STEWARDSHIP PARTNERS

# MARKET COMMENTARY

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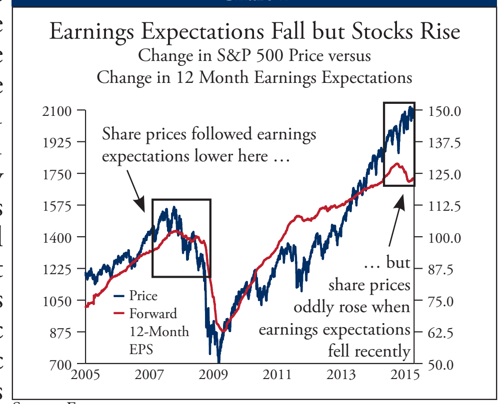
## Financial Markets Once Again Distorted by Government Interventions

***"Hear this, … you rulers of Israel, who despise justice and distort all that is right" Micah 3:9***

The strange feeling that the world's financial markets are no longer fully reflecting reality has reemerged. With the onset of the European Central Bank's QE program early this year, the value of the Euro has tumbled while trillions of dollars of European government bonds now trade at negative interest rates, which means the borrower is paying for the privelege of loaning these governments money rather than the other way around. Switzerland recently sold a new 10 year bond at negative interest rates! Mexico was recently able to find buyers for a 100 year bond denominated in Euros, a currency many doubt will exist in 10 years, let alone 100. Meanwhile, as China's economy continues to deteriorate, even when measured by official figures many believe are overstated, its stock market has moved straight up since late last year as government support for the financial system has encouraged wild speculation by uneducated retail investors who have sent margin debt to record highs. In Japan, the government's hyper-aggressive QE program includes buying equities as well as stocks, thereby directly boosting share prices in Japan even while the country's economic performance remains largely unresponsive to the government's stimulus efforts. Japan's economic minister actually said this: "A small bubble is something that can be contained. If recent stock gains are signs of a mini-bubble, this is something I would welcome." Bizarre pricing can also be found in the oil market where inventories are already sky-high and are still climbing forcefully, yet oil prices have nevertheless rebounded off the lows reached earlier. Other commodity prices have been crushed, however, as economic growth has slowed and no government effort has yet been made to support industrial commodities. The strong US dollar and a seemingly unending stream of disappointing US economic reports also dented first quarter earnings expectations for the S&P 500 (Chart 1). Even as expected first quarter S&P profits fell from +8% to -4-5% during the course of the quarter, equity prices still advanced slightly. Needless to say, with so many markets behaving so unusually, it leaves keen market observers worried about what might happen as all these distortions get sorted out.

**Chart 1**




Source: Factset

**Table 1**

**1Q15 Total Returns**

| US Indices | 1Q15 | 5y ann |
|---|---|---|
| S&P 500 | 1.0% | 14.5% |
| S&P 500 Value | -0.7% | 13.1% |
| S&P 500 Growth | 2.5% | 15.8% |
| NASDAQ | 3.8% | 16.7% |
| S&P 400 (Mid Cap) | 5.3% | 15.7% |
| S&P 600 (Small Cap) | 4.0% | 16.3% |
| Treasury Bonds | 1.8% | 4.1% |
| High Grade Corp. Bonds | 2.3% | 6.5% |
| Gold | -0.1% | 1.2% |
| **Global & International Indices** | | |
| MSCI World | 2.3% | 10.0% |
| MSCI EAFE | 4.9% | 6.2% |
| MSCI Euro | 5.2% | 4.7% |
| MSCI Far East | 9.0% | 6.3% |
| MSCI Japan | 10.2% | 5.9% |
| MSCI Emerging Markets | 2.2% | 1.7% |
| **US Economic Sectors** | | |
| Energy | -2.9% | 8.0% |
| Materials | 1.0% | 10.8% |
| Industrials | -0.9% | 14.5% |
| Consumer Discretionary | 4.8% | 20.1% |
| Consumer Staples | 1.0% | 15.0% |
| Health Care | 6.5% | 20.1% |
| Financials | -2.1% | 10.5% |
| Information Technology | 0.6% | 14.6% |
| Telecom | 1.5% | 12.8% |
| Utilities | -5.2% | 13.0% |

Source: Bloomberg

Table 1 highlights the performance of the various markets and US sectors during the first quarter. While the US market managed to eke out a small gain for the quarter, both January and March were negative months. February, however saw stocks rise sharply even as negative earnings revisions accelerated and economic reports chronically disappointed. We are hard pressed to logically explain February's unusual upturn. Some argue large amounts of corprate stock buyback plans positively impacted the markets. Others believe the "Great Rotation" from bonds to stocks played a role as worries about the Fed raising interest rates grew. Some suggest Japanese pension funds buying US stocks was the reason. Whatever the reason, the jump made little sense. At the start of the quarter US economic growth was expected to be in the 3% range but those expectations have now been beaten down to the 1.0-1.5% range by all the weaker than expected economic reports. Global economic growth expectations also fell as China, Brazil and Russia continued to suffer meaningful economic setbacks. Europe was about the only region to show signs of economic progress, although it was minimal. Moreover, Europe continues to have the Greek and Ukrainian situations hanging over its head. While the intensity of these probem areas diminished by quarter's end, we suspect further uncertainty will arise from both locales before too much more time has past.

While significant direct government intervention in the US markets ended last fall when QE was halted, the market's focus on the Fed's timing of its first interest rate hike still meant the government indirectly dominated the markets. Despite the distortions, some Stewardship Partners portfolios turned in index beating returns during the quarter largely due to good stock selection, while the defensive positioning we maintained led others to underperform. With so many markets reflecting a distorted reality, we remain concerned about a possible correction in equities.

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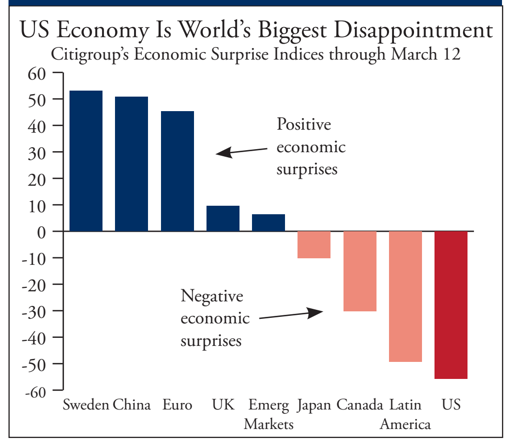
# US Economy Surprisingly Weak, Joining Japan and Emerging Markets

*"You also have become weak, as we are; you have become like us." Isaiah 14:10b*

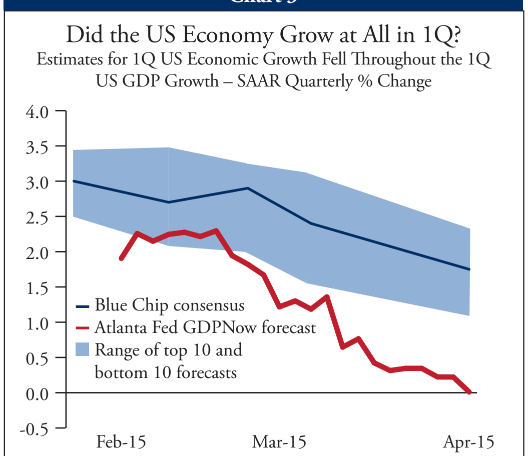
As we entered 2015, we were not overly concerned about US economic growth. It appeared the US economy might well have reached the point where it could finally grow at a moderate rate without the assistance of QE. Indeed, it seemed the US economy, aided by a strong banking system and continued employment growth, was by far the world's strongest economy. The deflationary forces that have been stalking the global economy since the Great Recession, however, seem unwilling to retreat. Expectations for US GDP growth in the range of 3% in the first quarter rapidly melted in the face of an onslaught of disappointing economic data. At times, nearly every new piece of economic data released came up short of expectations. Amazingly, the US economy has experienced the most disappointing data in the world (Chart 2) thus far in 2015! The West Coast port strike, the fracking bust and bad weather certainly played a role in this trend, but the shortcomings are so widespread concern has arisen the US has not yet freed itself from the deflationary grasp of the Great Recession even six years later. Perhaps most surprising is economic growth has waned even as consumers were receiving a huge boost to their disposable income from lower oil prices. Shockingly, it appears consumers have altered their historic behavior, perhaps reflecting a combination of frantic, last-minute retirement savings by baby boomers and student loan repayments by millennials, and did not spend the extra money in their pockets.

**Chart 2**




Source: Citigroup, Bloomberg

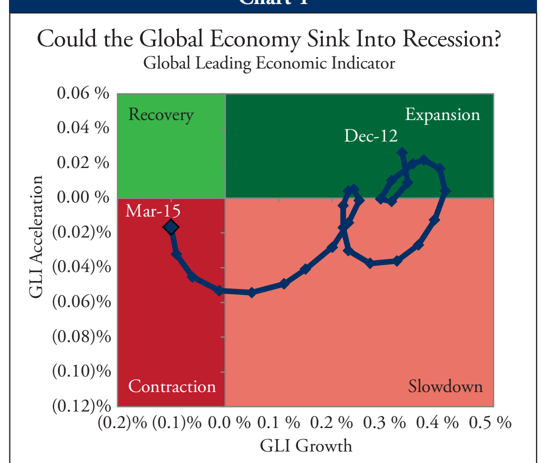
**Chart 3**




Source: Blue Chip Economic Indicators and Blue Chip Financial Forecasts

Whatever the reason, economic growth forecasts slid along with the bad data. Chart 3 highlights the downward trend in consensus forecasts for US economic growth in 2015's first quarter, from 3% to 1.7%. Furthermore, the Atlanta Fed has a model which tracks the economy and it has fallen to the point where it predicts virtually no economic growth in the first quarter. Could this weakness just be a temporary blip in an otherwise improving situation or is it an indicator of more trouble on the horizon? It is too early to tell, but it is certainly something we are keeping a close eye on. So is the Fed. Unless there is a quick reversal, the surprisingly weak trend has almost certainly put off the Fed's first effort to raise interest rates until later this year if not early next year. The trend in economic reports has improved slightly recently but, overall, the path ahead remains very unclear.

**Chart 4**




Source: Goldman Sachs

While Chart 2 indicated better than expected economic reports in Europe and China, a Global Leading Economic Indicator produced by Goldman Sachs (Chart 4) suggests a contraction in economic growth may soon occur. Part of the explanation for these diverting indicators is both Europe and China were able to beat economic expectations simply because the forecasts for their respective economies were already so low. In China's case, the better than expected economic reports may reflect government manipulation of the reported data. Brazil and Russia are also in recession already and Japan's economic growth remains tepid despite massive monetary stimulation which we have highlighted in past Quarterly Commentaries. With China and the US facing stalling growth, there is no engine to propel the world economy at the moment. The area showing the most resilience right now is Europe as it is benefitting from the much lower value of the Euro and reduced oil prices. Unfortunately, the still unresolved Greek and Ukraine problems cast a significant cloud over the improving economic trends in Europe.

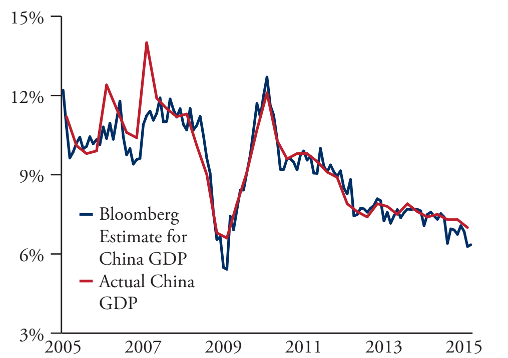
**Chart 5**


Source: Thomson Reuters, AMP Capital

Indicative of the deflationary grasp the Great Recession still seems to hold over the global economy is the very low level of inflation, if not outright deflation, in the world's developed markets. Chart 5 portrays over 40% of the world's countries currently are experiencing outright deflation. This is almost the same percentage as occurred in the aftermath of the Great Recession and certainly does not suggest we are in the midst of an economic boom. Given the backdrop of an absolutely enormous Japanese QE program

**Chart 6**

China's Growth Still Trending Lower
Bloomberg Chinese GDP Tracker vs. Actual Chinese GDP

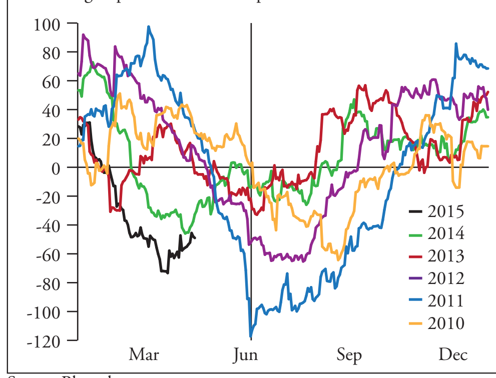



Source: Bloomberg

as well as a very substantial European QE effort, the lack of inflation is telling us the excesses that led to the Great Recession have still not been fully worked through. We believe the root of this problem lies in China where the government responded to the prospect of a depression by massively overbuilding just about everything. Now, the Chinese government is trying to slowly let the air out of this mal-investment monstrosity it created in order to avoid a more calamitous immediate outcome. This process of slowly winding down its bubble has exported deflation to the entire world in a slow drip fashion. It may be many years before Chinese growth can recover and global pricing of industrial commodities, in particular, can return to normal. Chart 6 shows the trend in Chinese economic growth remains decidedly negative as that nation struggles to bring balance to its economy following its gigantic spending spree in past years. Until this process is complete, the whole world may face unrelenting deflationary pressures, which could lead to more QE programs and the risk of creating even more financial market bubbles around the world as the markets are force-fed an ever growing amount of central bank created liquidity. To be sure, this excessive liquidity is largely responsible for the many distortions now present in the world's financial markets, most notably, negative interest rates. Already, an equity bubble has erupted in China and recently overflowed into Hong Kong. Japanese and European share prices are also beginning to act a bit bubbly.

**Chart 7**

Economic Disappointments May Reverse
Citigroup US Economic Surprise Index Historical Trends




Source: Bloomberg

While the economic news in the US has been surprisingly negative so far in 2015, a look at Chart 7 gives a little hope. Ever since the Great Recession, economists have looked for a better start to each year than was ever realized. By the second half of each year, however, economic surprises turned positive. Hopefully, the US will once again find its economic footing in 2015 before too much more time passes. Should the world's largest economy continue to stumble along, it would have negative ramifications for the whole world. What global economic growth needs right now is a resilient, self-sustaining US economic economy that can help pull other nations out of their own economic doldrums. Given the strong US dollar, we believe this will end up being the case, but we are proceeding with caution for now. The severe drought in the Western US is also a threat to second half 2015 economic growth which may hurt the markets.

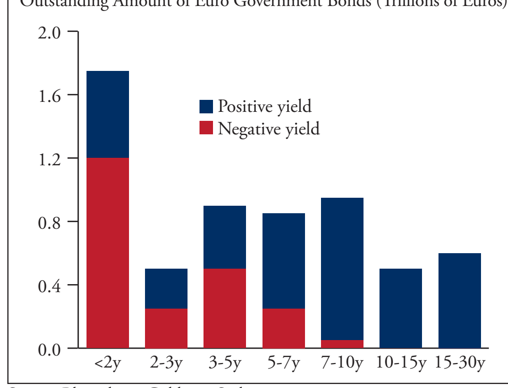
# Government Caused Market Distortions Inevitably Lead to Bubbles

***"They rely on empty arguments, they utter lies; they conceive trouble and give birth to evil." Isaiah 59:4***

Stewardship Partners' current defensive portfolio posture was originally put in place because valuations were at above average levels and potential movements in oil prices, and or disruptive geopolitical actions related to the low level of oil prices, could lead to a normal market correction. At the same time, however, we are also concerned about the possibility of the financial markets moving into bubble territory as the gargantuan amount of liquidity being pumped into the global markets by central bankers looks for a home. Clearly, the negative interest rates seen mostly in Europe are indicative of the biggest bubble on the planet at this time. Trillions of dollars' worth of European government bonds now sell at negative interest rates, some even with a 10 year maturity (Chart 8). Even outside of Europe, interest rates are at historically low levels as the bubble in bonds is not contained in Europe. As rates increase, money will fly out of bonds in order to avoid losses and new bubbles may be created wherever that money goes. We believe a "Great Rotation" from bonds to equities is likely at some point and this could push share prices into a bubble of their own. So far in 2015, however, new money continues to flow into US bond mutual funds and out of US equity funds as expectations for the beginning of a rate hiking cycle by the Fed continue to get pushed back. Even so, this is a key bubble we are watching as it could lead to unusually strong share prices.

**Chart 8**

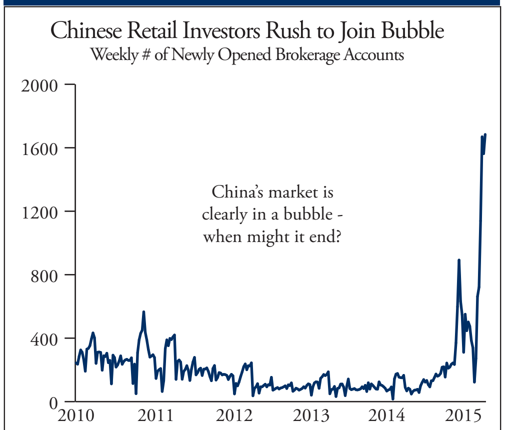
Paying the Government to Borrow Your Money!
Negative Yields Dominate Europe Bonds Under 5 Years
Outstanding Amount of Euro Government Bonds (Trillions of Euros)




Source: Bloomberg, Goldman Sachs

One area where an equity bubble is already in full swing is in China. Despite deteriorating trends in the Chinese economy, a monetary stimulus program begun by the Chinese last fall immediately kicked off a sharp increase in share prices which quickly got out of hand. All the elements of a bubble top already seem to be in place in China. Retail investors are rushing to open brokerage accounts (Chart 9) and valuations on many shares are nothing short of astronomic, even when measured against the standard of the US Tech Bubble valuations. While the overall P/E ratio of the Chinese stock markets is held down by low valuations given to banks (justifiably so given how many of their loans are probably bad), the prices being paid for the remainder of the shares are off the charts. Deutsche Bank notes that a ketchup manufacturer and a school uniform company sell at a P/E of 330x while a company that makes health care products

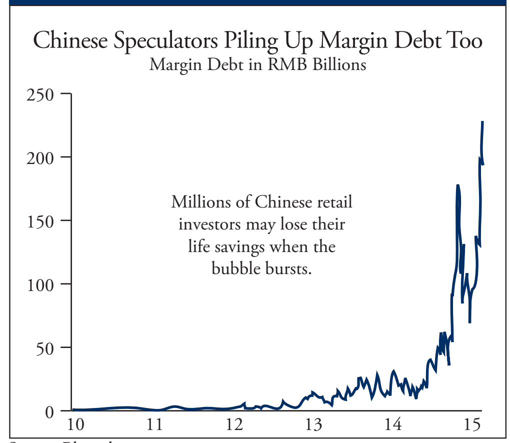
**Chart 9**




Source: Bloomberg

from deer antlers goes for 70 times earnings. The Financial Times reports that the median P/E on the Shenzhen Exchange is 39x and only 4 stocks have fallen in price this year while 244 have doubled in value or more. It will come as no surprise margin debt in China has soared since last fall (Chart 10). Due to very recent regulatory changes that allow Chinese mainlanders to invest more on the Hong Kong Exchange, the Hong Kong market has now begun to jump also as the cash flows in from China. It is never easy to know when such a bubble will end, but in terms of time, this bubble still seems quite young. In terms of investor behavior, however, it already looks closer to the end than the beginning. Sadly, roughly 30% of the new investors have no significant education and 6% or so are said to not even be able to read! Many of these will almost certainly lose their life savings when the collapse inevitably hits.

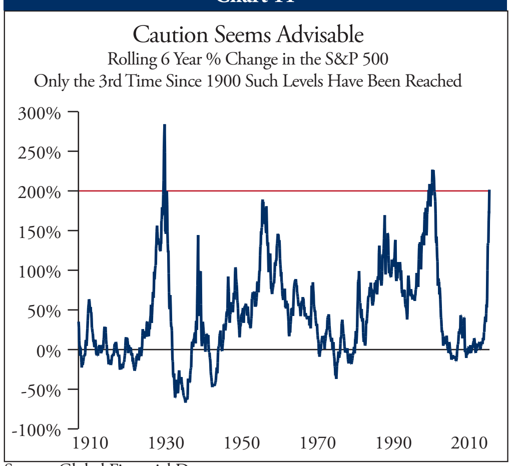
**Chart 10**




Source: Bloomberg

Valuations in the US and elsewhere are above average, but there is little evidence of a bubble. Even so, the strong six year advance in the S&P 500 (Chart 11) is not reassuring. Since 1900, only two periods have generated such a sharp increase in six years – the period before 1929 and the period before the Tech Bubble crash. There is some evidence of bubbly behavior in the US, notably in the venture capital and private equity arena where valuations for many new technology-related start-ups have been quite rich, to say the least. While institutional investors were falling over themselves to gain access to Uber's capital raising that valued the glorified taxi company at greater than $40 billion, the average investor fortunately had no access to this and similarly overpriced deals.

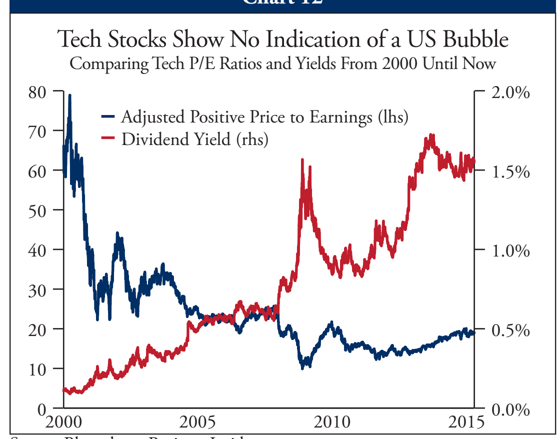
**Chart 11**




Source: Global Financial Data

On the public markets, however, there is scant evidence of such bubbly behavior. Chart 12 highlights just how different valuations are now for the US technology stocks versus those seen during the Tech Bubble that ended in 2000. P/E ratios in the tech sector have fallen from over 70x in 2000 to around 20x today. While that 20x is twice the level seen at the market's bottom in 2009, and is also above average, it falls far short of being described as a bubble. Perhaps the only portion of the US stock market which is acting a bit effervescent is the biotechnology sector which has been on a huge five year advance and is attracting unusual amounts of both money and investors. Even here, however, much of the gains have been supported by very strong earnings growth as biotech companies have been able to bring innovative new therapies to market.

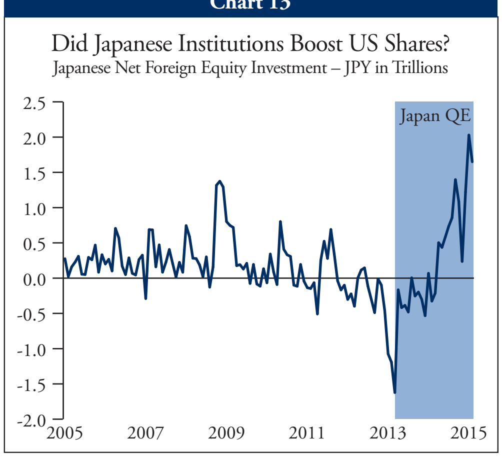
**Chart 12**




Source: Bloomberg, Business Insider

Even so, the US equity markets' strong move higher in February in the face of sharply deteriorating earnings expectations and disappointing economic reports was unusual to say the least. On most days in February, the market would initially open softer following a less than stellar economic report only to turn higher shortly thereafter and climb slowly through the day for no apparent reason. In the end, the S&P 500 jumped an astonishing 6% during the month. While the market turned down again in March, the big February gain was hard to fathom. Since money continued to flow into bond funds and flow out of equity funds, the cause seems unrelated to the Great Rotation. Certainly, share repurchases contributed to the buying as buybacks remain substantial. Still, these would likely be insufficient to power such a strong rally in the face of such nasty data. We believe Japanese institutional investors allocating increasingly large portions of their portfolios to US stocks in the face of a plummeting Yen is the likely culprit for the strange buying activity (Chart 13). It is not clear yet whether this trend ended in February or will continue, but we will be closely watching this situation.

**Chart 13**




Source: JP Morgan, Bloomberg

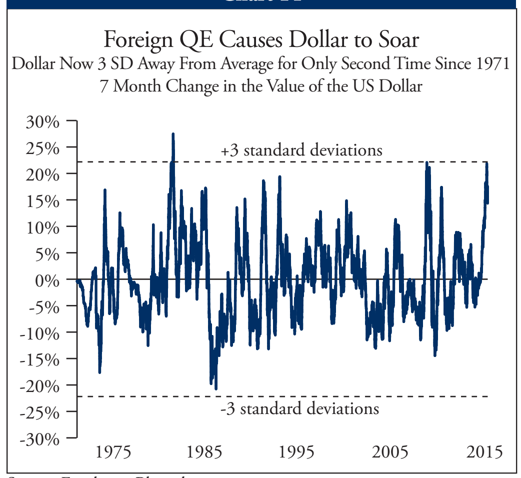
While we remain defensively positioned, we may alter the structure of our defensive holdings or replace them altogether if it appears the many market distortions we have noted will continue for a longer period of time. Europe and Japan already seem to be giving some signs of being in the early stage of an equity bubble.

# Global Equities are Not Cheap, the Strong Dollar Hurts US Earnings

***"People who have wealth but lack understanding are like the beasts that perish." Psalm 49:20***

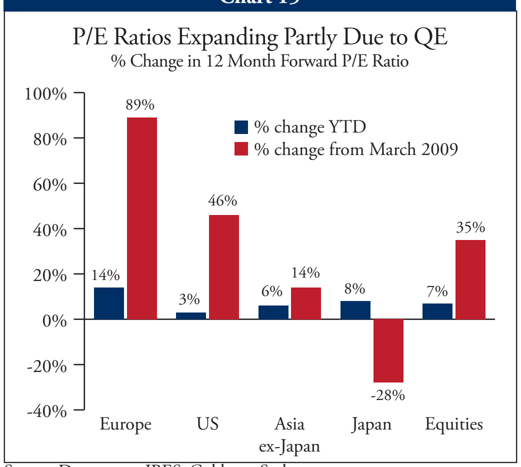
The US Dollar is in the midst of a bubble as well prompted by foreign QE. The US has already exited its own QE program and is now contemplating raising rates. Meanwhile Europe, China and Japan are all pursuing very aggressive monetary stimulus. The result is the value of the US dollar is being forced higher at a rapid rate. Chart 14 shows the seven month rate of change in the value of the dollar has exceeded three standard deviations from the norm, something which has occurred only once before since 1971. Given there is no expectation for Europe or Japan to end their QE programs anytime soon, the dollar may be inflated into an historic bubble. When the Fed signals it plans to raise interest rates, the dollar may move higher even faster than it has already. These government policies are such strong forces even the weakness in the US economy in the first quarter could not undermine the dollar's surge. Moreover, the implications of a bubbly dollar are widespread throughout the global economy. For example, foreign investors (like the Japanese as we have already have seen) are incentivized to sell assets in their own currencies and buy those in the US since the strengthening US dollar itself will provide a positive return to a foreign investor. As a result, a strong US dollar promotes bubbles in US stocks and bonds, especially since foreign QE is specifically designed to weaken local currencies versus the dollar. It is no wonder Japanese institutions are fleeing to the US since the Japanese QE has already lead to a roughly 35% depreciation in the value of the Yen to the dollar and the Euro has tumbled as well.

**Chart 14**




Source: Fundstrat, Bloomberg

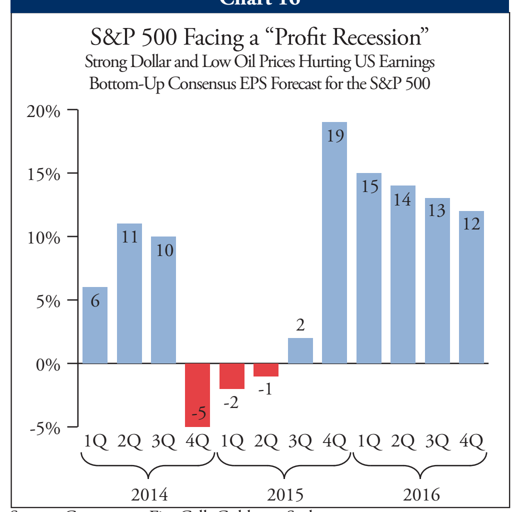
**Chart 15**




Source: Datastream, IBES, Goldman Sachs

The dollar began its rapid ascent almost one year ago and one of the repercussions has been a sizable jump in European equity valuations since then. As the Euro weakened, investors realized export-oriented European companies would see their sales increase and margins expand. Accordingly, P/E ratios expanded as investors sought to buy European shares in anticipation of better earnings (Chart 15). Indeed, valuations have been on the rise almost everywhere in 2015 as the equity markets are absorbing some of the liquidity being force-fed into the world's financial markets. While this caused foreign share prices to move significantly higher in local currency terms, dollar based investors have not enjoyed the same returns as the strong dollar eroded high local currency returns.

**Chart 16**




Source: Compustat, FirstCall, Goldman Sachs

Naturally, if a strong dollar helps foreign company profits, it hurts US profits. The higher dollar is a meaningful headwind for US companies as their exported products are now more expensive to their foreign customers. About 40% of the S&P 500's revenues come from overseas. Sinking oil prices have certainly hurt US energy company profits, but the strong dollar has impacted a broader swath of US companies. Both factors are significant reasons why the consensus currently expects an S&P 500 "profits recession" over the next three quarters (Chart 16). Since actual profits have managed to beat estimated profits every quarter since 1998, the actual profits recession may never fully materialize. Still, there is little doubt 2015 will not be a stellar year for US corporate profitability and this is a significant headwind to a market where valuations are already at above average levels. We should get a better feel for the impact of the strong US dollar as managements address this issue during first quarter earnings season. The risk is clearly on the downside as sales are expected to decline for the S&P 500 in 2015 meaning earnings increases must be attained from margin expansion in the face of a stronger dollar. If beleaguered energy companies are removed from the S&P 500 earnings forecasts, however, earnings expectations for the remaining companies are brighter.

**Table 2**

Bargains Hard to Find in Global Equities
Valuation and Profitability Around the Globe

| Index | P/E | EV / EBIT-DA | Div Yield | P/B | Net Income Margin (%) | ROE (%) |
|---|---|---|---|---|---|---|
| Stoxx Europe 600 | 16.4 | 10.0 | 3.0 | 2.1 | 6.4 | 9.6 |
| S&P 500 | 17.3 | 10.0 | 2.0 | 2.9 | 8.9 | 14.4 |
| MSCI Asia Pacific ex-Japan | 13.2 | 8.7 | 2.9 | 1.7 | 8.9 | 12.5 |
| Japan's Topix | 15.2 | 8.7 | 1.9 | 1.6 | 6.9 | 8.6 |

Source: Goldman Sachs

Due to the increase in local currency European share prices, valuations are now roughly comparable with those of the US even though profitability remains meaningfully below US standards (Table 2). Outside of the bruised emerging markets, which may now be near a point of maximum pessimism, there are currently few bargains to be found for global equity investors.

# MARKET COMMENTARY

STEWARDSHIP PARTNERS

## Sorting Through the Data and the Distortions – Still Cautious

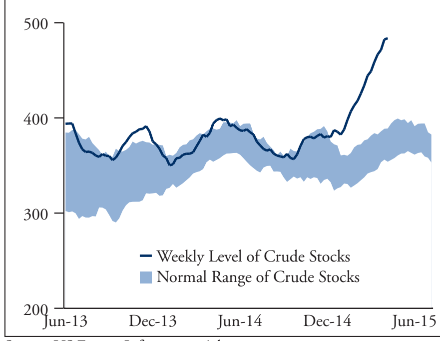
***"This is what the Lord Almighty says: 'Give careful thought to your ways.'" Haggai 1:7***

We moved your portfolio to a defensive stance in mid-January primarily over concerns about above averge valuation, the very long run higher in share prices without a correction, weakening earnings as a result of the strong dollar, the threat of the Fed raising interest rates soon and due to potential negative outcomes, both geopolitically and economically, from potential sudden movements in the price of oil. All of these remain a threat to the markets. Moreover, we have been joined by a chorus of other noteworthy investors expressing fears of a equity downturn in recent weeks, with many highlighting the government distortions in markets as a prime reason for their potential fragility. With the proxy war between Iran and Saudi Arabia getting hotter by the miniute, it is hard to know if the much greater than average stocks of crude oil in the US (Chart 17) will prove to be a blessing or a burden. At the same time, it is quite clear the QE programs in Japan and Europe are supporting financial asset prices in those regions for the moment by pushing massive liquidity into the markets. We have all seen, however, that liquidity is a coward which flees at the first sign of misfortune. Given there are plenty of opportunities for trouble in the world which could frighten the financial markets, we are hesitant to buy shares at above average valuations in a period where earnings growth is either weak or negative. For example, the renewed Cold War could turn hotter, the Middle East could explode into something much more consequential than the many small conflicts which seem to grow daily, dueling national QE programs could produce unintended outcomes, such as the US dollar strengthening continually thereby doing much more serious economic and earnings damage than we have seen so far. Actually, whatever ends up causing a correction, which is inevitable, is not likely something we can accurately predict at the moment. Nevertheless, with monetary authorities around the world juggling so many balls in the air, the risk of an error is greater than normal and their distortions make the markets more brittle than is typically the case. Even if everything continues to move forward without any unexpected negative surprises, the US market is still overdue for a what we would define as a normal correction (Chart 18). Whether such a correction would develop into something more serious cannot be known at this time, but the conditions are ripe for some form of downturn in the markets as investing giants such Bill Gross, Mohammed El Erian, Stanley Druckenmiller, Ray Dalio, Julian Robertson and others have recently highlighted. Druckenmiller stated recently, "Our monetary policy is so much more reckless and so much more aggressively pushing people … out the risk curve". We do not want to be way out on the risk curve when one of these risks finally takes hold and rattles the markets!

**Chart 17**

Massive and Still Growing US Oil Inventory

US Crude Oil Stocks – Millions of Barrels

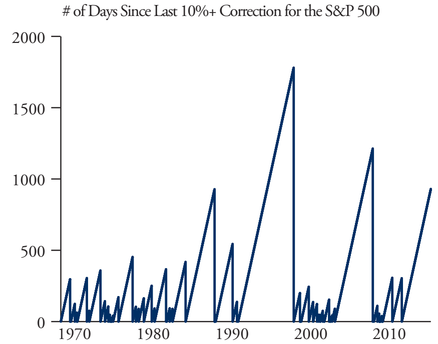



Source: US Energy Information Administration

**Chart 18**

US Shares Overdue for a Correction

# of Days Since Last 10%+ Correction for the S&P 500



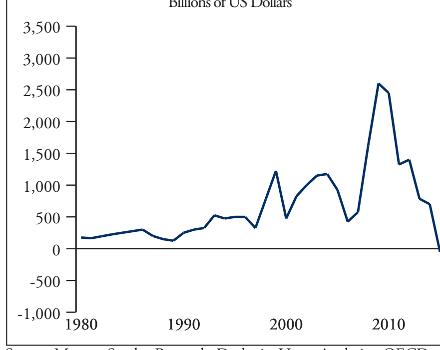

Source: Bloomberg

**Chart 19**

QE is Buying All Newly Issued Bonds!

Total Net Issuance of Government Bonds Turns Negative

Billions of US Dollars



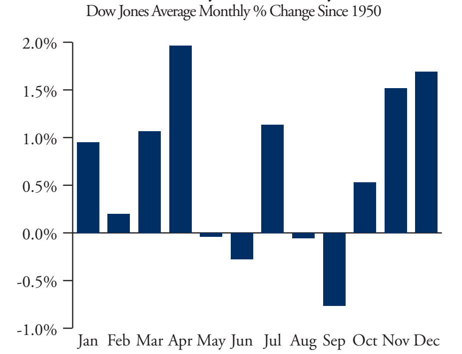

Source: Morgan Stanley Research, Dealogic, Haver Analytics, OECD, DMO, US Bureau of Public Debt

One of our concerns is the financial markets will suddenly lose faith in the ability of the world's central banks to keep the global economy on a steady footing. As can be seen in Chart 19, central bankers have now instituted so much QE they are purchasing more government bonds than their nations are issuing in 2015. Many talk about a shortage of bonds and JP Morgan CEO Jamie Dimon recently predicted an impending crisis due to there being insufficient liquidity in the global bond markets. The US's QE program was reasonably calibrated with the reality of the markets, but the Japanese and European QE programs may be taking what some believe to be a good thing way too far.

**Chart 20**

Sell in May and Go Away?

Dow Jones Average Monthly % Change Since 1950




Source: Chartoftheday.com

Looking at the Dow Jones Industrial Average, the best month for investors, on average, since 1950, has been April with almost a 2% gain. Over the next five months, however, the average return is negative four times, with only July providing some relief (Chart 20). If the historic "sell in May and go away" pattern holds in 2015, our cautious positioning may prove helpful. Still, what we are minimally expecting is a normal 10-15% market correction. We believe there are enough concerns and high enough valautions to bring one about before too much longer. And other than a liquidity fueled bubble, which is possible, it is hard to see stocks flying higher while economic and earnings trends remain weak.

***We at Stewardship Partners continue to be grateful for the opportunity to serve your investment needs. Please do not hesitate to contact us if you have any questions or if we can be of assistance.***

# Biblically Responsible Investing (BRI) – Investing as Jesus Would

***"Blessed are they that maintain justice, who constantly do what is right." Psalm 106:3***

Stewardship Partners, founded in 2000, is a leader in the field of investing with a Christian perspective, a form of Socially Responsible Investing (SRI) known as Biblically Responsible Investing (BRI). Rusty Leonard, CFA, Stewardship Partners' founder and CEO, practiced this investment philosophy while managing over $3 billion of assets as a portfolio manager during his decade of service with the Templeton organization. He also had the privilege of working directly with world-renowned global mutual fund manager, Sir John Templeton. **By employing a BRI approach to investing, Stewardship Partners seeks to achieve long-term capital gains through ownership in securities of companies that are a blessing to mankind. Conversely, we seek to avoid profiting from owning companies engaged in sinful activities which bring physical and spiritual loss to our fellow man. Our heart's desire is to do no harm to our fellow man in the process of being the best possible guardians of the wealth the Lord has given us stewardship over.** Simply put, a "what would Jesus do" approach to portfolio management is what we seek for our clients.

Below are just some of the issues of concern to Stewardship Partners and the specific sinful activities that fall into each category:

1. **We desire *justice and mercy for the defenseless* so we seek to avoid companies involved in:**
   - Abortion
   - Life destroying or distorting scientific research
   - Human rights issues such as religious persecution, terrorism and political oppression

2. **We desire *justice and mercy for the poor* so we seek to avoid companies involved in:**
   - Greed-based marketing techniques
   - Discrimination and unjust labor practices
   - Any abuses of the poor, children and/or the elderly

3. **We have *compassion for those addicted and/or engaged in sinful lifestyles* so we seek to avoid companies involved in:**
   - Alcohol, Gambling and Tobacco
   - Pornography
   - Homosexuality (those companies deemed to be the most active supporters)

4. **We desire to *protect marriage and the family* so we seek to avoid companies involved in:**
   - Entertainment that seeks to destroy biblically-based attitudes
   - Efforts to promote lifestyles the Bible indicates are sinful

**Additionally, we favor companies that clearly embrace:**
- Honesty, Compassion, Diligence, Prudence and Creativity
- Support for quality products at fair prices and constructive stakeholder relations
- Support for a sustainable and healthy environment
- Support for charitable giving
- Support for the Jewish people and the state of Israel

We obtain information on both the objectionable practices and the exemplary attributes of corporations from our affiliate **The Biblically Responsible Investing Institute** (www.BRIInstitute.com). We believe BRII gives Stewardship Partners the most comprehensive database of BRI information that currently exists and utilize much of it to realize our goal of investing in a manner that most honors our Lord. Equipped with this information, we are then prepared to make as strong an effort as possible to build investment portfolios which best reflect our clients' biblically-based Christian worldview.

Like all people, all companies are sinners. Therefore, we attempt to use the BRI information at our disposal to eliminate the worst offenders from our portfolios. At times, this is easy. For example, a company involved in making drugs used in the abortion process will always be excluded from our portfolios. In many cases, however, we need to utilize judgment, such as when a company has operations in a country that is a known violator of human rights. The type and size of that exposure, among other considerations, are taken into account before eliminating the company from our portfolios. When judgments must be made we are guided by the principal of trying to do what we believe Jesus would do if He were making the decision.

For a more in depth study of the topic of Biblically Responsible Investing (BRI), please see our paper entitled "The Scriptural Basis for Biblically Responsible Investing".

## BRI in Action – Comparing Good and Bad Corporate Behavior

***"Love must be sincere. Hate what is evil; cling to what is good." Romans 12:9***

Below you will find an example of both a company exhibiting exemplary attributes, The Andersons, and one we avoid, Roche Holding. The Andersons is a holding in some of our Stewardship Partners portfolios while we actively avoid ownership in Roche in order not to be co-owners in enterprises engaged in or supportive of activities which are harmful to our fellow man and our Lord's creation. **We believe, in the long run, both countries and companies that best align their activities with biblical principles will achieve the greatest success.**

## The Good – The Andersons – Christian Values Shine Through

***"Instruct them to do good, to be rich in good works, to be generous." 1 Timothy 6:18a***

Harold and Margaret Anderson founded The Andersons in the 1940's in Maumee, Ohio. Starting as a truck terminal, the company has steadily expanded its activities over the years under the wise guidance of a variety of Anderson family members, expanding into six segments: grain, plant nutrients, ethanol, rail, turf and specialty, and retail. In the grain division, the company operates 45 grain terminals in eight states which can hold up to 140 million bushels of grain. The Andersons also distribute 2 million tons of fertilizer in the nutrients division and can manufacture up to 330 million gallons of ethanol in its ethanol group. The rail segment manages, repairs and leases 22,000 rail cars and locomotives while the turf and specialty sector is engaged in a variety of odd tasks including turning corncobs into a variety of industrial products. The retail group operates 4 general stores and other retail outlets. Clearly, The Andersons is a classic middle-America company and the values the company lives by reflect its roots in the farm belt. Most intriguing to us is the company's willingness to acknowledge divine authority in its affairs as well as its embrace of patriotism. Here is what the company says in its own words: "This Company is founded on the belief that all of us are subject to a higher and divine authority, and that we should aspire to goodness, integrity, fairness, respect and those virtues which we think are consistent with divine will. We believe that possession of these qualities develops self-esteem, merits the approval of others and enhances both private and public welfare. We believe in the traditions of freedom and liberty that exist in the United States. We believe in the free enterprise system, fair competition, compliance with law, the incentives of profit and personal gain and the importance of capital accumulation. We also believe that profit or personal gain must never come at the expense of personal integrity or the public welfare, and that a balance must be struck between the inequalities which come with freedom on the one hand and aspirations for equality on the other." As Biblically Responsible Investors, Stewardship Partners certainly appreciates and are impressed by these stances The Andersons have been willing to take. Precious few companies are willing to clearly acknowledge divine authority in their affairs. In the case of the Anderson family, we know the divinity to which they refer reflects their Christian faith.

By taking such a clear Christian stand in its affairs, The Andersons have the burden of living up to them as skeptical outsiders cynically look to poke holes in their faith. While the company would admit it is far from perfect, it seeks to avoid trouble in a variety of ways, including its Standards of Business Practice policy and its Anti-Fraud policy. The Standard of Business Conduct Policy covers a wide variety of areas which an employee should avoid, including conflicts of interest, supplier relationships, improper payments, respecting other companies' employees and property, protecting The Andersons' assets and keeping important company information confidential. Employees must protect corporate records, seek to preserve corporate assets and provide timely disclosure of developments that would be of concern to management. The company provides employees with an 800 phone number through which they can anonymously report issues of concern to management or the board of directors. To further enhance the ability of the company to quickly identify, investigate and resolve potentially fraudulent activities, The Andersons' comprehensive Anti-Fraud policy sets up each employee's responsibility to report suspected problems and the procedures and process the company will follow to address reported suspicious situations. While no company can assure it will avoid all fraud or other problems, this company clearly makes a concerted effort to inform employees of the risks and their responsibilities as well as put in place procedures to cut off as much trouble as possible before it can gain a foothold. Not surprisingly, The Andersons' reputation in the marketplace for honesty and integrity is strong. While these policies are clearly helpful, we suspect management's attitudes are the main reason for the company's success.

The laudatory Christian character of The Andersons organization is easily observable in the company's treatment of its employees. Here is a sampling of what the company says about it relationship with its employees, "We believe in the dignity of honest work and that working toward Company goals should provide support and opportunity for each member of the organization to establish and progress toward personal goals. We are guided by a sense of caring and equal treatment and avoid excessive symbols of rank and status. We strive for leadership which not only cares, but listens. We emphasize face-to-face communication and our Open Door Policy provides an opportunity for any member of the organization to sincerely and constructively seek a solution to a job-related problem without necessarily following the usual chain of authority. Opportunities for employment and advancement are available to all qualified candidates, regardless of gender, race, age, religion, national origin, disability, or other differences which have no relationship to job requirements. We are committed to providing a work environment free from all forms of harassment." Not surprisingly, the company's salary and benefits packages back up its commitments to treat its employees with dignity and respect. The company states it is committed to providing a benefits package that supports and encourages a healthy lifestyle. A comprehensive healthcare plan is provided including HSA and flexible spending accounts. It also makes available a healthy lifestyle plan that encourages employees to stay fit and adopt habits that lead to good health. The Andersons offers retirement savings plans, incentive plans and employee stock purchase plans to assist workers with long term economic security. Life insurance and educational assistance are also provided. The company also has a policy of promoting from within the company whenever possible.

Given The Andersons Christian-based values, expressed very clearly and eloquently in its Statement of Principles, it should come as no surprise that its philanthropic efforts are also extensive and noteworthy. Chairman and CEO Mike Anderson stated this, "We believe we should generously share our time, talents and financial resources in support of worthwhile community endeavors. In addition, we encourage others to do the same so that collectively we can improve and sustain the quality of life in our communities." Every year since 1947, the company has donated money to non-profits highlighting the company's long legacy of charitable efforts. Giving comes not only directly from the company but also from foundations The Andersons have set up over the years. In 2012 and 2013, the company gave over $1 million in gift cards to community groups which could be used at its general stores. The Andersons has a matching gift program to help employees enhance their own gifts to charity. Each year the company contributes millions of dollars to a broad array of charities including environmental groups, social service charities and civic, health and wealth non-profits. Charities such as the Nature Conservancy, the Salvation Army, Habitat for Humanity, homeless shelters, food banks, the Autism Society, emergency responders and Junior Achievement, among many others. Clearly, the company is committed to "walking the walk" in addition to "talking the talk". The Andersons commitment to assisting those in need is both broad-based and substantial. In 2012 and 2013 its gifts reached 729 individual communities in 39 different states. Shareholders can be proud of the generous nature of this company.

**The Andersons' good works, while numerous, are of course, no guarantee of long-term investment success. As Biblically Responsible Investors, however, the company's commitment to Christian values as well as its outstanding treatment of its employees and exemplary charitable efforts, allows us to know we are shareholders in a company seeking to be a blessing to all. While no company, like no person, is perfect, this is clearly a company which benefits those it comes into contact with and one we can be proud to own!**

## The Bad – Roche Holding – Embryonic Stem Cells and Terror Exposure

***"Things that cause people to sin are bound to come, but woe to that person through who they come." Luke 17:1***

Switzerland-based Roche Holdings is one of the world's largest pharmaceutical companies. Founded in 1896, the company has been responsible for the development of many drugs which have vastly improved, if not saved, the lives of millions of people. On its website Roche states, "We are proud of who we are, what we do, and how we do it." For the most part this sentiment is justifiable as the majority of the work the company performs makes our world a better place. Unfortunately, there are serious exceptions to this which we find it difficult to ignore.

First, the company is heavily exposed to the use of embryonic stem cells in its research. Despite the fact that embryonic stem cell research has proven to be a big disappointment to researchers over the years, the company still is committing serious shareholder resources to this research which sadly uses stem cells obtained from aborted children. In the past, the company has been a major sponsor of stem cell conferences as well as funding and participating in at a leadership level collaborative industry groups seeking to advance the use of stem cells in medical research. Recognizing the horrifying reality of using the remains of aborted children for medical research, the company has chosen to mitigate the negative feedback from concerned pro-life individuals and groups by using only embryonic stem cells from embryos created via in-vitro fertilization that were "no longer needed" and which the parents had voluntarily donated to research. While the company has admirably sought to minimize the impact of its research work by taking this approach, it remains a controversial method. Since we desire to avoid any company that has even a remote connection to abortion, we will not purchase Roche's securities for Stewardship Partners' clients.

Additionally, Roche operates units in Iran, Sudan and Eritrea which have terror connections or are oppressive regimes.

**Excluding Roche Holdings from our list of potential investments is not a difficult decision. As BRI investors seeking to please and honor our Lord, we naturally look elsewhere to achieve investment success as we do not want to be associated with a company using shareholder resources in a manner the Bible defines as sinful and which can have a negative impact on individuals and society in general.**

# STEWARDSHIP PARTNERS MINISTRY COMMENTARY

## Our Ultimate Goal – Funding the Lord's Work

***"Therefore go and make disciples of all nations." Matthew 28:19a***

**It is our hope that Stewardship Partners' ability to create an abundance for you will help you to share with those who are in need and assist in fulfilling the Great Commission.** Our non-profit ministry affiliate, Wall Watchers, provides a free service to help you educate yourself about the many wonderful Christian giving opportunities available to wise donors. We invite you to join the thousands of visitors to our ministry's website at www.MinistryWatch.com, as best we can tell, the Internet's top site for donors to Christian ministries to gather critical information about the ministries they are considering supporting. The site contains a variety of helpful information about hundreds of the largest US-based Christian ministries including ministries statements of faith, the history of the ministry, program accomplishments, ministry financial statements and financial efficiency ratings. Please feel free to utilize this free resource as you seek to be a wise and effective donor to Christian ministries. We would be pleased to help you bless God's people who are in need, and clients of Stewardship Partners have access to further resources from MinistryWatch.com. It is our sincere desire to see Christians leading the way in giving generously, wisely and effectively so that the Lord's work on earth can be completed and many can be both blessed and saved.

## Featured Ministry – Baptist Medical and Dental Mission International

***"Is it not to share your food with the hungry and to provide the poor wanderer with shelter?" Isaiah 58:7***

The Baptist Medical and Dental Mission International was founded in 1974 by missionaries Charlie and Carolyn Herrington in Honduras. Having ministered in this country for six years, the Herringtons had become all too acquainted with the ravages of poverty afflicting those they were seeking to lead to an eternal relationship with Christ. Witnessing a woman dying of cancer with not so much as an aspirin to ease her pain and seeing many with rotted teeth, the Herringtons were moved to ask the Lord what more they might be able to do to help with the practical as well as spiritual needs of those they sought to serve. Out of this yearning to help came the concept of short term mission teams coming to Honduras to help with a variety of healthcare problems the people there faced. Last year over 100 short term missions trips were organized to assist people not only in Honduras but now also in Nicaragua and Nepal as well. These teams will not only bring much needed medical and dental help but also the message that Jesus provides forgiveness from sins and eternal life.

The ministry also runs the Good Shepherd Children's Home in Honduras for abused and abandoned children. More than 100 children currently have all of their basic needs met here and all within a loving Christian environment. The Emmanuel Home for Protection assists abused women under the age of 18, including those with special needs, in Nicaragua. This ministry also operates two Christian schools which currently serve over 500 students by providing a quality education and a hope for the future. A facility housing a clinic, pharmacy and surgical center is located in Honduras. Here is where the most difficult cases are brought to have their needs met and where medical professionals on short term missions trips can operate effectively. The ministry also sponsors two bible institutes for those who are seeking to enhance their theological training. All of this work is accomplished while maintaining a relatively small staff in the US to coordinate the mission's trips and obtain funding. The ministry claims to have served the needs of over 2 million people in its lifetime and to have led over 200,000 people to Christ. Moreover, over $20 million worth of free medicine has been distributed to those in need.

**Baptist Medical and Dental Mission International not only has performed many good deeds, but also has managed the ministry's financial affairs well. As a result, this ministry has attained the highest Financial Efficiency Rating from MinistryWatch.com - five stars. We believe Baptist Medical and Dental Mission International is worthy of your consideration for financial support. While affiliated with the Baptist church, this is an independent ministry that receives its funding from individual like you.**

## The Christian Ministry Marketplace – Helping Donors Give Wisely

***"A generous man will prosper, he who refreshes others will himself be refreshed." Proverbs 11:25***

Much like the stock market provides for a sensible and efficient allocation of capital in our economy, the rise of a Christian Ministry Marketplace is providing donors with a myriad of helpful resources to maximize the impact and joy of giving to the work of the Lord. As donors begin to take their giving as seriously as their investing, they will find the assistance offered by the groups listed below to be invaluable. By utilizing these resources, donors are not only likely to make better personal giving decisions, but are also contributing to the growth in the marketplace itself. By so doing, they are helping to lay a foundation for wiser giving for all who follow in their footsteps. Accordingly, we encourage donors to investigate how these groups might help you to give more wisely, achieve a greater impact and create increased joy for both yourself and receivers of your gifts.

## The Christian Ministry Marketplace
### Resources for Christian Donors

**WHY** to give to Christian ministries?

Teaching on Stewardship:

- Crown (crown.org)
- Eternal Perspectives (epm.org)
- Generous Giving (generousgiving.org)
- Global Generosity Movement (generositymovement.org)
- The Steward's Way (thestewardsway.org)
- The Gathering (thegathering.org)
- MaximumGenerosity.org (maximumgenerosity.org)
- Stewardship Ministries (stewardshipministries.org)

**HOW** to give with a discerning mind?

Professional Advisors:

- Kingdom Advisors (kingdomadvisors.org)
- National Association of Christian Financial Consultants (nacfc.org)
- WaterStone (waterstone.org)
- National Christian Foundation (nationalchristian.com)

Donor Advisors:

- Excellence in Giving (excellenceingiving.com)
- Calvin Edwards & Company (calvinedwardscompany.com)
- E Six-Thirteen (esixthirteen.com)

**WHERE** to invest in kingdom ministries?

Ministry Research:

- ECFA (ecfa.org)
- MinistryWatch.com (ministrywatch.com)
- Acton Institute (acton.org/public-policy/effective-compassion)
- Intelligent Philanthropy (intelligentphilanthropy.com)

Ministry Mutual Funds:

- National Christian Foundation (nationalchristian.com)
- Strategic Resource Group (srginc.org)
- Sovereign's Wealth Fund (kingdomimpactfund.com)

## Featured Ministry Marketplace Participant – Waterstone

***"We carry the offering, which we administer in order to honor the Lord." 2 Corinthians 8:19b***

Founded in 1980 as the Christian Community Foundation, Waterstone helps donors to Christian charities, financial advisors and Christian charities themselves by offering wise counsel and innovative giving strategies to promote generosity to the Lord's work. Over the last 35 years, Waterstone has helped many people to sort through their complicated financial situations in order to reduce taxable income, eliminate estate taxes and minimize capital gains in order to free up as much money as possible to be donated faithfully to worthwhile Christian ministries. Thousands of ministries have been blessed by the work of Waterstone with over $300 million in disbursements to a wide variety of projects. The uses of the foundation's gifts have ranged from orphan care to campus ministry to refurbishing C.S. Lewis' Oxford home and just about anything in between. Under the aggressive leadership of Chief Executive Officer Steve Leach, Waterstone hopes to expand its giving at a much more rapid pace in the future. Waterstone's current target is to more than triple its past giving by reaching $1 billion in donations by the year 2020. In order to help reach that lofty goal, Waterstone has made a special effort to reach out to Christian financial advisors. The open platform the foundation offers and the multiplicity of aids it makes available to advisors make it easy for them to provide enhanced service to their clients while helping them properly set and meet their charitable goals. Whatever the need may be of a donor, financial advisor or charity, there is a very good chance Waterstone will be able to provide a solution which will make the giving process flow easily, provide unanticipated benefits to all involved and yield more eternal rewards than otherwise. When Stewardship Partners' founders were accumulating the needed funds to start MinistryWatch.com, they took advantage of the helpful staff and resources available at Waterstone to help get their ministry launched seventeen years ago. Since that time, Waterstone's services and capabilities have expanded dramatically so that now many more Christian donors, financial advisors and Christian ministries can be blessed by this ministry's efforts. Perhaps you can help Waterstone reach its goal of $1 billion in giving by 2020! One thing is certain, Waterstone will help you use all the available tools and resources to make the most of your giving to the Lord's work.

## *Knowing Jesus Christ as Your Lord and Savior*

While most of those reading this will have already established a personal relationship with Jesus as their Lord and Savior, it is very likely that many have not. If you are someone who has not yet turned your life over to your Creator, we would have failed you miserably if we presented only information relating to your investments yet did not share with you the most important information of all: truths which have eternal significance for your soul and that will have an overwhelmingly positive impact on your life on this earth.

The gospel message is a simple one, far less complicated than the global impact of rising oil prices or the effect of a revaluation of the Chinese currency. For most people, the first part of it is easy to relate to – you are a sinner. If you are anything like the rest of us (and you are) more often than you probably would like to admit, you either do, say or think something that is clearly wrong and which you are ashamed of. "But what's the big deal", you might say. "If everyone has this problem with sin, can't we all just accept the fact and try our best to get along?"

Well, on this earth, that is exactly what we try to do. We forgive one another's faults and press on with life. From an eternal perspective, however, there remains a problem. Our Creator, who loves us with a love that can only be described as extravagant, has prepared an eternal home for us that He very much desires to share with us. Unfortunately, in our sinful state, we are unable to enter into heaven, which is by its very nature perfect. Desperate not to be separated from us for an eternity, our God devised the only possible solution – a divine exchange. He sent His very own son, who was perfect and thus without sin, as a sacrifice to pay the penalty for our sins. In this exchange, Jesus bore, through His death, all of our sins, so that we in turn could receive all the glory that was due to Him. He was made sinful while we were made perfect and, in our now perfect state, we are able to enter into the eternal home our Lord has prepared for us.

What then gives each of us access to participate in this divine exchange?  By responding to this incredible demonstration of extravagant love by our God through an amazing act of your own. As you let the realization of just what your Lord has done for you filter through your heart, mind and soul, you will unavoidably desire to humbly come before Him, acknowledging that it was your sin that led to His sacrifice and recognize His Lordship in your life. And with this step of faith, the divine exchange is completed in your life, and along with it, the assurance of eternal life with a Lord whose love for you knows no bounds. If you have not done so already, we encourage you to take this time to contemplate the issue of your eternal destination and to take that step of faith that will make all the difference in your life, both now and eternally. Based on my experience and the experience of literally millions of others throughout history, it is the most satisfying, enriching and worthwhile choice you will ever make. Years of wonderfully inspiring spiritual growth await you and, if the Bible ever seemed confusing to you in the past, you will now find its wisdom leaping off the pages and into your heart.

If we at Stewardship Partners can be of any assistance to you in this all important matter of your eternal destiny, please do not hesitate to contact us. Like Jesus, we also greatly desire to share an eternal heavenly home with you!



STEWARDSHIP PARTNERS

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