VWS Financial Resources Group, Inc.

Fiscal Fitness

Vorpahl Wing Securities
421 W. Riverside Ave., Ste 1020
Spokane, WA 99201
509-747-1749

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Special Edition

The Top 10 Economic & Investment Predictions for 2015

The Investment Policy Committee

The Investment Policy Committee (IPC)—a group comprised of the top financial consultants at VWS Financial Resources Group that meets once a month—compiled the top 10 investment themes for 2015. This group was formed for the discussion of sound investment advice and appropriate investment vehicles for our VWS client base. We discuss such topics as macroeconomic thoughts, theories, and trends and how these trends relate to the markets on a short-, medium-, and long-term basis. We also discuss current geopolitical events and how we think such events will affect the markets.

The 2014 Scorecard

We did very well with our predictions in 2014. Here is the scorecard. Data as of December 5, 2014.

The Good

- We saw a trend starting to develop in 2013. Companies were moving back to the U.S. or moving to different parts of the country, if it made sense from a cost perspective. We believed those companies would do better overall than all the companies in the S&P 500. We were right. Companies in the S&P 500 that made at least 50% of their sales within the U.S. had higher earnings than all companies in the S&P 500 overall.
- With the amount of cash companies were holding, we believed merger and acquisition (M&A) activity would continue into the new year. For 12 months ending October 31st, M&A in 2014 totaled $1.509 billion versus $1.013 billion in 2013.
- With the housing market growing at a gangbuster rate in the beginning of 2013, we forecast this sector would grow but at a slower rate in 2014.
- Our predictions for where the DOW would close ranged between 17,400 and 18,000. The DOW currently stands at 17,958.
- The dollar will remain strong—it is still the safe haven and currency of choice.
- Large-cap and mid-cap stocks did have a good year with both posting returns of over 12%.
- For the fixed-income aspect of portfolios, municipal bonds were one of the best performing assets.
- European stocks continue to slump, so investors must be very selective in choosing companies in this area.
- Natural gas will continue to make headway, especially with new drilling techniques.
- Emerging market stocks, as predicted, have been flat for the year.

The Not-So-Good

- Small-cap stocks are not having a banner year.
- We thought the easing of QE would drive the 10-year Treasury to 3.5%. It is now hovering around 2.3%.

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Executive Summary

We are surprised as anyone how fast oil prices have fallen. (We are also surprised that OPEC did not cut production to stabilize prices.) But whatever the reason for these lower prices, there is by no means a shortage of economic forecasting for the global economy. Some economists warn that the recent 40% drop in oil prices is a result of a slowdown in Europe, which is staggering towards a recession, as well as a slowdown in China. Japan has also been thrown in the mix, but Japan has been struggling for years. For the major oil exporting countries such as Iraq, Algeria, and Nigeria, falling oil prices are taking a toll on their economies. Venezuela is also hurting. In order to balance their 2015 budget, they calculated oil at $117 per barrel. Ouch!

On the positive side, countries that are mostly oil importers could see a boom, possibly adding a full percentage point to their GDP. These lower oil prices could also be a shot in the arm for the consumer, redirecting the dollars from their gas tanks to the malls. Since 70% of the U.S. GDP is made up of consumer spending, this could boost the GDP at home. But who knows what the consumer will do with this windfall? Time will tell.

Interest Rates and the Strength (Weakness?) of the Greenback

We expect volatility in the short-term interest rates market. We also expect the feds to raise interest rates sometime in the third or fourth quarter, with small incremental increases of about 1/4 point per shot. Our forecast: the 10-year Treasury at 3% by year end. But inflation will remain in check, keeping long term interest rates low. This will result in a flat yield curve.

We continue to believe the dollar will remain strong relative to other currencies. Despite the $17.9 trillion of debt in America, the U.S. dollar is still the currency of choice. Economic trouble in any overseas country normally causes a flights to safety, which is still found in the U.S. dollar.

The Top Asset Classes

Large-Cap dividend paying companies did very well in 2014, gaining over 13%, based on the Russell 1000. We believe these companies will continue to do well in 2015. Our favorite sectors are healthcare, technology, and energy.

Small—cap companies did not have a stellar performance in 2014, rising only 2.87%. We believe this asset class is well positioned to recover, and we expect a decent return in the coming year.

Mid—cap stocks did much better in 2014 than small-cap stocks, gaining over 12%. We expect mid-caps to continue to give investors decent returns in 2015.

Europe is having a lousy year. Even large-cap, developed companies have not faired well so far. We believe Europe will continue to struggle, but there could be positive implications for investors who are very selective.

We believe fixed income should be part of most portfolios. Having said that, we are committed to managing risk for our clients and the fixed income market could be one of the riskiest asset classes in 2015. Although there are no guarantees, the Feds have almost talked themselves into raising rates next year. As interest rates rise, bond prices fall. Investing in a fixed-income product that pays 4%, high yield, for instance, doesn't make much sense if the value falls 5%. The coming year could offer some interesting reallocation opportunities.

Energy

It has been an interesting month in the energy sector. The cost for a barrel of oil has dropped around 40% since mid June. We could see a further drop, but this drop, we believe, will be short lived. We think oil prices will stabilize and begin to climb back closer to $80 per barrel. Smaller oil companies could get pinched and some acquisition activity might take place. Natural gas fired generators will continue to replace coal fired generators.

Commodities

Commodities are bulk goods and raw materials such as grains, metals, livestock, oil, cotton, coffee, sugar, and cocoa that are used to produce consumer products. This sector is normally very volatile year after year; one year it could be the top performer and the next the worst. It did not fair well in 2014, and we see commodities still struggling in 2015.

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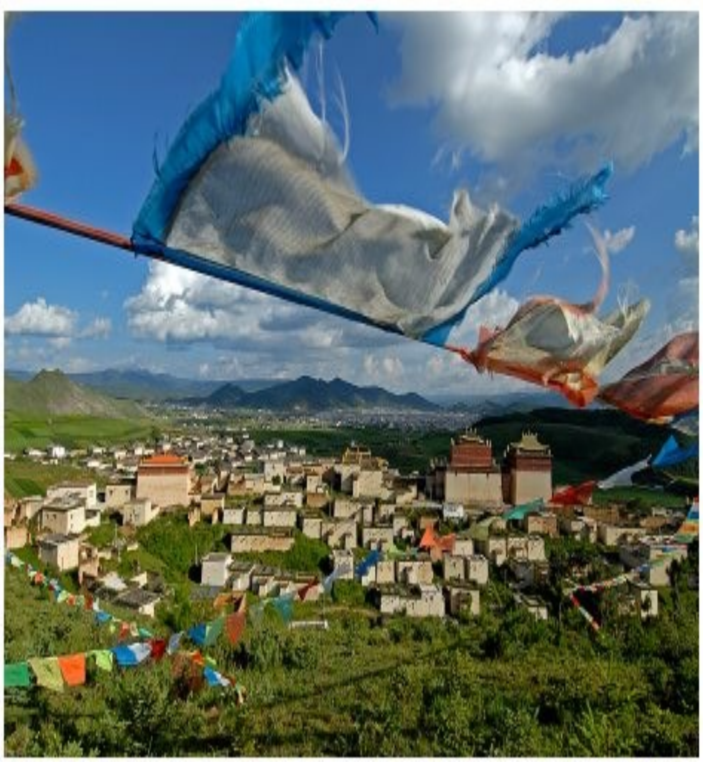
Market Predictions

After a stellar year for the DOW in 2013 (with returns of over 26%), the DOW cooled to a return of around 8% in 2014. We think the DOW will perform about the same in 2015 as it did in 2014. Our range predictions for the DOW are between 19,200 and 19,600 for the new year.



Emerging Markets

A strong dollar and low oil prices do not bode well for emerging markets. Citizens of these countries want to move from their farms to the middle class, but this is a slow process. Emerging markets were basically flat in 2014 and we expect the same for 2015.

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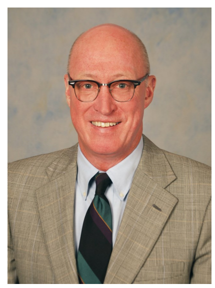
Tim Vorpahl

Jon Strine



Lee Nordstrom

Dennis Roginski

Chris Lefkowski

Samantha Hokenson

Eli Petropoulos

Craig Landron
Affiliated with
Allegro Wealth Mgmt

Mike Hines
Affiliated with
Movement Mortgage
LLC NMLS #7704

Vorpahl Wing Securities 421 W. Riverside, Ste 1020 Spokane, WA 99201

Cell: (509) 590-7156 (509) 747-1749

Visit our website at www.vorpahlwing.com