in certain areas. The JP Morgan Global PMI was at 50.5 in March up 0.5% from February. The Emerging economies are averaging 48.8. This is considered contraction territory but many countries are growing. China, Indonesia, Korea and Taiwan all showed better numbers in March. The Eurozone PMI has dropped to 51.6 and appears to be cooling. Softness in France, Germany and Greece contributed to the slight decline from prior quarters.

## EQUITY AND BOND MARKETS

Equity markets went on a wild roller coaster ride in the first quarter, only to end up roughly where they started. The first six weeks was like Jordan Spieth's 12th hole at the Mastersé not good. The decline in crude oil prices made investors nervous that the energy sector would see many companies shut down their operations. The potential ripple effect into other sectors was the main concern. In February, the price of Brent crude oil dipped to $26 per barrel. It has now recovered to around $40 per barrel.



**Change in production and consumption of oil**
Production, consumption and inventories, millions of barrels per day

| | 2013 | 2014 | 2015 | 2016* | Growth since 2013 |
|---|---|---|---|---|---|
| **Production** | | | | | |
| U.S. | 12.4 | 14.1 | 15.0 | 14.5 | 17.4% |
| OPEC | 37.3 | 37.2 | 38.2 | 39.3 | 5.1% |
| **Global** | **90.9** | **93.3** | **95.7** | **96.4** | **6.0%** |
| **Consumption** | | | | | |
| U.S. | 19.0 | 19.1 | 19.4 | 19.5 | 2.7% |
| China | 10.5 | 10.9 | 11.2 | 11.5 | 9.7% |
| **Global** | **91.4** | **92.4** | **93.7** | **94.9** | **3.8%** |
| Inventory Change | -0.4 | 0.9 | 2.0 | 1.6 | |



The chart above shows the drop in active oil rigs from roughly 2,000 down to around 500. However, efficiencies have driven production higher and have increased oil inventories. So while the recent surge in oil prices has helped spark an equity rally, the second leg will need to come from another source.

One of the potential sources could be a weakening in the U.S. Dollar. After two solid years of appreciation versus other currencies, the dollar softened in the first quarter. In fact, the dollar has dropped to $1.14 vs. the Euro after reaching $1.06 late last year. If this trend continues, it will have a big impact on domestic earnings, (since roughly 48% of revenue comes from outside of the U.S. for S&P 500 companies) as well as international market returns.

In 2015, the Developed International Market (EAFE) was up 5.8% in local currencies, but was down 0.4% in U.S. Dollars. Emerging markets were down 5.4% in local currencies, but dropped 14.6% in Dollar terms. This trend has changed in the first quarter of this year. The EAFE index was down 6.9% in the first quarter in local currencies but was only down 2.9% in U.S. Dollars. Emerging markets were up 2.8% locally in Q1, but that translated into a 5.8% gain in Dollar terms. If this trend continues, diversified investors will see big benefits in 2016.

The bond market has been interesting so far in 2016. The Federal Reserve raised interest rates in December by 0.25%, but has now indicated that they might only raise target rates twice in 2016. This would mean that the Fed funds rate would still be less than 1% by the end of the year. Subsequently, yields have dropped and bond prices have increased. The 10 year yield on US Treasuries is now around 1.8% after beginning the year at 2.27%.

## PORTFOLIO MANAGEMENT

As mentioned in the first quarter newsletter, we began the year with our most conservative approach since 2007. We created a cash position to decrease risk and increase flexibility. We altered our fixed income investments to decrease their correlation with equities and provide more true principal protection. We decreased our alternative investment allocation. We modified our equities to larger companies, with more of a U.S. focus.

The changes that were made allowed the portfolios to handle the January/February correction quite well. With the cash position, the portfolios were well positioned to recover the last 7 weeks of the quarter. Some of the cash has been deployed back into U.S. equities over the last 6 weeks. We still have about half of the cash available if an opportunity presents itself.

Meanwhile, the market has largely recovered most of its earlier losses. So, where do we go from here? There is still plenty of concern. Earnings season is just beginning, and expectations are relatively low. The Federal Reserve has lowered guidance on future hikes, but other central banks around the globe are dropping rates (Some are even negative). In addition, we have a Presidential election in the fall. However, we believe that a recession in the short-term is unlikely and earnings will recover over the next few quarters. If this occurs, equities will offer a better return than bonds. Stay diversified and keep a long-term perspective. We know it works over time.

## FINANCIAL PLANNING

We are now three months into the New Year and taxes are already due. It is important to review some common planning items for 2016 and beyond. Here are a few places to start.

- Review your pay stub ï Make sure you are withholding enough in taxes so there are no surprises.
- Defer into your retirement plan ï Try to defer the maximum amount for your plan and your age. At the very least, defer the percentage that your company matches. Remember that if your spouse is not working, you can still contribute to a deductible or non-deductible IRA depending on your income level.
- Review your asset allocation ï If you are not utilizing an Advisor to help manage your assets, you should review your allocation annually to make sure you have the appropriate risk in your portfolio.
- Safe Guard against Fraud ï We recommend that all clients freeze their credit, not just monitor it. It is free for Indiana residents to freeze their credit. We assist our clients with this process.
- Qualified Charitable Deductions (QCDs) ï If you are over age 70.5 and are charitably inclined, consider making charitable donations directly from your IRA. The limit is $100,000 per year.
- Roth conversion ï Consult your tax advisor to see if converting some money to a Roth makes sense.

Here are some smart phone apps that we think you might enjoy. Please let us know if you have any new apps that you would like to share with everyone.

- **Bitmoji Keyboard**: This application allows you to create your own personal Avatar emoji that you can use when texting right from your keyboard. The app is free and adds a personal touch to your texting communications.
- **Google Photos**: Google Photos is a great way to back up all of your photos and videos for free. They are organized and labeled automatically. The application has an assistant that creates collages and videos from your pictures. This is a must have! It is a free application.
- **CamScanner:** This application allows you to use your phone as a portable scanner. Take a picture of a document and save it as a PDF. You can then organize the files, or share them via email, fax, print or save to the cloud. This application is free on most platforms.

## Company News

Galecki Financial Management has been very active in the Fort Wayne community and surrounding areas. In addition to being major sponsors for the Isaac Knapp Dental Society, Camp Watcha-Wanna-Do Golf Outing, the Jyothi Foundation, and the Shruti Foundation, we have also been busy in other roles.

Greg Galecki, CFP® our founder and president is on the Board of Directors and Treasurer for Fort Wayne Trails Inc. He has been volunteering his time and resources over the last few years to growing our existing trail system and keeping it updated and safe. They now have 90 miles of trails with a goal of 100 in the next few years.

Brady McArdle, CFP® has been serving on NAPFA’s Midwest Region Board for the last year. NAPFA is the National Association of Personal Financial Advisors. It is the primary professional organization for Fee-Only firms like Galecki. Brady has also been serving on the Finance Committee for the Fort Wayne Country Club and is the co-chair for the 2016 Invitational. Brady recently retired from coaching tennis after nine years at Bishop Luers High School.

Melanie Colwell, CFP® is on the Board of Directors for Whitington Homes and Services in Fort Wayne. Whitington serves children and families in their homes that are at risk or in crisis. Whitington has case managers and therapists that go into homes and support and stabilize these families. Melanie has also been reaching out to the community as a Certified Divorce Financial Analyst, helping women in transition.

A.T. Kohout, CFP® has been serving on the Board of Directors for the Fort Wayne Museum of Art. The Museum has many different exhibits and events that truly enhance the culture of the community. A.T. also serves on the investment committee for the Fort Wayne Community Foundation and the Questa Foundation. Their mission is to help local individuals complete degrees with less debt so they will be contributing members to our region.

*- Galecki Financial Management Investment Committee*

**Special Note: If you would like to schedule an appointment with a Certified Financial Planner™ Professional, please visit [www.galecki.com](http://www.galecki.com).**