Spring
2015

Spreng Capital Management Inc.

Spreng Capital Management is an investment advisory firm registered with the State of Ohio. Founded in 1999 by James Spreng, Spreng Capital has grown to encompass the very best in service and support for our clients.

Our client base is quite diverse. With clients in 23 states, we offer structured, customized investment management for individuals, profit sharing plans, Foundations, endowments and businesses. We are fee only investment managers, receiving no commissions nor do we sell any financial products. We are paid only by the investment management fees of our clients. We advise our clients on financial planning and manage their assets, making recommendations based entirely upon our clients' needs and goals. Everyone on the Spreng Capital team has a vested interest in the success of our clients' portfolios. Our team has a unique blend of experience, youth and business credentials.

Our use of high quality stocks and mutual funds along with investment grade bonds, allows us the opportunity to deliver consistent long term returns. We focus on minimizing risk and volatility, striving ultimately to deliver the very best after-tax returns possible, within the constraints you have established.

There is nothing that signals success more than referrals from existing clients. Our success is a result of our clients' continued confidence in us and their willingness to recommend us to their family and friends.

If human history has taught us anything through the millennia, it is that often our best attempts at doing the correct thing lead to unintended consequences that can sometimes be worse than the original action. This leads us to the current state of the Federal Reserve in US and world economic policies. During the financial meltdown of 2008, the Federal Reserve and the US Treasury did a wonderful job of coordinating financial responses and improvising new and innovative ways to pour billions of dollars into our staggering economy. Some of these actions were far reaching in scope, and to some, borderline illegal based upon the original mandate of the Federal Reserve System when it was founded in 1913. However, the policies that were put in place bought the US economy and banking system the time that was necessary to patch and heal the damages from the greed and avarice of the many individuals who were making and re-selling fraudulent loans. By lowering interest rates to almost 0% and literally printing money through the policy of buying our own US debt with dollars that magically sprung from the Treasury's printing presses, the excess liquidity of cash that was poured into the economy turned a possible Great Depression II into just the Great Recession!

Index	Qtr.
DJIA	(0.26)%
NASDAQ	3.48%
S&P 500	0.44%

To their credit, the Fed realized that they were dealing in uncharted waters with many of their newly minted policies. This uncertainty rattled investors around the world who desperately crave stability and openness. In an effort to ease the concerns of taxpayers, politicians and investors, the Fed publicly announced criteria that needed to be met before they would begin the process of unwinding the historically low interest rates and the Quantitative Easing. This was nothing more than printing money to buy our own debt from the marketplace. The Fed proclaimed that unemployment had to drop to a certain percentage, inflation had to meet certain criteria and certain other financial parameters from which the Fed makes decisions, had to meet certain levels. Fortunately, for the most part, all of these criteria have been met in recent months. Therefore, in keeping with this new goal of increased transparency and openness from the Fed, in theory, the Fed should start to raise interest rates in the US as soon as June of this year.

This is where the issue of unintended consequences rears its ugly head. We really don't think that the Fed wants to raise interest rates and yet, due to its previous pronouncements of the financial parameters needed to be met to raise rates, they are backed into a corner where they must raise rates to save face. This is never a good situation. It's never good on the playground and it's really a bad idea in public policy!

"9 of the last 10 recessions in the US were preceded by a significant increase in the price of oil."
Federal Reserve Bank of St. Louis

Why is the Fed reluctant to raise interest rates when their original goals have supposedly been met? There are multiple reasons for their reluctance. The rest of the world is cutting interest rates at the exact time that we may be raising rates in the US. All of the other Central Banks of the world's economies are terrified of deflation and are cutting interest rates to boost economic activity and spur domestic spending. There are several countries that will now charge you to keep cash in the bank. Germany recently issued 5 year government bonds that actually sold for more than the face value of the bonds yielding the investors who purchased the bonds a return of -0.08% per year for the next five years! Switzerland and Japan will charge you interest to keep cash in the bank. Why would someone accept a negative return on their German government bonds? Quite simply, they expect the European Union to continue to cut interest rates instead of raising rates. As interest rates go down, the value of the German bonds will go up and the investors will sell the bonds for more money than they paid to some fool who in turn thinks that rates will go even lower. Then they can sell to the next fool. The statement that "trees don't grow to the sky" was made in relation to the prices of stock in the internet boom of the late 1990s. It simply meant that prices on stocks of these high flying technology companies could not continue to go up forever. The crash of the internet boom in 2000 proved it to be a true statement. While common sense would indicate that interest rates cannot drop below 0% a year, several economies are testing that very hypothesis.

As other economies have cut interest rates the value of the US dollar has risen against the other currencies of the world. While this is wonderful if you are travelling to Europe on vacation this summer, everything will cost you 20% less than it would a year ago due to the difference in the currencies. A stronger dollar is a terrible thing if you are a company who exports a lot of your goods and services to another country. The ugly American tourist may benefit from the 20% valuation change but the company Caterpillar or General Electric, who exports 40% of their product overseas, finds that the cost to their buyer is now 20% more than it was a year ago just due to nothing more than a change in value of the currencies in play. Imagine trying to convince an overseas consumer that your product is worth 20% more than it was just a year ago with no changes in the basic product! This makes it very difficult for companies who export a lot of product to maintain their profits and revenues let alone try to increase them. Raising interest rates in the US will only strengthen the US dollar against other currencies and make US companies that export a lot of goods and services that much more at a disadvantage. Ultimately, this hurts the US economy in the long run to have a currency that is too strong against the rest of the world's currencies.

Raising interest rates also hurts US consumers with big ticket purchases like homes, cars and washers and dryers. Any purchase that is usually financed with borrowed money becomes more expensive if the Fed raises interest rates, further threatening the nascent US economic recovery. The one entity hurt the most with rising interest rates is the world's largest borrower, the US government itself. While the Fed emphatically states that it is apolitical, only a fool would think that the Chairman of the Federal Reserve and the Fed Board Members do not read the newspaper or listen to the talking heads on television. If there is even a remote possibility that raising interest rates would hurt the US economy due to larger budget deficits run by the Federal government due to larger interest payments on the Federal debt, then it is one more reason for the Fed to hesitate when it comes time to vote on raising interest rates.

While consumers may cheer the falling price of oil, investors nervously watch on the sidelines. A great deal of the gains in employment in the US labor market have been due to the increasing number of oil rigs and the transportation needs of removing oil from the fracking rigs in certain areas of the US. As the price of oil drops below the break even price of extracting oil from the fracking of shale, rigs will eventually be shut down or capped thus increasing the number of unemployed workers again. The oil boom was one of the few bright areas of employment for the US worker and now even that one bright spot looks cloudy.

Greece is once again on the verge of defaulting on its sovereign debt. Haven't we seen and heard this before? The European Union politicians did what all good politicians do when confronted with a crisis with only painful solutions available. They delayed any action for four months! Now that is what you call leadership. There is even a new term coined for the eventual exit of Greece from the European Union, Grexit. When Greece eventually withdraws from the EU, notice we said when, not if, the Fed may again have to stimulate our economy with cash in the form of lower interest rates or Quantitative Easing or both. There will be shocks to the monetary systems of the World when Greece leaves. There are all kinds of contracts that have been written with the understanding that Greece will pay in Euros. How will these contracts be negotiated or

"Undocumented immigrants that will receive a social security number under President Obama's 11/20/14 executive order are eligible for up to 3 years of tax refunds under the earned income tax credit even if they never filed a form 1040 in any of the 3 years."
Internal Revenue Service

altered? Who will win and who will lose when Greece starts to print their own currency, as worthless as it may be. Again, just more stresses to a world economy that is wrestling with the throes of deflation.

Last, but certainly not the least of the worries that the Fed must deal with in analyzing the risk to raising interest rates in the US, is the continued world struggles with terrorism and belligerent dictators like Vladimir Putin in Russia and Kim Jong-un of North Korea. Bad characters have been around for thousands of years but in a world where so many economies are so closely intertwined on a daily basis, disruptions and dislocations purposely perpetuated on the peoples of the world community have consequences that reach far beyond provincial locales. The Fed and the US government need to be in a position to respond to the slightest provocation with a swift and effective reaction.

So what will the Fed do as far as raising interest rates? It is always dangerous to make predictions because the odds of being incorrect are usually much greater than being absolutely correct. We think that the Fed has backed themselves into a corner with their pronouncements and to save face they will raise interest rates this summer by 0.25%.....and then stop raising rates. We think that they fear the unintended consequences of raising rates while everyone else is lowering rates. By raising rates, albeit by very little, the dollar will strengthen more, export sales will drop and jobs will be lost. Raising rates lets them say that "Hey, we did exactly what we said we were going to do, just not by a very substantial increment". The Fed can then take another "wait and see" position and issue new criteria that must be met before interest rates start to rise to more normalized levels..... whatever that level might be deemed "normal".

So how did the US equity markets perform in the first quarter of 2015? They were basically flat for the quarter. The Dow Jones Industrial Average actually lost (0.26%). The NASDAQ was up 3.48% and the Standard & Poors 500 Index was up 0.44%. The market is responding to all of the pending uncertainty with much more aggressive swings to the upside and to the downside than we experienced last year. 2014 was a very mild year for volatility in the markets, abnormally so. 2015 is starting out to present more normal levels of volatility but when investors worry and fuss over every little issue on a daily basis, increased volatility does little to sooth their jangled nerves. I found a very interesting fact that really puts gains and losses from the equity markets in perspective. According to BTN Research, the split between ***up*** and ***down*** days for the S&P 500 Index over the last 50 years from 1965-2014, is ***53% "up"*** and ***47% "down"*** days. The split in 2014 was ***57/43***. That certainly speaks volumes for trying to "time the market" and get out and then get back in just in time to hit the up days. Timing the market cannot be done on a consistent basis by anyone.....no matter what the CNBC talking heads say or the "investment newsletter" boys and girls might profess.

As a child of the 1970s and the first Arab oil embargo, I realize that I am scarred by that experience as much as people living through the Great Depression were in the 1930s. When I was in college in Upstate New York in 1973, I could only buy gasoline on odd or even numbered days of the monthly calendar based on the last number of my license plate on my car. When I was driving home I had farmer friends lined up along the way so that I could stop at their farms and buy "farm gasoline" from them if the stations were out at the time of my travels. I find that in the ensuing 40 plus years I have remained hyper sensitive to energy costs and availability. You can imagine how perplexed I am with the current state of affairs in oil production and politics. The fracking boom in the US has turned the old power structure of the Middle East oil sheiks on its ear. OPEC has literally had a stranglehold on oil production and pricing power for the last 50 years. Saudi Arabia has decided that they are the lowest cost producer of high quality oil and are not pleased with their loss of pricing power and market share. They have always been the producer who controlled the markets. The vast majority of the other members of OPEC cheated on reducing their oil quotas into the marketplace because their governments and people had become so addicted to oil revenues that they feared a reduction of any kind would trigger civil unrest and the possible resulting overthrow of the current "oil baron" in charge of the country. For the first time ever, Saudi Arabia has decided that they will not reduce their oil production and sale for the sake of their OPEC brethren. The Saudis want to lower the cost of oil to a point where the fracking boom in the US cannot compete due to higher costs of production. A totally unanticipated side effect of this oil war has been the destruction of Russia's economy in the process. Russia's economy is still very primitive. Their primary source of revenue and exports traditionally have been raw materials like energy in the form of oil or natural gas, timber and probably their only quality value added export..... vodka. The combination of Western sanctions and the drop

"The average interest rate nationwide for a 30 year fixed rate mortgage was at least 10% for the 12 consecutive years of 1979-1990. The average rate today is 3.78%!" Freddie Mac

in oil prices by 50% have bitten into Putin's loyalist's pockets quite severely. With no reduction in pumping of oil anywhere in the world, stockpiles are building to a level never seen before. Almost all above ground tanks, salt mines in Kansas and idle oil super tankers anchored offshore are filled to the brim with crude oil present a very unique situation that the world has not experienced before. The Japanese basically attacked Pearl Harbor in 1941 drawing the US into the war because the US was at that time, the world's largest exporter and producer of crude oil. As retaliation for Japan's incredible devastation and cruelty in their occupation of China, the US had stopped all exports to Japan. Japan tried to destroy the US Pacific Naval Fleet at Pearl Harbor so that the Japanese could invade the Dutch Indies and Indochina to gain access to the oil available in these locales. While US consumers may cheer lower energy and eventually, lower gasoline prices, oil prices that drop so low that they create economic and political instability are not a recipe for sunshine and roses. Greece, deflation, interest rates and crude oil prices that may crater to the point of instability can cause some restless moments for investors going forward.

Our task as investors in 2015 will be like any other year, to garner good rates of return with an acceptable amount of risk. This is not an easy task and requires diligence and hard work. Energy investments are a prime example of the obstacles that we face. We all know that energy costs will rise again in the future. However, how long is in the future? We can buy great energy companies on sale right now……and then watch them drop even more in price if the price of crude oil continues its free fall in price! As investors we need emotional stability and above all, patience.

We are excited and optimistic about the future both for you and for our firm. We continue to receive large influxes of new funds thanks to you and your many referrals that we receive every month. No one said securing a viable financial future is easy; nor should it be. There are many challenges and headwinds that we will face every day. The markets contain risk and they offer reward. Our task is to balance the two and to deliver good returns with an acceptable amount of risk.

If you have questions about your holdings or about the general condition of the economy, please contact us at once. If we do not have a current email address for you would you please email us and allow us to add you to our regular list of clients with whom we correspond. Our email addresses are jspreng@sprengcapital.com, tbrown@sprengcapital.com and lkunzer@sprengcapital.com Please be assured that we are monitoring market situations at all times.

If there have been any changes in your financial circumstances of which we should be made aware, please notify us at once. If you would like a copy of our most recent Form ADV or our Privacy Policy, please call the office. If you have not visited our website, please do so at www.sprengcapital.com

We appreciate the opportunity to work with you, your families and your businesses. We are very grateful for the many referrals that you have provided to us. We can think of no greater compliment than to have you recommend us to your family and friends. We will continue to do our very best to provide you with healthy, consistent returns with a minimum of risk. Always remember, "Investing is a marathon, not a sprint."

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