OPTIVEST

Turning Success into Peace of Mind.

Quarterly Newsletter

Contact Us

24901 Dana Point Harbor Drive
Suite 230
Dana Point, California 92629
949-363-8686

or visit our website:
www.optivestinc.com

Second Quarter 2013

US & World Economy - Animal spirits are back! With Europe in a mild but stable recession, China on an upswing, US housing starts and prices rising (Case Shiller Index up 8.1% over the last 12 months ending in January – best since 2006), and the Dow Jones and S&P 500 both making new all-time highs, consumers and businesses alike are feeling better. Consider these new economic levels: the stock market at new highs from 2007, S&P 500 quarterly earnings at new highs, US household net-worth at a new high ($69 trillion vs. $67 trillion), and household debt service to income ratios at a 30 year low (J.P. Morgan).

Are we finally back to "normal"? Yes, but still in slow motion. A slow motion which, in a way, is a good thing because if we had a "normal" dynamic rebound from the recession four years ago, we would be nearing the end of a business cycle already. As it stands with unemployment still high and valuations reasonable (particularly compared to interest rates), the economy will likely continue to expand for another couple of years before the next peak.

While stocks and real estate advanced this quarter, both commodities and bonds dropped which is unusual as the two tend to move in opposite directions depending on inflation. We believe this was because all the investment focus was on US stocks and the capital to purchase them was pulled from these two sectors. Over the months and quarters ahead, this will be self-correcting and if stocks keep advancing, commodities will rise; if stocks fall, bonds will rise.

US Stocks- The US economy, as reflected by the stock market, had a great first quarter with the S&P 500 up about 10.6% at 1569 (and within the low end of our 1550-1600 full year target). This gain is very similar to the gains in the first quarters of 2010, 2011 and 2012. Each of these last three big first quarters was followed by drops of 10-19%. After a 16% run up over the last 4 ½ months, the stock market might again be vulnerable for a 5% pullback before meaningful new highs emerge later in the year. Given this, we tactically reduced our US equity exposure near the end of the quarter. However, as you will read below, we like the US stock market over the rest of the decade. If you can absorb moderate volatility, we suggest that you stick with stocks for the long-term.

Fixed Income - One consequence of the slow economic recovery is the lack of inflationary pressure. We all "know" it is eventually going to rise along with interest rates – but despite being ready, it has not happened yet and may not for 6-18 months. However, we recognize the damage that rising inflation/interest rates can and/or will have on long-term bonds. We have already transitioned to shorter term bonds, floating rates and inflation hedges, choosing to be early (giving up some extra cash flow from longer bonds) rather than risk being late.

The End of the Lost Decade– Much has already been written about America's current "lost decade" where incomes, stocks and real estate prices have not meaningfully advanced since the turn of the century. This has happened twice since World War II; once in the 1950's and again in the 1970's. When these extended flat periods ended, they launched a 15-18 year run of remarkable performance. I believe the stage is now set for a similar advance over the next decade and a half.

Our economic/valuation peak in the early 2000's was the end of the breakout run that started in 1982. Like most significant long-term peaks, we were over-valued then largely because of the belief in new technology and the Internet's promise of unending gains. These two factors did in fact change how commerce, lifestyle and entertainment are now conducted, that change just took a decade to happen.

Today, the technological benefits of worldwide price efficiencies, a reduction of middlemen (travel agents, stock brokers, etc.), and the popularity of smart phones have finally started to fulfill the "dream." These same efficiencies have created enormous savings for consumers and businesses at the expense of jobs. This digital disruption is not over and the winners and losers are coming and going at an increasingly rapid pace. Speed to market, viral Internet marketing/awareness, virtual companies and global access are converging on every marketplace. The results will be wealth creation, efficient use of material resources (less inventory, waste, office use, energy, etc.) and eventually new jobs that produce a significant increase in output compared to old jobs. In addition, abundant domestic natural gas and advancements in its recovery are moving the US toward lower energy costs and independence. These are the types of game-changing economics that can and should propel America - and secondarily the world - to the next breakout period of economic and asset growth.

On January 19, 2011 we wrote a white paper entitled "A Rational Argument for a 15,000 Dow Jones in 2013" (see our website). Further, the article predicted a 25,000 Dow Jones by 2020. Our analysis continues to suggest these outcomes. There will certainly be at least one recession over the next seven years and probably wars, inflation and financial crisis. Yet, the American economy will again survive and continue to make new highs.

Summary - With the drama in Washington moving into the background, consumers and businesses are finally feeling more confident about the US economy and their futures. Yet we are a long way from exuberance or even "typical" economic expansion. US stocks are one of the leaders in world markets this year and inflation remains low for now. Enjoy the moment, as it has been a tough recovery from depths of the Great Recession.

Optivest News

Optivest Properties has joined forces with three other medium-size regional self-storage operators around the country and formed National Storage Alliance (NSA) to create a $1-$2 billion REIT to go public in 2015. Our current properties will be converted to the NSA REIT over the next years and should result in a significant IRR premium when public.

In January 2013, industry veteran, Paul Donnelly, launched **Optivest Investment Banking** as Senior Managing Director. Paul brings 17 years of experience and over $3 billion in transactions to help local middle-market business owners gain liquidity. Paul and Mark are also founding members of the Orange County Exit Planning Roundtable (OCX) team. To meet with Paul and his investment banking team, call our offices or email Paul at pdonnelly@optivestib.com .

Thanks to you, the **Optivest Foundation** had a record year in 2012, distributing over $313,000 to 48 deserving charities and individuals. Please visit www.optivestfoundation.org for full details about our current projects and trips. If one of these charities piques your interest, kindly reach out to our Director, Trish Van Mourick, at trish@optivestfoundation.org for more information and how to get involved.

Mark Van Mourick
CEO
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[1]Chartered Financial Analyst (CFA), Certified Public Accountant (CPA), Certified Investment Management Analyst (CIMA), Accredited Investment Fiduciary (AIF).