KAYINVESTMENTS

SEC REGISTERED INVESTMENT ADVISOR

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When the wind blows, the grass bends.

~ Analects of Confucius

[Note: I will be away until July 23 but checking voicemail and email].

The first half of the year has been interesting. One thing we know without doubt is that the markets dance according to whatever tune Fed Chairman Bernanke calls. The suggestion that quantitative easing (QE or "money printing") might end this year sent the bond markets into a freefall starting in May. The wind really blew. The stock market dropped as well but steadied itself in June.

Many of you have called me because of the bond funds. We use them to stabilize the accounts and offset some stock market risk. This has been a rare instance where the bond funds have destabilized the stock funds.

Where Are We Going?

I don't believe the bond market damage will continue at this time. For one thing, Mr Bernanke reassured the financial world on Wednesday that there will be no change to the easy money policy before well into 2014. This was exactly what the markets wanted to hear. For another thing, the jump in rates was largely a panic attack of selling. The economy is not really sufficiently healthy and robust for rates to spike THAT MUCH via lending demand. Finally, a further increase in rates would jeopardize the real estate market (think mortgage rates), the overall economy (think fragile recovery) and the deficit (think debt limit crisis). This is why I think rates will retreat (or at least stabilize). For now the genie is still in the bottle.

I think the stock market will stay on track to a good year but it is breakable. The problem is that the U.S. stock market is standing somewhat alone. There are uncertainties everywhere. From China to Europe to the emerging markets to commodities to precious metals we see weakness. So the question might be whether the U.S. market can lift the other boats or whether it eventually is dragged down.

So why is the U.S. stock market rising? I think part of it is that investors don't see many better options. Part of it also is the abiding belief that, as long as Chairman Ben keeps rates low, things will be OK. The bulls continue to have the upper hand. I don't see a reason to fight it.

What Are We Doing?

We have high quality funds, generally 5 star funds and/or 5 star managers. Beyond that, I am looking for diversification, which has become ever more difficult – given that so many

investment sectors move together any more. For example, our bond positions are diversifiers and we expect them to rebound. They may hold steady when the stocks drop.

We also hold positions in two funds (in the brokerage accounts): 361 Capital Managed Futures and Pension Partners Inflation Rotation fund (AMFQX and ATACX). These funds have appeal because their underlying strategies (pre-dating even the funds themselves) have track records of making steady returns in down markets. So they may not correlate highly with the stock market year to year. For this reason, I consider them to be good diversifiers.

If you would like to discuss your risk/reward orientation or any changes that may be appropriate, please contact me at the below.

Regards,

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