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Greetings,

The most hated, disrespected market that I have ever seen continues to march on. In addition to watching the economic fundamentals as well as corporate earnings, I do pay attention to market sentiment. On occasion, I hear some talking heads on CNBC chat about their concerns that there is too much complacency in the market. Surprisingly, there has been a lack of volatility and the market has gone straight up since the election. I don't equate a lack of volatility and market strength with complacency. I occasionally like to chat with people about the market. I don't sense anything resembling the euphoria of 1999 and early 2000 and I consider that a good thing! I don't even get the same feeling as I had back in 2006 and 2007 from people. The feeling I get from most people now is caution. There is still no real trust with this market.

I think the reasons are a combination of several factors. Many people are still affected psychologically from the markets decimation of 4 ½ years ago. I believe that what happened in 2008 and early 2009 will keep some people out of stocks permanently. That is bad for them but good for the markets since some people simply don't belong in equities. Part of the problem back in 1999 is that many people were jumping in when they should have stayed in fixed income. Now, there are people who should be in the market but are staying in over priced bonds. Another factor is the poor economy. The fourth quarter GDP was just revised down to a 0.4% annualized growth rate. If anyone is thinking that you can't do well in the stock market in a very slow growth economy, then they are badly mistaken. In a zero interest rate environment, as long as we are not in a recession, the market can do well. The third factor is the total dysfunction in Washington D.C. The political situation has kept some people on the sidelines who might ordinarily want to put some cash to work.

As long as the politicians don't sling mud at each other on TV most days as they did during the summer of 2011, then the market will ignore the noise. If anything, this last quarter the market has shown that it can totally tune out the politicians. As long as both sides don't play a game of chicken with the debt ceiling, Washington D.C shouldn't affect the markets. It has helped that the Republicans have become smarter and more selective in which fights they will pick with the President, who they are now stuck with for the next 3 years and nine months, whether they like it or not.

I look at the markets and the economy now and then I tend to look back to 2011 when the market finished exactly flat for the year. In my view, the economy really isn't that much better now than it was 2 years ago when the market did nothing. As mentioned, the fourth quarter GDP grew at less than a 1% annual rate. You don't need me to point out that isn't very good.

One of the reasons that the market is doing better now is because the market is forward looking and perception is now becoming reality. Back in 2011, while the economy wasn't good, it really wasn't so bad that it warranted the market to be flat. That was one of the reasons I was so frustrated back then. The economy wasn't that bad, corporate earnings were great plus stocks were cheap to boot! Yet stocks did nothing so PE multiples contracted. There was a huge amount of uncertainty mostly because many of the naysayers thought (incorrectly) that the problems of Europe would spread to the U.S economy and cause a recession here. Money flooded out of cheap stocks and into expensive bonds. Europe's problems have stayed over there. While corporate profits are not good right now (partly because of Europe's recession), the market seems to think that the domestic economy will pick up later on in the year and that things in Europe won't get worse. That (along with the Federal Reserve continuing to pump cash into the markets each month) is one of the reasons why PE multiples have expanded this year.

What I find interesting this year is that the market has done this well without a rotation from fixed income to equities. Once that happens, the market should do even better than it is now since stocks are under owned based on historical asset allocations. There have been net inflows into equity mutual funds this year but the amounts have been insignificant.

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