Comprehensive
Financial Planning Inc

900 Main Ave • Suite 200
Durango CO 81301
970.385.5227
Stan@CompFinancial.com
www.CompFinancial.com



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Here is our newsletter for the 2nd Quarter of 2015.

**The Markets and Our Portfolios**
In late January we added two funds to our portfolios. The Powershares Commodity Tracking EFT is an index fund which tracks the index of about 20 commodities. The Fidelity Select Natural Resources Fund invests in the equity of energy and other commodity companies. The commodity index lost over 28% last year and the Natural Resource stocks trailed the S&P 500 by about 25% last year. We sold expensive assets (U.S. stocks) to buy these cheaper assets.

Our portfolios are positioned to emphasize minimizing the potential for large losses as opposed to seeking high returns. The next two sections of this letter explains some of the reasons why. I understand it has taken a high level of patience for my clients and I appreciate all the confidence you place in me.

**Irrational Exuberance-Third Addition**
I just read the 3rd Edition of Robert Shiller's book "Irrational Exuberance". Robert won the 2013 Nobel Prize in economics for his work on identifying and understanding how investment manias or bubbles form. The Economist magazine wrote "Irrational Exuberance should be compulsory reading for anybody interested in Wall Street or financially exposed to it; at the moment that would be roughly everybody".

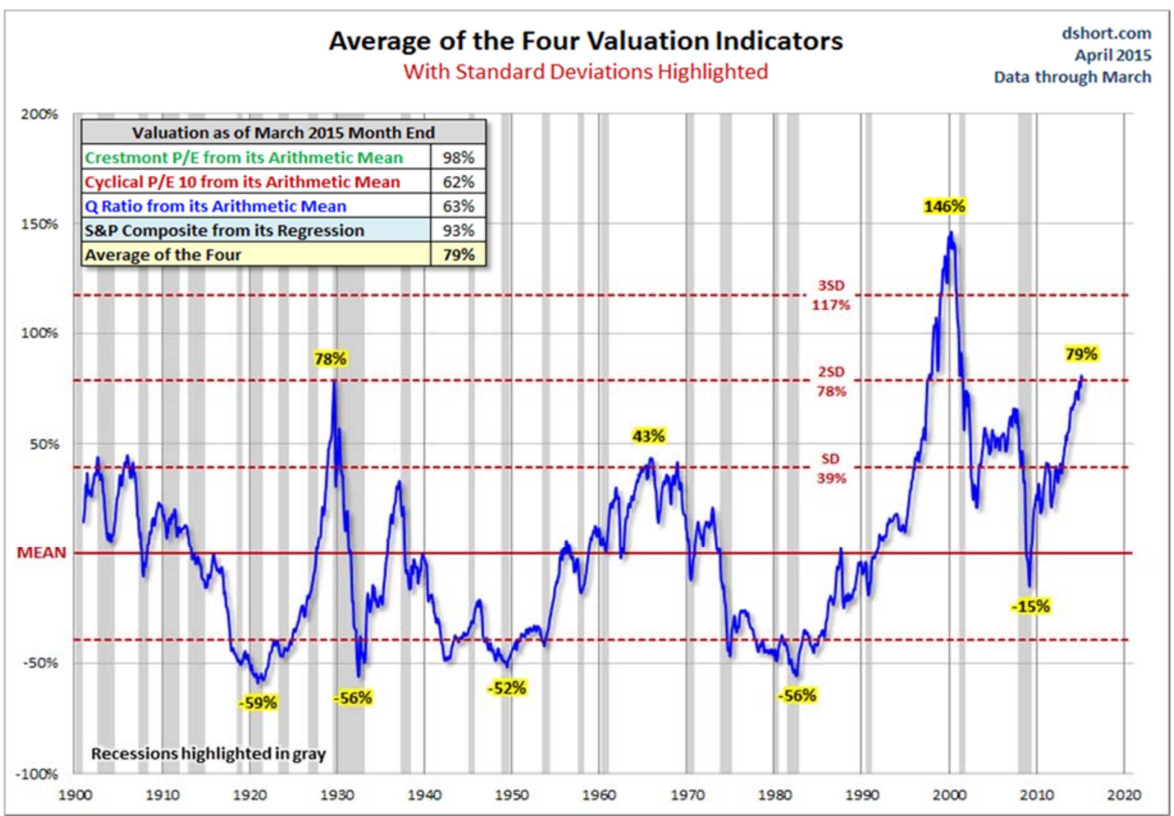
The term "irrational exuberance" was coined by Alan Greenspan in a speech in late 1996 where he voiced concerns about the behavior of the stock market. The 1st Edition of Shiller's book, which came out in early 2000 accurately identified the stock market bubble where prices were much higher than any measure of real value. The 2nd Edition of his book in 2006 described the same thing happening in the real estate market, particularly home prices. Eight years later home prices are still 16% below the peak in 2006, based on Robert's own Case-Shiller 20-city home price index.

In the new edition of his book he emphasizes that the stock market, especially here in the U.S., has again reached bubble territory. Robert devotes much of his book attempting to explain why markets keep doing the same thing again and again. His explanations are complicated and numerous, but I would boil it down to one most important factor: group think. Here are two quotes from the book.

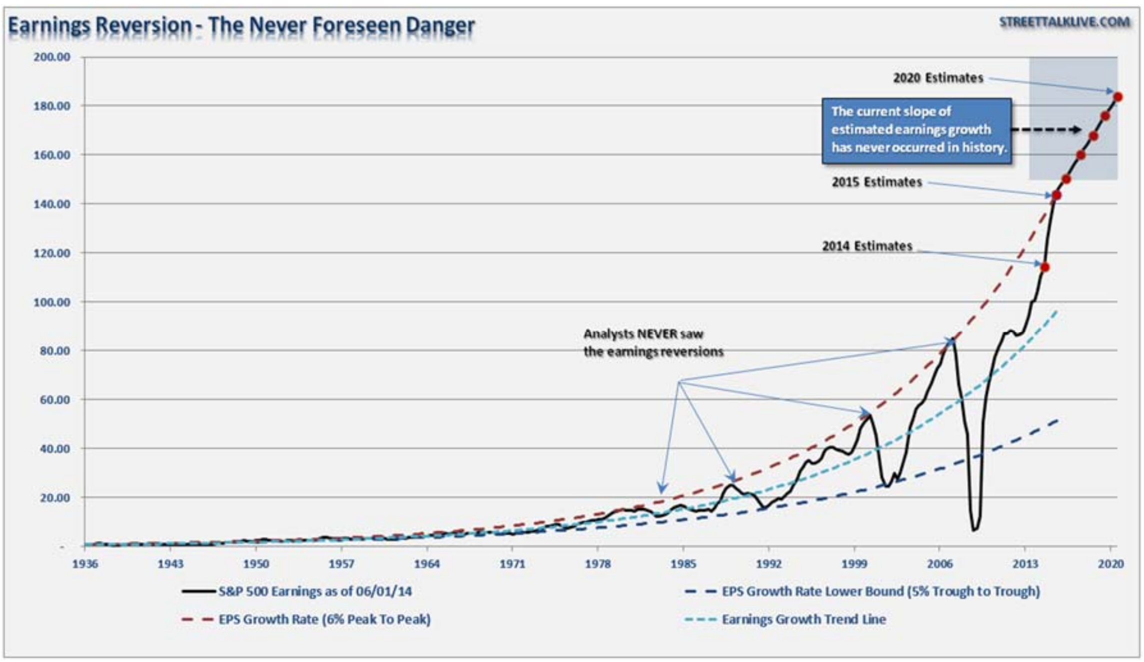
"The present stock market displays the classic features of a speculative bubble: a situation in which temporarily high prices are sustained largely by investors' enthusiasm rather than by consistent estimation of real value. Under these conditions, even though the market could possibly maintain or even substantially increase its price level, the outlook for the stock market into the next ten or twenty years is likely to be rather poor-and perhaps even dangerous.

Robert goes on the write “I cannot accurately predict the ups and downs of the markets. But I do know that, despite a significant slip in confidence since 2000, people still place too much confidence in the markets and have too strong a belief that paying attention to the gyrations in their investment will someday make them rich, and so they do not make conservative preparations for possible bad outcomes.”

How do we know that stocks are expensive, especially in the U.S.? Shiller is the developer of the Shiller P/E ratio. If you don’t believe Robert the chart below shows an average of four valuation methods. One is the CAPE ratio developed by Robert Shiller. The second is the Q ratio developed by another Nobel Prize winning economist James Tobin and two other methods. The average of the four methods shows a current valuation of the S&P 500 of 79% over the long-term mean. Another valuation method, Price/Sales is currently at an all-time high and more than twice its historical average. Again as I have mentioned before, these methods are not good for determining what will happen over the short term but very good at evaluating returns over 5 years and longer.



**Earnings Reversion**
In our January 2008 newsletter we pointed out how the S&P 500 Reported Earnings had risen well above the long-term trend, pointing out that earnings always eventually revert back to the long-term average trend. http://compfinancial.com/newsletters/2007q4-newsletter.pdf
We have included an update of this chart with data thru late last year which shows the hard earnings slump in 2008 and 2009 which took earnings well below trend line. Today earnings have again returned to well above trend line, and most importantly estimates of future earnings growth have never been higher. Earnings estimates of Wall Street analysts as of late last year are shown in the chart below by the red dots. Earnings estimates have started to come down and will eventually return to more realistic values, bringing equity prices with them.




**New Risk Questionnaire**
When designing portfolios for our clients there are three aspects of risk that we explore. First, risk tolerance is the level of volatility a client can withstand before wanting to go to cash. Second, risk capacity is how much risk clients can afford to take. Third, risk needed is how much risk clients need to take to achieve their financial goals. The last two aspects can only be addressed by developing a comprehensive financial plan that evaluates all your resources, liabilities, needs and wants.

The first aspect we address by using a risk questionnaire. Our firm has recently evaluated several and are now using an online system from Riskalyze. It is very simple yet very powerful tool to understand your risk tolerance and to monitor the risk in your current portfolio.

We will invite all our current clients to use the new Riskalyze system to ensure their portfolio fits well with their risk tolerance, capacity and needs. I also invite anyone else interested in finding their risk score and determining the risk in their current portfolio by following the link on our website.

**Tax Time**

It's not too late to make contributions to your retirement plans and IRAs for 2014. Contribution limits go up every year and, as mentioned in my last newsletter, there are great opportunities in 2015 to do a back-door Roth IRA. For 2014 contributions you have until April 15th or, if you file for an extension, you can contribute to some plans up to the filing extension date. Give me a call to discuss your own situation.

Sincerely,

Stan Johnson, CFP(R)
Comprehensive Financial Planning, Inc.
Registered Investment Advisor
970-385-5227
www.CompFinancial.com