Oxford Chase Advisors
2Q 2016

Economy & Market Valuation

2Q'2016 was a very interesting quarter for the US Stock market. The global economy faced turbulent events like Brexit and yet the market went up in 2Q'2016, albeit by only 2%. A likely reason for this rise is that, in the opinion of the market participants, Brexit and other macroeconomic events such as a slowdown in China and troubles in Europe and Japan will delay and/or slow interest rate hikes by the Federal Reserve. The US economy is in a sweet spot of good economic activity combined with low inflation. Low inflation gives comfort to the Fed that they can keep interest rates low to continue to stimulate the economy. In addition, zero and negative interest rates in Europe and Japan will keep interest rates low in the US for a longer time. The stock market always likes low interest rates. It makes borrowing cheap for the companies who are in a position to borrow and many of these companies are using cheap funding to buy back their own shares resulting in an increase in their share price. Low interest rates are also boosting home prices and new home construction. We think that there is shortage of new homes and the number of new homes will keep on increasing, aided by low rates. US GDP grew at anemic rate of 1.2% in 2Q'16. Even very low growth rate coupled with low interest rates could keep the US stock market rising for some time. There are certainly risks which could tip US market into recession such as global economic shocks and uncertainty created by US elections. We keep an eye on these events and other economic indicators as has been explained in earlier letters.

Investment Philosophy & Examples

As you might have noticed, there is a theme behind many of our stock picks like Moody's, Visa, MasterCard, S&P Global Inc, O'Reilly and AutoZone. These companies have pricing power, show consistent revenue growth and buy back shares every year. These companies are able to increase their earnings every year at a much higher rate because of the combination of operating leverage and share buybacks. We have picked O'Reilly (Ticker: ORLY) as an example to illustrate this point. In 2Q'16, revenue for ORLY increased by 7% Year Over Year (YOY), operating income increased by 10% thus showing operating leverage. Earnings per share (EPS) for ORLY increased by 16% YOY, thus showing the combined effect of operating leverage and share buybacks.