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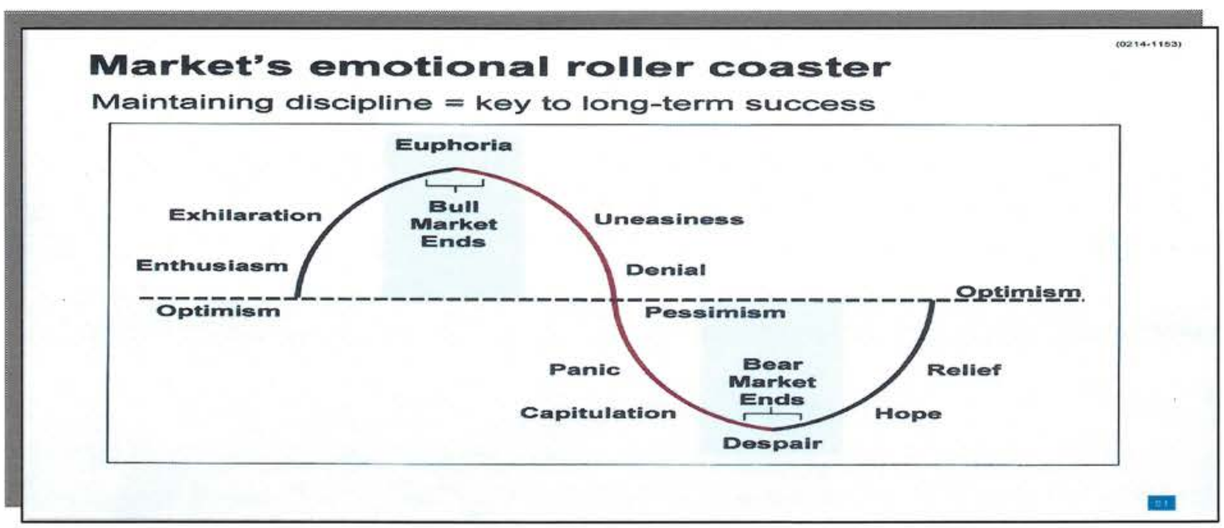
Recently I was in mid-town Manhattan for the annual Investment Management Consultants Association conference (IMCA) – thankfully it ended a full 24-hours before our latest winter storm. Liz Ann Sonders, Schwab's Chief Investment Strategist was running thru a series of PowerPoint slides. Her presentation was about the stock market, in particular the metrics she looks at regarding valuation and where we may be within the classic "investment cycle." And just like that… BAM! I got the opening of another Bodnar Financial White Paper.

Unlike Liz Ann's technical indicators, for me there are no better stock market indicators than the landline phone located at 248 Columbia Turnpike, Florham Park NJ, and my email IN-BOX.



Looking at Ms. Sonders' chart above, I posit that we are currently somewhere between *Enthusiasm* and *Exhilaration*. Recent internet chatter would have you believe that we are in the *Euphoria* phase of the Bull Market, ready to dive back down into the depths of despair. I doubt it. We are just at the beginning of another long cycle.

With the passing of December 31,2013 the financial crisis no longer exists on the 5-year performance chart of most funds (That roar you hear is every portfolio manager in the world shouting "AMEN BROTHER!"), yet the damage done to investor psyche is still not healed. As noted in these pages before, FEAR is a much stronger human motivator than GREED. It would take very little bad news to push the market psychology right back to PANIC and DISPAIR. The hangover is still too intense for many investors.

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Why do I believe we are between enthusiasm and exhilaration? Because my phone is ringing and my inbox is making that funny Bing-sound. The stock market has gone from 16,000 on the Dow, down to a low of 6,500 and as I type it closed at 16,133 yesterday. Yet, I have received more communication regarding individual stock purchases in the past 4-weeks than I have in the prior 4-years. Why is it that my phone was quiet at Dow 8,000 even Dow 10,000? Strange to some, but perfectly logical to one that has witnessed this cycle phenomena consistently play itself out since 1981.

Understand that I am not buried under an avalanche of calls – and please, don't feel guilty if it sounds like I'm describing you – we need the outliers. Those faint blips on the radar screen announcing, "Something's happening." Truth be told, most of the messages are from newer clients—defined as new to Bodnar Financial since the Financial Crisis in 2008. The requests take the form of one or the other generic question; both performance driven, but requiring different answers:

1. Do you think I should buy ________? (Fill in the blank with a company name).

Or,

2. One of my accounts was only up 5% last year; shouldn't we close it and put it into the other account that was up 20%? *(You may substitute "funds inside my 401k" for the word "accounts").*

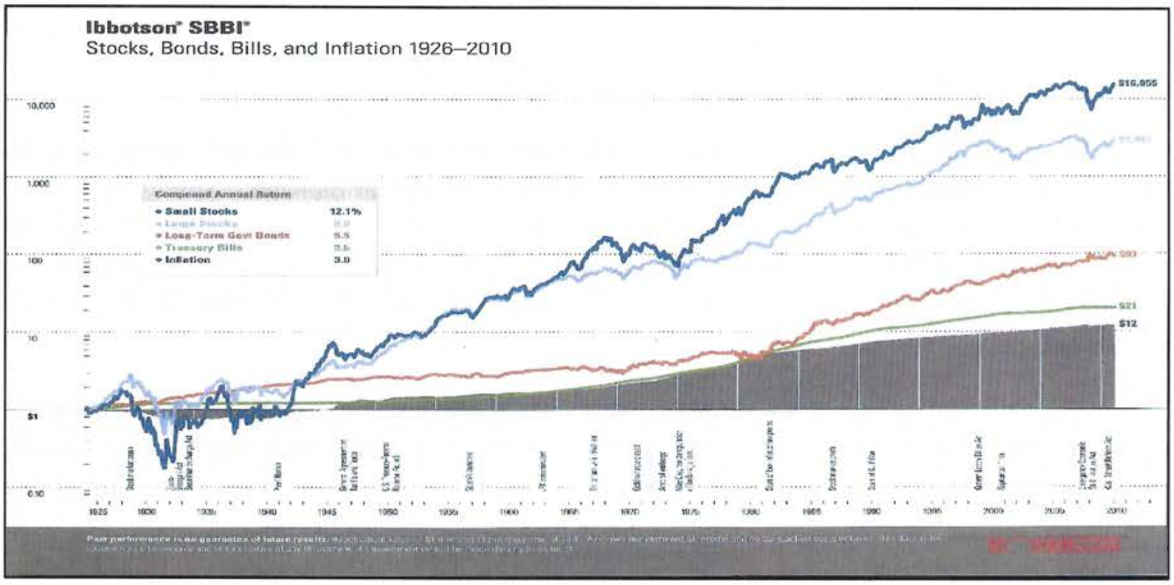
The volume of #1-type questions almost always increases as we leave the bear market phase of the cycle and the greed gland comes back to life. Long-time Bodnar clients will recall that during market sell-offs, greed secretions are mitigated by PCD*Syndrome. It is only with the metabolic rise in Hope & Relief that Optimism is rekindled.

Clients beginning to experiment again with individual equities are a bullish signal. Not necessarily for those clients doing it, but definitely for the rest of us. Few investors have the capacity to pick individual equities correctly on a consistent basis. Successful investing is counter-intuitive for humans. Biologically we are simply not wired for the investing game. Additionally, when a scheme, system, or technique begins to work on Wall Street, and it becomes common knowledge—it almost immediately stops working. Too much money chasing too little inventory always ends up badly in the capital markets.

But back to Question #1: ***"Do you think I should buy Consolidated Fuzz?"*** The answer you usually get from me regarding individual stock picks is something that sounds like: ***"I'm not sure. Tell me again why YOU like it?"*** And should you inquire regarding a company outside the S&P 500, I have even less of an opinion. Picking individual winners and losers inside the Wall Street casino, as noted above, is very difficult. Clients often retort: but you always seem so confident regarding the stock market. True, but that confidence comes from my reading of history and society, not Barrons or the Wall Street Journal.

**PCD-Panic, Capitulation, Despair*

History is my marker that the arc of humanity is forever upward. There are setbacks and lapses in that upward arc, but like the little engine that could, the small blue line on the Ibbotson chart chugs forward. And why is that? Because the S&P500 never dies – individual companies within that index die all the time – in fact, many economists surmise that creative destruction not only exists as a positive force for the marketplace, but also is absolutely necessary for the capital markets to maintain the risk premium investors expect. That periwinkle line is the home to the 500 largest companies within the most powerful nation on Earth; and the list is re-configured and re-balanced on a semi-annual schedule.



Companies within the S&P500 get no points for past performance. The S&P500 is a world of "what have you done for me lately?" Past stars of the index, now extinct include: Western Union, Penn Central, Bethlehem Steel, TWA, MCI, Woolworths, Pan Am, Pullman – I'm sure each of you could add a few more. Individual stocks may die, but the index lives on, and in fact grows in value.

So, using history as a guide – and it's the only guide based on reality that I'm aware of—each day I enter my office and I pledge allegiance to the Ibbotson chart.

Now this is where questions #1 and #2 overlap. Oftentimes my first move is to see if the stock in question fills a missing need in your overall asset allocation and is it something that your children and grandchildren should own. I am confident that multiple generations of your family will want to be invested in the S&P500; there are few stocks or industries that instill the same level of confidence. I can hear the murmur from the back of the room – what about Exxon?

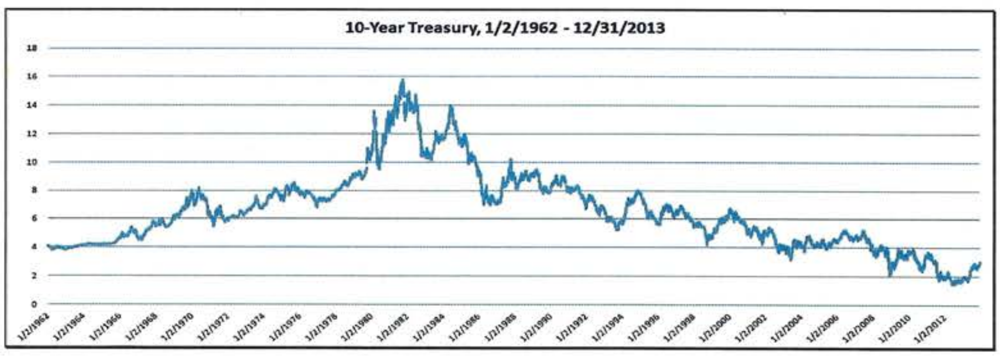
True. I do have a somewhat soft spot for Standard Oil of New Jersey, but I don't recommend Exxon because it's a bargain. I recommend it because most portfolios are terribly energy deficient AND because oftentimes energy is counter-cyclical to the normal S&P500 or Dow cycle.

The Investor's Lament: *"Why do I own this? Market is going up and this dog is going down! Let's sell it and buy one that's going up."* I'm flattered that many of you think that I know which ones are going to go up, but seasoned clients know that I'm just as capable of choosing a lemon as any of you. When forced to pick individual stocks, my goal is simply to fill industry voids in your portfolio; not necessarily stocks that I think are poised to rise during the next few weeks or months.

Now for question #2 -- Performance in 2013 can be summarized thusly: Did you own stocks? How much? The more you owned in U.S. stocks, the better your performance. If you owned no stocks at all and were entirely in bonds, it is possible that your total return in 2013 on your portfolio was a negative; and if your entire portfolio was invested in equities, your return should have been between 20%-30% or possibly even higher. Some small cap funds experienced returns over 40%!

Why such an extreme performance variance from one account to another? As we look back on 2013 it is quite possible that investors experienced a true existential moment. Spring 2013 may mark THE APEX of the greatest bond bull market in history. A rally that began in August 1981 with the dynamic duo of Paul Volker and Ronald Reagan attacking the scourge of inflation and culminating with Helicopter-Ben Bernanke ushering into the investor lexicon the word "taper." And bond investors went on a "taper-tantrum" this past summer.

The chart below says it all – interest rates were at all-time highs in 1980. And for the next 33-years bond investors enjoyed the ride from peak to valley. It is likely that over the next several years interest rates will trend upward as the global economy continues to improve, driving bond prices down.



It was a hell-of-a-ride for 33-years, and bond investors reaped the benefits. The party is probably over.

Ergo...sell all our bonds and dive headfirst into stocks?

Not so fast. January was a wake-up call for stock investors—the sell-off reminds us that stocks are still a volatile asset class. And during that sell-off U.S. bond funds posted a positive month –there's that negative correlation again.

Asset allocation is not about how many assets you own, but about how the assets you own correlate to each other. Investor-A with only two mutual funds may be more diversified than Investor-B who holds ten 5-Star funds, but all ten funds invest in U.S. large cap stocks.

Owning a lot of stuff doesn't make your portfolio diversified. Owning assets that ZIG when others ZAG provides true diversification. Unfortunately, that means that something in your portfolio is probably losing money while others are booking profits. A very tough concept to get your head wrapped around. Think of it this way – if everything you own is going up at the same time that means that eventually everything you own will go down at the same time too. OUCH !

This year, how about a little spring cleaning? With the melting snow, it is the perfect time for a visit or teleconference with your financial planner to: 1) update your balance sheet, 2) review your asset allocation, and 3) re-balance to a portfolio that makes sense for your age and risk tolerance.

Give the office a call and schedule your financial planning spring cleaning.

John Bodnar, CFP®, CIMA®

Florham Park, NJ
February 21, 2014

For clients that wish to experiment with individual stocks, I strongly suggest that you open an on-line brokerage account at E-trade or TD-Ameritrade. You will get quicker access to quotes and information, better on-line reporting, and most importantly it will cost you less than the rates I am required to charge you for individual trades.

One other note – if you must make trades through your account at Pershing – regulators insist that I cannot accept any trade requests via email or voicemail. You MUST speak with either Jeanne or me to confirm your trade. You must tell us the symbol and number of shares you wish to purchase or sell. No exceptions to this rule.