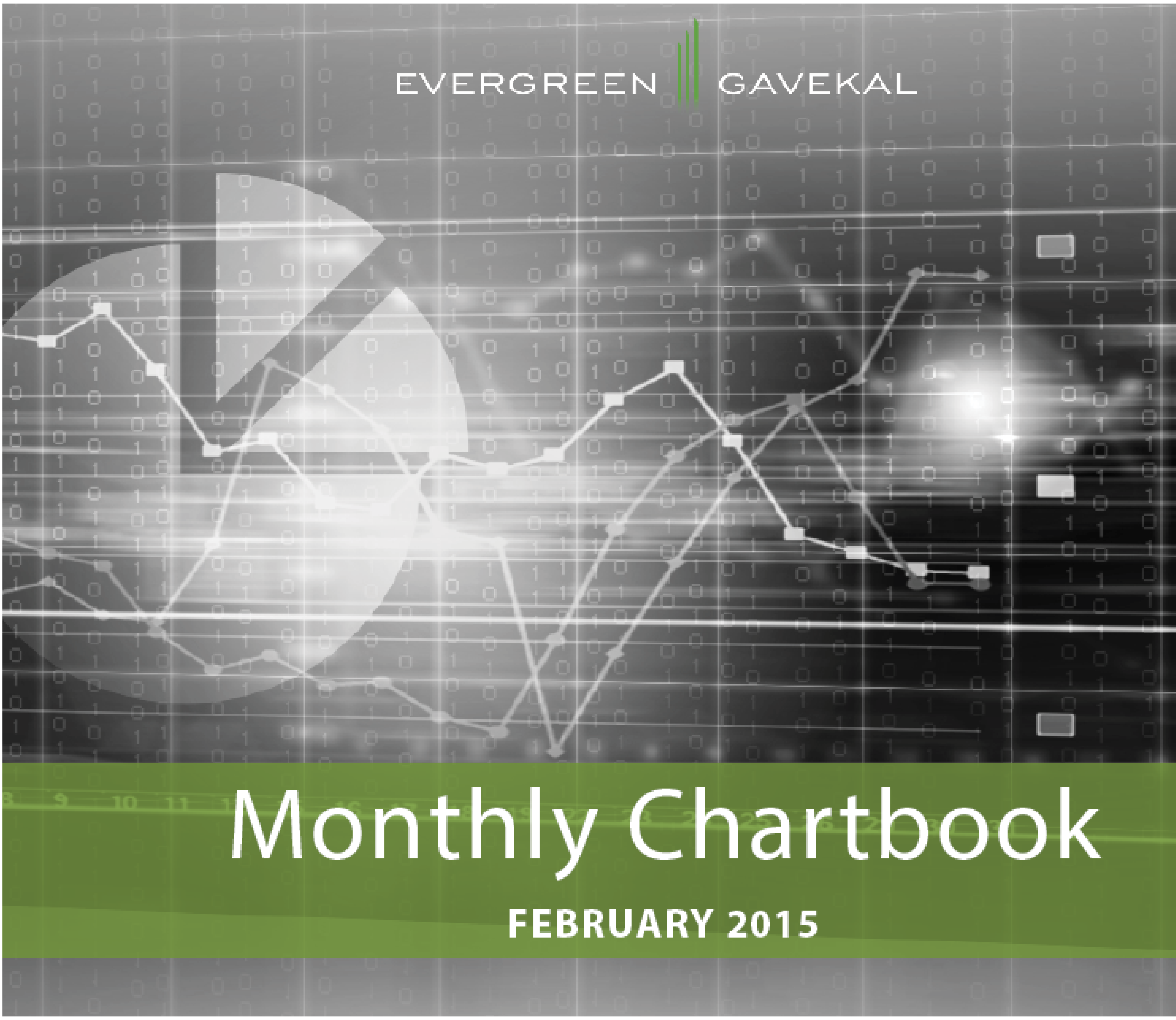
February 27, 2015

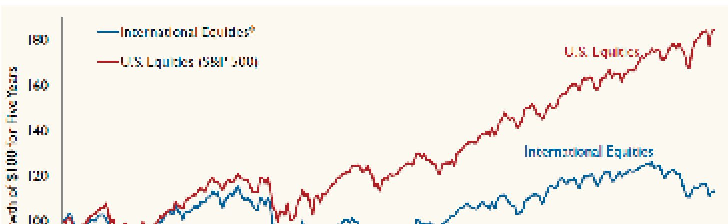


Monthly Chartbook

BY DAVID HAY

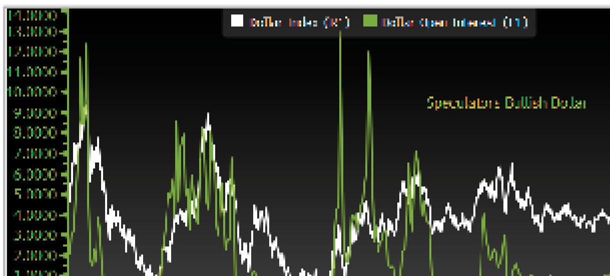
A doozy of a do-over? For those of us who, in recent years, have been too skeptical about the US market's ability to continue its astounding ascent, we may have been granted a mulligan. I certainly include myself in the overly cautious category, at least since 2012. But in 2010 and 2011, when international investing was all the rage, this newsletter consistently suggested that US stocks were a better value. And, as you can see below, that most definitely has been the case.

NEXT ALLOCATION MOVE IS LIKELY GLOBAL



evaluate our Canadian bond holdings in the loonie rat
greenback! But, since almost all of Evergreen's clients p
in bucks, I don't think that's fair. The dollar, though,
for a counter-trend reaction based on the rabidly bulli
toward our once-shunned currency.

TRADE WEIGHTED DOLLAR AND N
SPECULATIVE POSITION

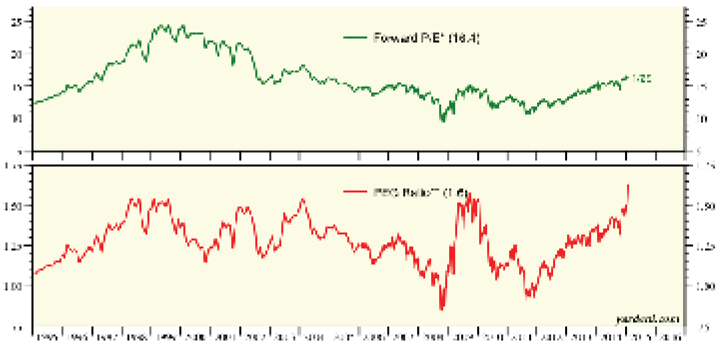


BY DAVID HAY

PEG-asus rising..and rising...and rising. The standard valuation measure for stocks is, of course, the P/E ratio. But like a lot of *shortcuts* to determine if a security is cheap or dear, it has some *shortcomings*. Beyond the issue of the profit margin cycle, as we so often cover in these pages, there is also the aspect of comparing the P/E to the underlying growth rate.

For example, if a company is growing at 10% (which few companies are doing these days) and its PE is 15, the PE-to-growth-rate, or PEG, is 1.5. Yet, if another company, also selling at a P/E of 15, is in a much faster growth stage and can realistically be expected to continue growing at 15%, its PEG is just 1. Naturally, for individual companies there are a lot of misses when

S&P 500 VALUATION



**Price divided by 12-month forward consensus expected operating earnings per share*
***P/E relative to consensus 5-year LTEG forecase*
Source: Thompson Reuters I/B/E/S

it comes to projected long-term profit growth rates. Fo overall, though, it's a more predictable process. On th the esteemed Ed Yardeni, the S&P 500 is more gener than it ever has been.

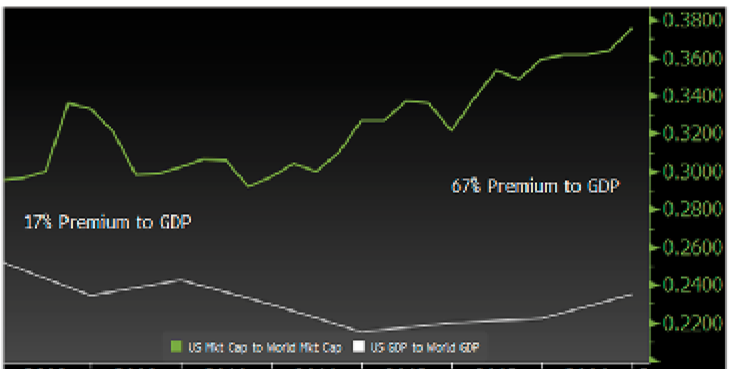
Frankly, this might still be too charitable, as this ana on some highly optimistic five-year earnings forecas the reality is similar euphoria has been the case in the particularly after years of swelling profits.

The mythological Pegasus

BY DAVID HAY

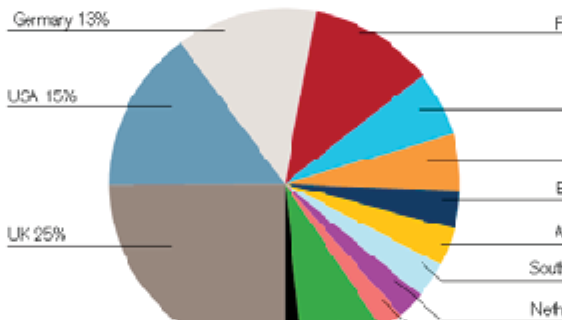
A tad over-cooked? The US is unquestionably home to a disproportionately large number of our planet's most profitable companies. Yet, per the chart below, the fact that America generates 22% of global GDP but represents close to 38% of total stock market value, might indicate that our profitability advantage is perhaps overly priced in.

US MARKET CAP AND GDP RELATIVE TO THE WORLD



It's also interesting to look back to the allocations at the 20th Century. Clearly, being the big winner in two as well as having the world's most dynamic economy benefited America's stock market (conversely, Germ and the UK have all seen their relative market caps contract to 2.9%, 3.0%, 5.7%, respectively).

RELATIVE SIZES OF WORLD STOCK MA END-1899

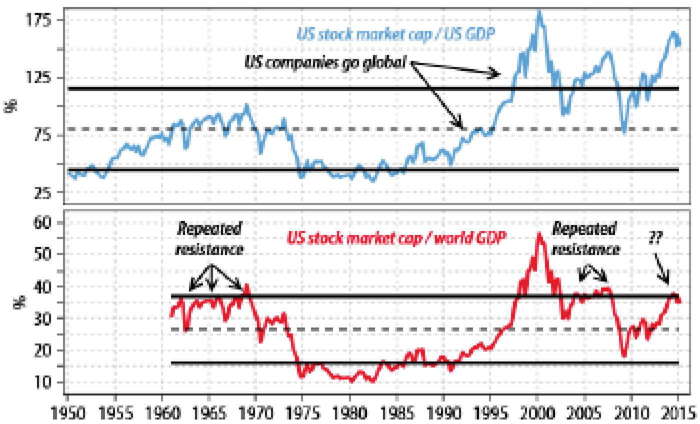


Monthly Chartbook

BY DAVID HAY

GaveKal's talented Will Denyer, who was prominently highlighted in the issue of *Barron's* (click here to read), recently published an intriguing chart, shown below, in a similar vein.

BUMPING UP AGAINST THE CEILINGS



Source: GaveKal Data, Macrobond

The upper chart is the standard way of looking at market cap compared to GDP. On this basis, which we've run several times, US stocks appear in the extreme danger zone. Will's version is the second chart which compares US market cap to global GDP. This is possibly more accurate based on the fact that the S&P 500 generates about 40% of revenues from abroad. Obviously, Will's iteration is less alarming.

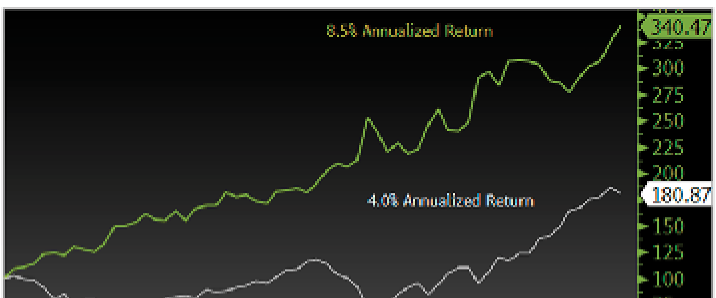
However, excluding the absurd stock bubble of th the US market is priced at levels where it has hit the w accurately, ceiling—in the past.

Monthly Chartbook

BY DAVID HAY

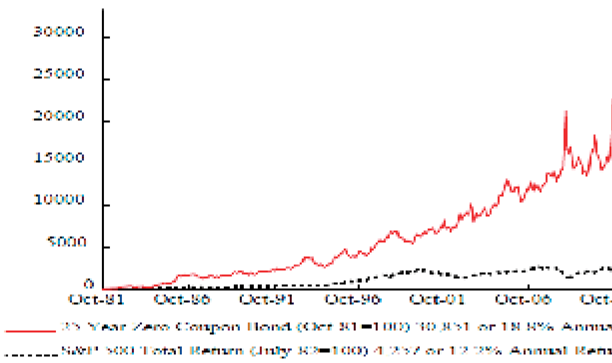
Bonds for the long run? It would have been swell to have anticipated that US equities would soar to such dangerous levels so soon after the cataclysmic decline at the end of the past decade—not to mention the one that kicked it off. But, remember, the S&P still has returned a mere 4% annually since this millennium began, versus 8.5% per annum an investor would have earned with a 30-year Treasury bond purchased at the start of 2000.

30-YEAR TREASURY AND S&P 500 TOTAL RETURN NORMALIZED 12/31/1999



the past thirty years. If you smell a trap, you've got th bloodhound!

COMPARATIVE STOCK AND BOND PERFO



Source: Bianca Research LLC, Haver Analytics

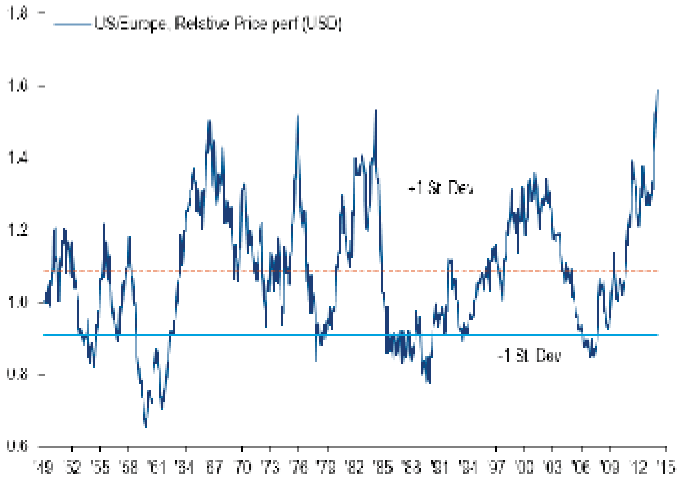
A long-term zero-coupon treasury has returned annually since the early 1980s, a stunning 7% more pe

Monthly Chartbook

BY DAVID HAY

Relatively speaking. Regular EVA readers are well aware that Evergreen is not exactly bullish on Europe's long-term prospects, at least while that incongruous creation known as the euro continues to be the sole currency for most of the Continent. However, when we look at a chart like the one below, we have to admit that eurozone stocks may be priced to out-perform the US over the next three to five years.

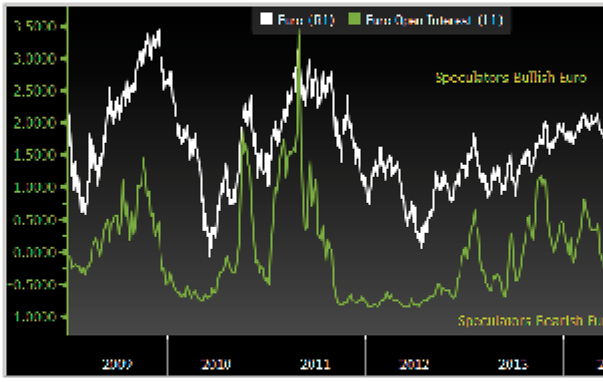
US STOCKS AT 60-YEAR HIGHS VS. EUROPE (USD)



Source: BofA Merril Lynch, Bloomberg, GFD

The feverish bearishness on the euro is nearly the exact inverse of the hyper-bullishness on the buck. This causes us to wonder if the euro isn't poised for a rally, despite its intrinsic flaws. If so, this would add to any stock-driven returns fron issues, rather than detracting from them as has been t years.

EURO/DOLLAR EXCHANGE RATE AND SPECULATIVE POSITION



Source: Bloomberg, Evergreen GaveKal

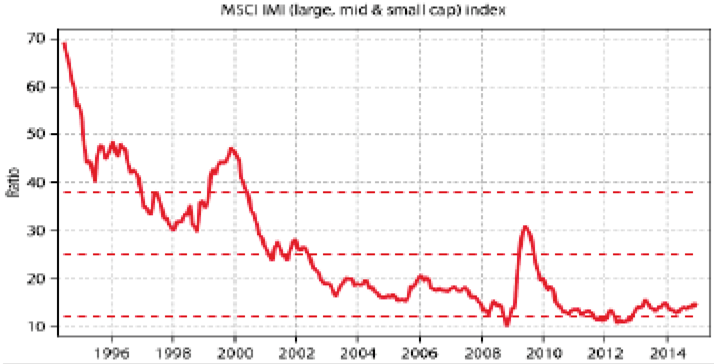
Japan is another leading economy that has been in a endless lag position versus the US, and the same is equity market. What was the most expensive market i up to the mid-1990s is now one of the cheapest. As y from the charts on the next page, this is true on both price-to-book value basis

Monthly Chartbook

BY DAVID HAY

JAPAN 12M FORWARD P/E

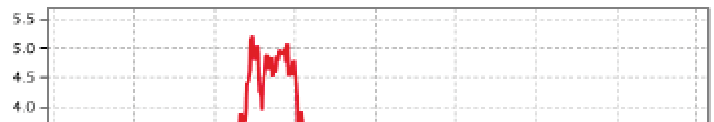
MSCI IMI (large, mid & small cap) index



Source: Gavekal Data/Macrobond

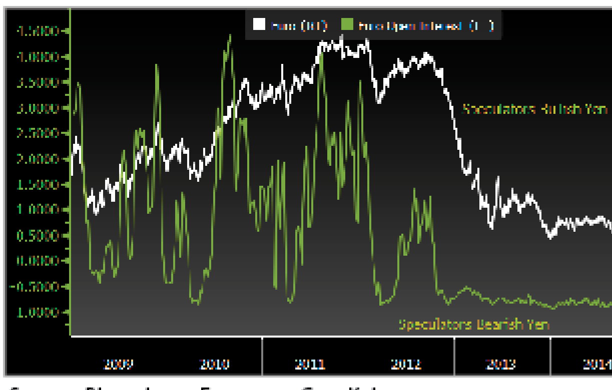
JAPAN MARKET PRICE TO BOOK VALUE

Japan MSCI (mid and large cap), price to book value; vs LT mean and std. deviation



Also, the yen has fallen much further than and sentiment is extremely hostile toward Japan Accordingly, with almost everyone all bulled up on the and ferociously bearish on the euro and the yen, it's qu the US dollar is on the verge of a sharp correction.

DOLLAR/YEN EXCHANGE RATE AND N SPECULATIVE POSITION



Monthly Chartbook

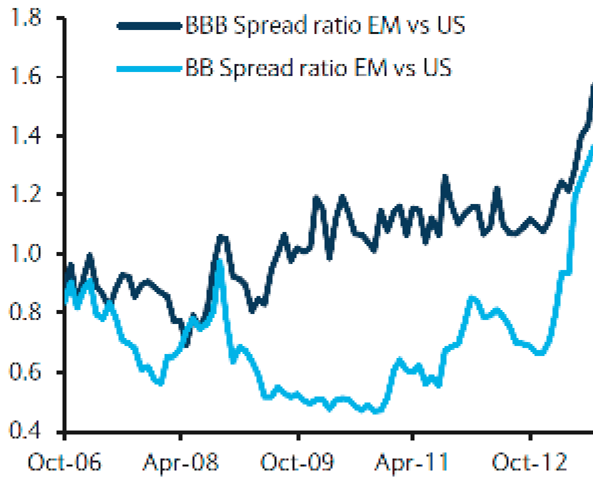
BY DAVID HAY

Are the submerged set to emerge? There is no asset class as detested right now—outside of those commodity-related—than emerging markets. Our preference from the equity angle is to play these primarily in Asia but developing bond markets are looking almost irresistibly cheap, at least in their own currencies.

EMERGING CURRENCIES BACK TO 2003/2009 LOWS: A GLOBAL VIEW

Source: JPM Index of Emerging Currencies

THE EMERGING MARKET/DEVELOPED M SPREAD RATIO IS BACK AT ITS HISTORICA



Source: Barclay's Research

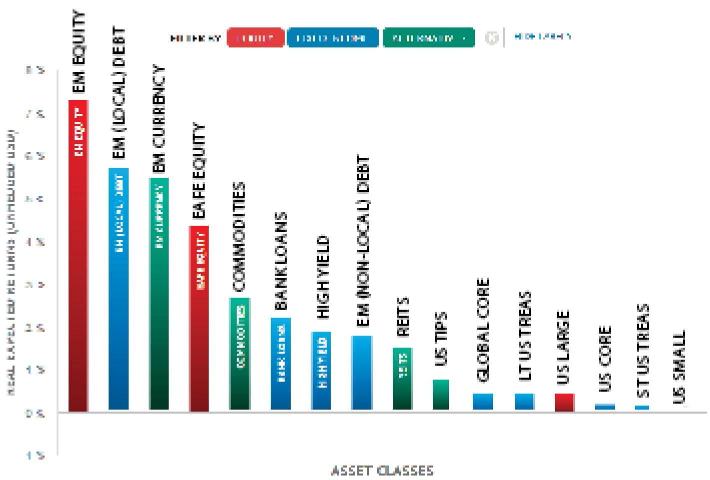
After selling out of our local currency emerging m last summer, we are seriously considering a retur closed-end funds dedicated to these bonds (most o selling at material discounts to their underlying net a which also have been seriously punished).

Monthly Chartbook

BY DAVID HAY

Same song, different key. To conclude my section of this month's Chartbook, I thought I'd run a twist on a graphic I've used several times in the past. EVA readers may recall the tables we've previously included on projected asset class returns over the next seven years from GMO, the Boston-based money management firm with a stellar record in this regard. The following chart comes from the left coast, California-based Research Affiliates, home to one of the smartest men in the investment business, Rob Arnott.

REAL 10-YEAR EXPECTED RETURN



Source: GMO

The above return projections are after inflation, so add around 2% to arrive at the nominal number. Thu cap stocks are forecasted by Research Affiliates to pro 3% annually before inflation. This is slightly more opti GMO (though their timeframe was shorter) but stil above what you can get even with a 10-year treasury days. If both of these firms are right, as Evergreen be are, you need to go offshore, particularly into areas lik Asia, for returns that justify the downside.

Otherwise, investors are back to accepting return bad bargain they've settled for twice in the last 15 y got this nagging feeling we're headed for a three-pea

Monthly Chartbook

BY JEFF DICKS & JEFF EULBERG

2014 S&P 500 SALES AND EARNINGS GROWTH

Sector (GICS)	Reported	Sales Growth	Earnings Growth
11) All Securities	461 / 500	2.45%	6.36%
12) > Energy	38 / 43	-4.42%	-1.74%
13) > Materials	29 / 29	1.34%	7.72%
14) > Industrials	64 / 64	2.36%	7.42%
15) > Consumer Discretionary	66 / 84	4.65%	2.26%
16) > Consumer Staples	37 / 39	2.15%	2.14%
17) > Health Care	53 / 56	8.45%	14.25%
18) > Financials	83 / 85	0.02%	4.65%
19) > Information Technology	62 / 64	4.85%	9.10%
20) > Telecommunication Services	6 / 6	3.65%	20.57%
21) > Utilities	23 / 30	6.74%	7.23%

Source: Bloomberg

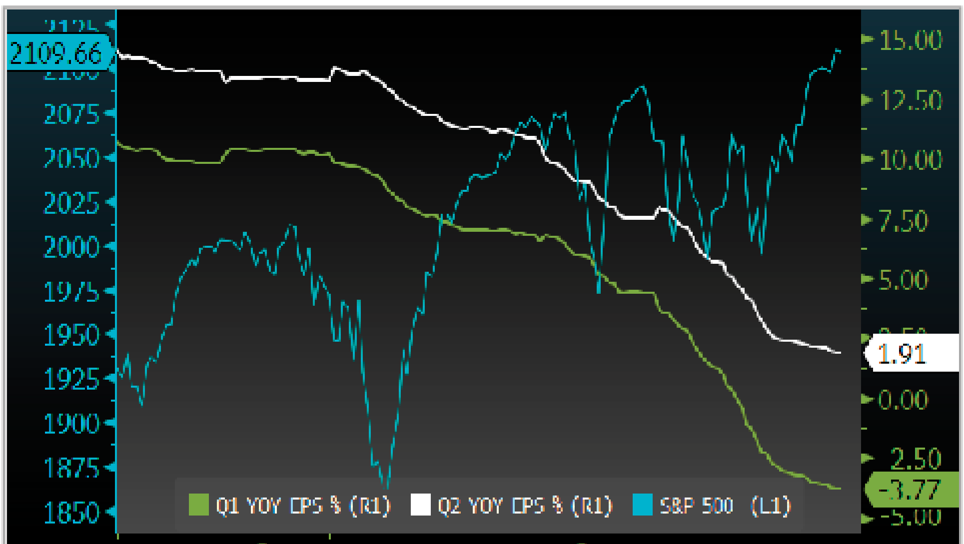
Given that 90% of the S&P 500 h fourth quarter earnings, we though be a good time to reflect on both t earnings period, as well as the over the reports. Due to the catastrophi the price of oil over the last six mon companies obviously experienced a headwind in 2014. However, as the the left shows, outside of the healt telecom sectors, most industries st show meaningful growth in earnin As of now, reports show that sales and earnings grew 6.4% in 2014. O are pretty mediocre numbers, and even worse when taking sales grow account. While energy was a big re disappointing results, strategists w these numbers don't warrant conc

S&P 500 EARNINGS ESTIMATES REVISIONS

Source: Bloomberg, Evergreen GaveKal

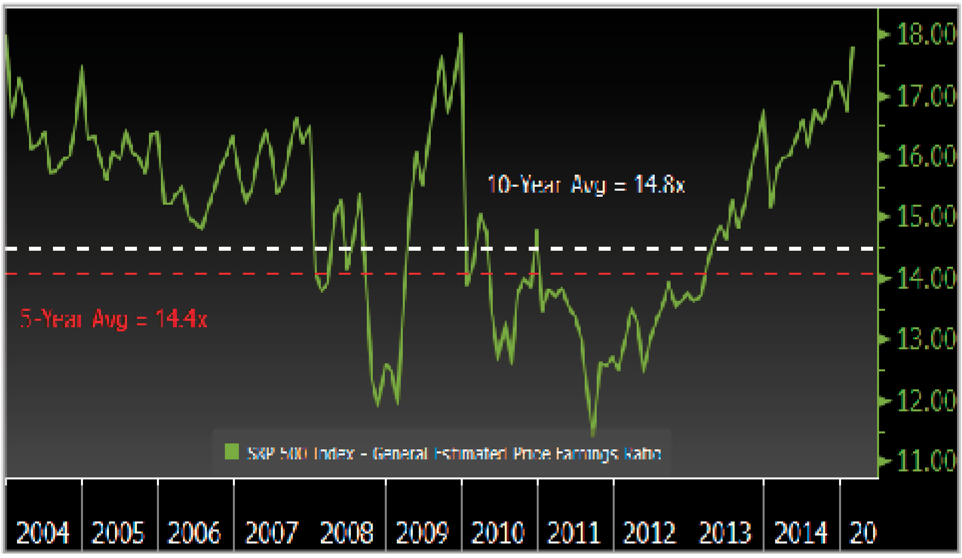
Market participants often shrug o
disappointing results because expe
steadily decreased throughout the
once the companies finally report, r
they're in line with expectations. Fo
earnings were expected to grow ov
the start of 2014, and despite dram
missing the mark at 6.4%, two-third
companies ended up beating their
The chart on the left shows the pro
of earnings estimates over the last f
as well as the expectation for 2015.
earnings expectations have been se
than expected, and as the market c
to rise, valuations were further stret
It's interesting to note, in 2012, earn
expectations for 2013 were within 5
current estimate for 2015. Despite r
missing these projections, the mark
by over 50%. While market appreci
definitely surprised us, the lackluste
growth has been exactly what we e
This has been the weakest economi
on record, and as John Maynard Ke
"There is nothing so disastrous as a
investment policy in an irrational w

S&P 500, Q1, AND Q2 YEAR-OVER-YEAR (YOY) GROWTH FORECASTS



Worse yet, the report's outloo
called for, similar to the previou
lowered expectations. The main
for lowered company guidance
stronger dollar and lower oil pri
trade-weighted dollar is up ove
last June, with oil plunging by c
in that same timeframe. And wi
half of the S&P 500's earnings c
outside the US, a stronger dolla
a viciously competitive environ
multi-nationals. The plunge in c
obviously been a huge drag on
sector, which makes up 12% of
500. In fact, as the chart shows,
year (YoY) growth expectations
Q2 earnings fell from 10% and 1

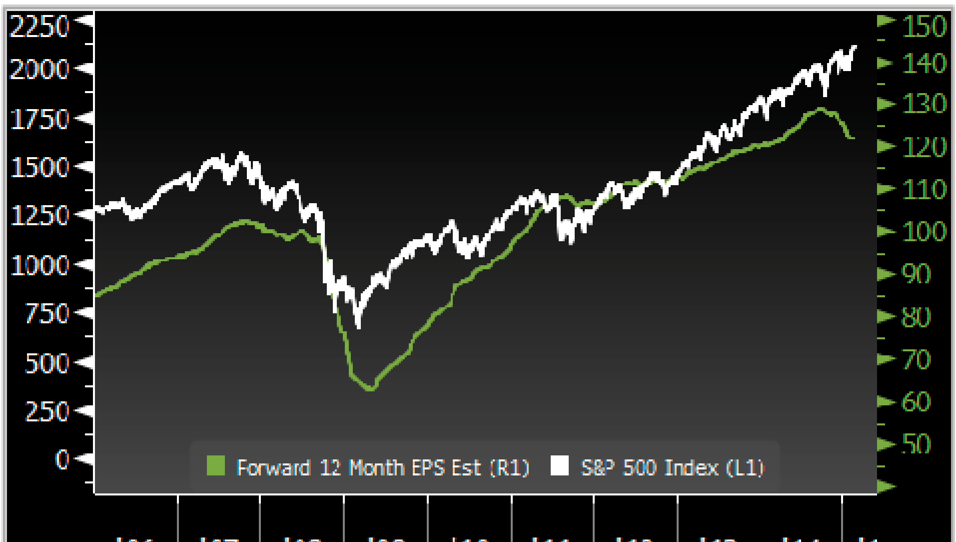
S&P 500 FORWARD PRICE-TO-EARNINGS RATIO



Source: Bloomberg, Evergreen GaveKal

The previously illustrated combo
profit forecasts and rising stock pri
to a significant expansion of the fo
to-earnings multiple (i.e how much
willing to pay for next year's earnin
the past 18 months, we've seen nu
valuation metrics reach all-time hig
making US stocks the second most
in history. Over this time period, th
metric that market bulls routinely h
hats on—because it was only sligh
long-term averages—was the forw
to-earnings ratio. After reviewing t
record of forward earnings estimat
one has to wonder why this metric
much attention. Nonetheless, as th
to the left shows, the current forwa
the S&P 500 is closing in on its 200
and is significantly above its five- a
averages. Today, bulls are left proc
earnings will recover but, as we'll d
below, we have our doubts.

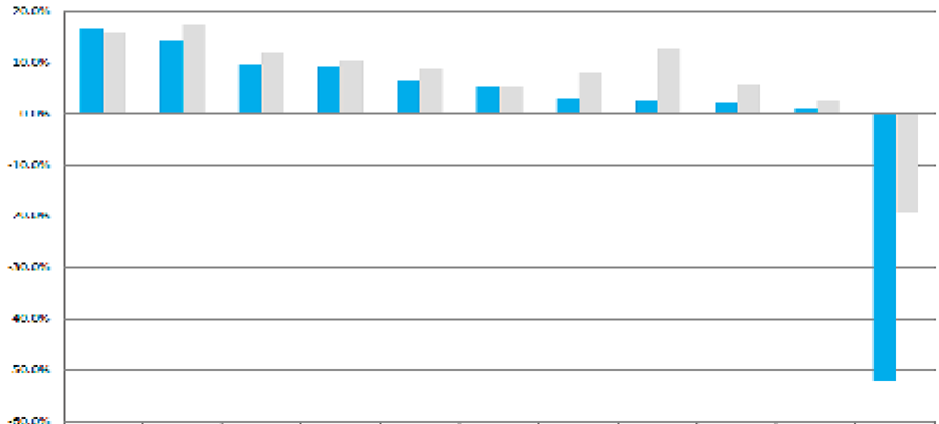
S&P 500 AND FORWARD 12-MONTH EPS ESTIMATE



Historically, there has been a tig
between forward earnings estimat
stock prices. As illustrated to the le
periods of either flat, or falling ear
have corresponded to weakness fo
As we've discussed, we've seen ear
estimates for 2015 plummet, while
prices continue to rally. We'll admi
recovery in profits is possible, but t
that US companies have glided on
reversing in extraordinary fashion.
which are currently at an all-time h
soon see wage pressure, which has
but non-existent in this recovery.
Federal Reserve, which has been fo
historically dovish policy, has alrea
its quantitative easing program an
raise interest rates at some point i
12 months. Doing so will not only

BY JEFF DICKS & JEFF EULBERG

2015 S&P 500 EARNINGS GROWTH EXPECTATIONS

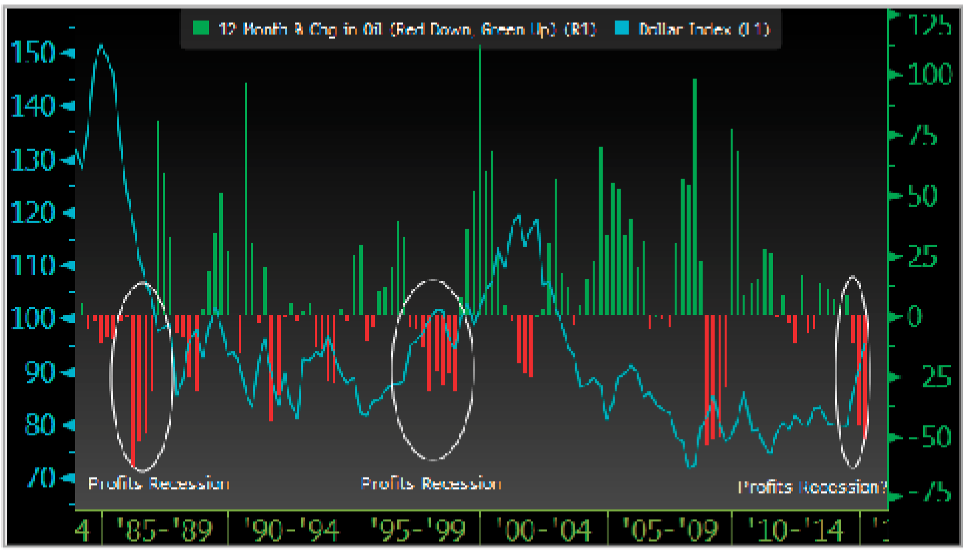


	Financials	Consumer Disc.	Health Care	Info. Technology	Industrials	Telecom Services	S&P 500	Materials	Consumer Staples	Utilities	Energy
Today	16.7%	14.2%	9.5%	9.1%	6.5%	5.2%	2.5%	2.3%	2.1%	1.0%	-51.8%
31-Dec	16.1%	17.4%	12.2%	10.4%	9.0%	5.3%	8.1%	12.5%	5.7%	2.4%	-19.4%

Source: Bloomberg, Evergreen GaveKal

As previously mentioned, a big p
the decline in S&P 500 earnings is r
the drop in oil. Obviously, lower oil
on energy companies' profitability,
sector makes up 12% of the S&P 50
can clearly see from this chart, earn
the energy sector are expected to p
50% in 2015, which has already gro
an expected 20% decline to start th
However, it's important to note tha
with the exception of financials, ha
downgraded over the last few mon
as noted earlier, 2014 only turned o
decent earnings year thanks to the
explosion in telecom and healthcar
consumer-related companies shoul
from lower gas prices, many others
will likely find the fallout from the o
down, a stronger dollar, and other a
pressures, to be more challenging t
expected.

YEAR-OVER-YEAR CHANGE IN OIL AND USD INDEX



Source: Bloomberg, Evergreen GaveKal

Overall, we think there is a po
we will see an earnings recessio
(Refresher: an earnings recessio
straight falling quarters of corp
profits during a period where G
The chart on the left shows the
times we've seen a profits reces
well as the 12-month change in
clear that a large drop in oil has
during both instances. Addition
can see an overlay of the US do
The strength in the greenback t
the mid-90s contributed to this
For the profit recession in the 8
cause was a Fed tightening cycl
though, we are facing a large d
a stronger dollar, *and* a Fed pre
tighten. Basically, it's shaping u
perfect storm for further downg
2015 earnings. This is clearly no
priced in given the climb in bot
prices and valuation metrics.

IMPORTANT DISCLOSURES

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