

THE COMPASS

April 2016

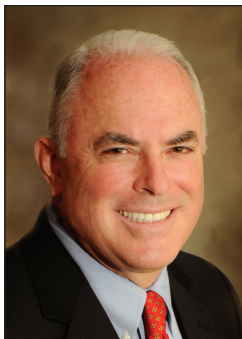
A Quarterly Newsletter of Martin Capital Advisors, LLP

INVESTMENT PERSPECTIVE by Paul Martin, Managing Partner

Wild Ride for Stocks in the First Quarter Finishes About Where It Started

April 26, 2016

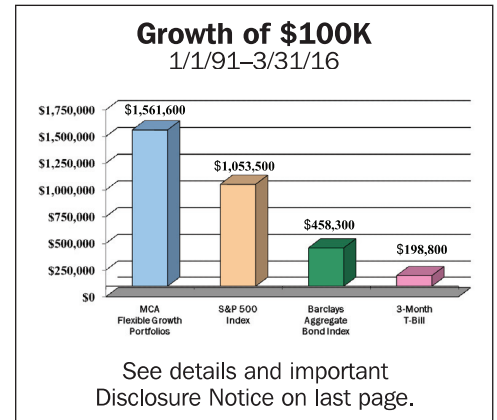
The first quarter opened with relentless selling in the stock market, but managed to recover to about where it started by the end of the quarter. Although slowing economic data from China and falling oil prices were blamed as reasons for the heavy selling at the beginning of the year, I believe that uncertainty about how aggressive the Fed might be in raising rates was the primary catalyst. At the end of my commentary for the previous issue of this newsletter, written on January 25, I said that my best guess was “that data dependency will once again become the watchword for the Fed, in which case the odds are good that the stock market is in the vicinity of a major market bottom.” It turns out that the intraday low for



the S&P 500 had occurred five days earlier on January 20 and was successfully retested two and a half weeks later on February 11. Since then the stock market has recouped its earlier losses as the last half of the quarter

saw a reversal of the Fed’s hawkish rhetoric that had begun last summer. Bonds performed well in the first quarter with a better than 3% total return on the Barclays U.S. Aggregate Bond Index. Gold bounced back from its bear market low with a very strong counter-trend rally from the beginning of the year until early March; however, long-term technical indicators continue to be bearish and point to a resumption, sooner than later, of the down-trend in gold since 2011.

Stock prices have remained resilient into the second quarter, increasing the likelihood that the



lowers seen in January and February did, in fact, signal a major market bottom. Although there are plenty of mixed signals, economic and corporate data are beginning to show signs that there could be a significant improvement in GDP and earnings in the latter half of the year. Despite the recent rally, however, most sentiment indicators are still showing fairly bearish expectations. This suggests that there is plenty of cash on the sidelines that could come into the market when fundamental conditions are eventually perceived to warrant a more positive outlook. Bottom line, the odds continue to favor higher stock prices this year.

COMPARISON OF INVESTMENT RESULTS

January 1, 1991 to March 31, 2016

	Martin Capital Advisors ¹	S&P 500	Wilshire 5000	Barclays Aggregate Bond Index	3 Month T-Bill	Consumer Price Index
Total ²	1461.6%	953.5%	1001.5%	358.3%	98.8%	77.2%
Avg. ³	11.5%	9.8%	10.0%	6.2%	2.8%	2.3%

¹Total performance, net of commissions, fees, and expenses of all Martin Capital Advisors’ Flexible Growth Portfolios.

²Total compounded return, including reinvestment of dividends and interest. ³1991-2016 annualized return.

— See Important Disclosure Notice on last page. —

Real annualized gross domestic product expanded at a rate of 1.4% in the fourth quarter, slowing down from the 2.0% rate recorded in the third quarter. Growth for the year increased 2.4%, which was the same rate as in 2014. Estimates for the first quarter are hovering around 0.5% indicating that the economy continued to decelerate. This weakness along with low inflation has caused the Fed to strike a more dovish tone in 2016, which has helped alleviate uncertainty over the cadence of future rate hikes and has led to a weakening in the U.S. dollar. **(Figure 1)**



Despite the tepid GDP number, the labor market continues to be exceptionally strong. In March, the economy added 215,000 nonfarm jobs, marking the 66th month of consecutive job gains. In the last two years, job growth has averaged 241,000 jobs per month. Despite the growth in jobs last month, the unemployment rate edged up to 5.0% from 4.9% as more workers entered the labor force. The labor participation rate is now 63.0% and has made considerable headway since the historic low of 62.4% that it touched in September. However, the labor participation rate is still well below the pre-recession peak of 66.0%. Wage growth continues to be uneven, rising 0.3% in March after falling 0.1% in February. While wage growth has been lackluster, for the year wages are 2.3% higher than a year ago and have outpaced inflation. **(Figure 2)**

Manufacturing appears to potentially be on the rebound. Over the last two years, manufacturing has been weakened as the dollar has strengthened, global economies have slowed, and low oil prices have hampered the domestic energy economy. However, in March the ISM Manufacturing Index reached 51.8 – the first expansionary reading in the last five months. The ISM Services Index also increased in March to 54.5 after slowing the past four months. It was the first month since July that both ISM Services and Manufacturing were above 50.

As gasoline prices have risen, consumer sentiment has waned. In March the index dipped to 91, which is the lowest level since October. Rising concern about

the economy is manifesting itself in Americans' spending behavior. Consumer spending has only ticked up 0.1 percent each month since December. The negligible increase in spending has been reflected in retail sales, which unexpectedly fell 0.3 percent in March.

The housing market continues to trend upward and is being bolstered by the improving labor market. Housing starts increased 5.2% in February and permits increased 3.2%. While new homes sales were strong, existing home sales fell 7.1%. The strong labor market, pent up demand, and short housing inventories should continue to drive a strong housing market for the foreseeable future, especially as long-term interest rates have fallen again recently.

Inflationary pressures remain weak. Both the CPI and core inflation increased 0.1% in March. For the year, the CPI is only up 0.8% and core inflation is up 2.2%. Although core inflation is above the Fed's target rate of 2%, the Fed has indicated that they are comfortable with slightly higher inflation rather than further rate hikes. **(Figure 3)**

When the Fed announced the rate increase last December, they indicated that rates could be raised four times in 2016. However, over the last few months, the Fed has changed their thinking. As a result, many Economists expect only one rate hike to occur this year. This change in expectations along with heightened fears over the health of the US economy has caused the yields on US Treasuries to fall and the yield curve to flatten. At the beginning of the quarter, the 2-year yield was 1.02% and the 10-year fetched 2.24% for a spread of 122 basis points. By the end of the quarter, the 2-year yield was 0.73% and the 10-year was 1.78%, a spread of only 105 basis points. **(Figure 4)**

Despite the strong labor market, the first quarter was undoubtedly weak. As we move into the second quarter, the more positive reports in March suggest that the economy will likely rebound and won't continue to decelerate as it has the past three quarters.

Figure 1

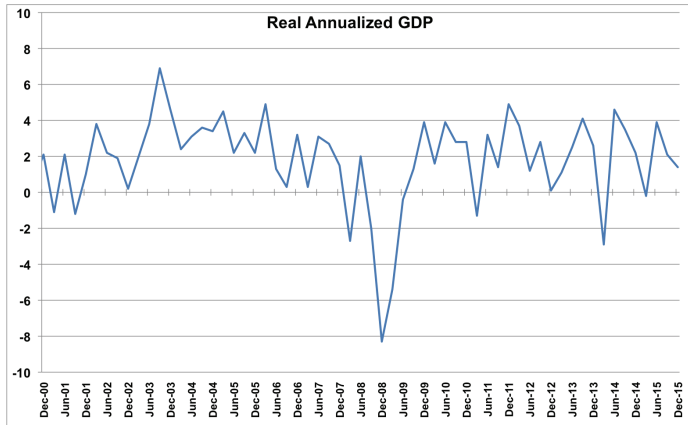


Figure 2

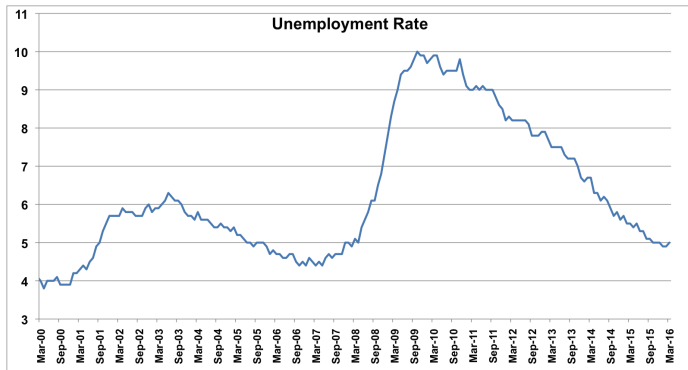


Figure 3

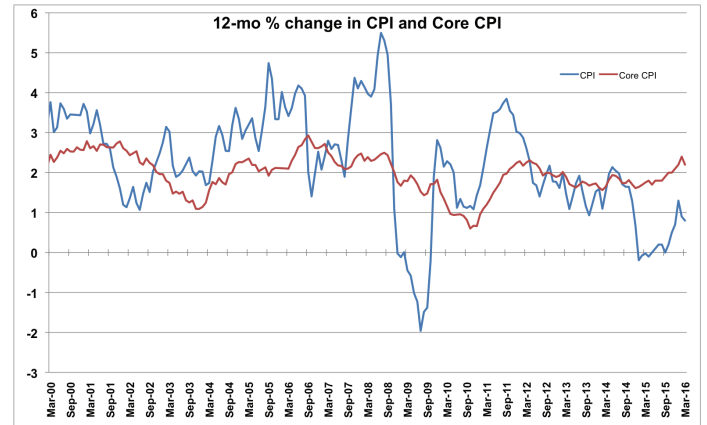
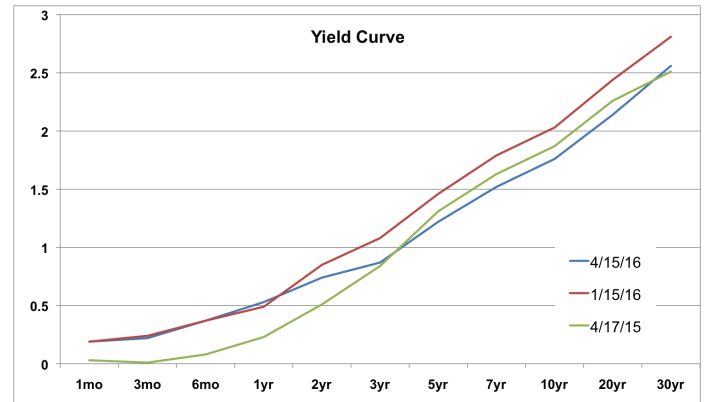
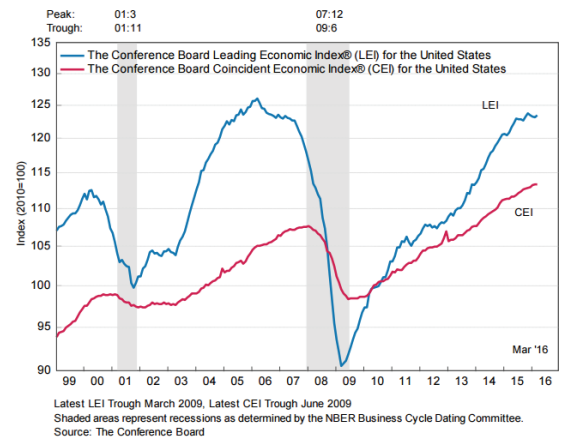


Figure 4



LEADING ECONOMIC INDICATORS

	Current Reading	1-month change	6-month change
Conference Board Leading Economic Index	123.4	+0.2%	+0.8%
S&P 500	2021	+6.1%	+4.0%
Average weekly hours, manufacturing	41.7	unch	unch
Initial Jobless Claims	266.8K	+5.6K	-4.1K
Manufacturers' new orders, capital goods ex. aircraft	140.8B	+0.1%	+0.9%
Manufacturers' new orders, consumer goods and materials	40.0B	+0.8%	-2.4%
ISM New Orders	58.3	+6.8	+8.5
Building Permits	1086K	-38.9%	-1.7%
Spread between 10-yr Treasury Note and Federal Funds Rate	1.53	+0.13	-0.25
Avg. Consumer Expectations for Business Conditions	0.00	+0.30	-0.06
Leading Credit Index (negative readings are positive for the LEI)	123.4	+0.30	+0.80



RELATIVE LONG-TERM PERFORMANCE

January 1, 1991 to March 31, 2016

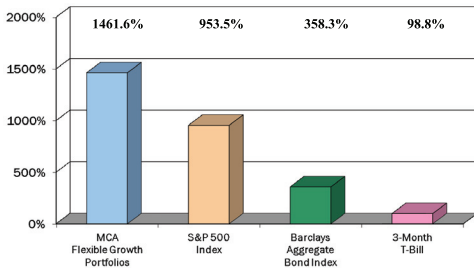


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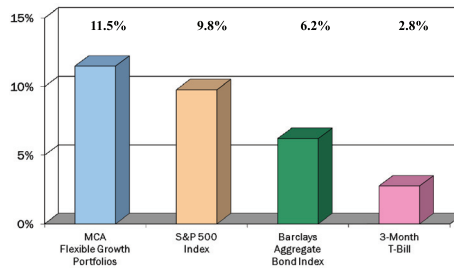
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Martin Capital Advisors, LLP, is a registered investment advisor managing private and institutional investment portfolios.

Total Return



Annualized Return



MCA FLEXIBLE GROWTH PORTFOLIOS TOP 20 STOCKS

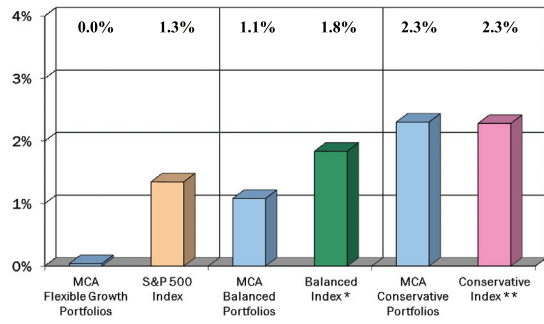
as of March 31, 2016

1 Apple	108.99	6 MasterCard	94.50	11 Texas Instruments	57.42	16 Tiffany	73.38
2 Starbucks	59.70	7 SanDisk	76.08	12 Visa	76.48	17 Diamond Hill Inv. Group	177.36
3 Intuitive Surgical	601.05	8 Charles Schwab	28.02	13 Tractor Supply	90.46	18 Costco Wholesale	157.58
4 Whole Foods Market	31.11	9 Oracle	40.91	14 IPG Photonics	96.08	19 Blackrock	340.57
5 DaVita	73.38	10 Williams-Sonoma	54.74	15 Alphabet	792.90	20 ARM Holdings	43.69

INVESTMENT RESULTS

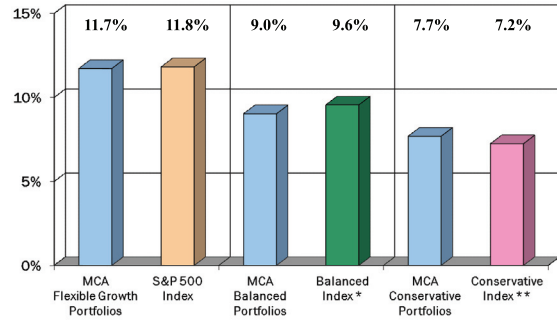
Martin Capital Advisors' Investment Portfolios vs. S&P 500 and Barclays Aggregate Bond Indexes

Year-to-Date Returns as of 03/31/16



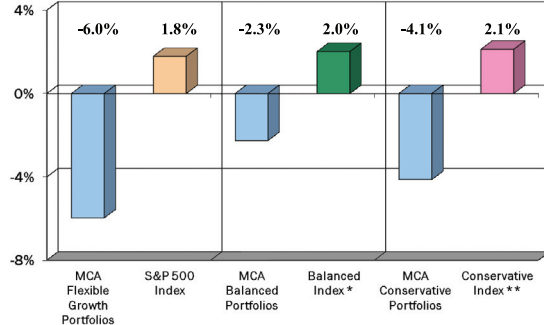
* 75% S&P 500 Index + 25% Barclays US Aggregate Bond Index
** 50% S&P 500 Index + 50% Barclays US Aggregate Bond Index

Three-Year Annualized Returns as of 03/31/16



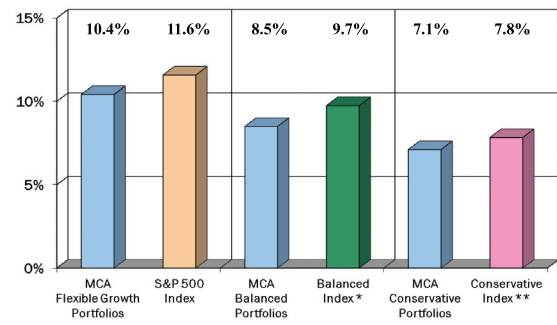
* 75% S&P 500 Index + 25% Barclays US Aggregate Bond Index
** 50% S&P 500 Index + 50% Barclays US Aggregate Bond Index

One-Year Returns as of 03/31/16



* 75% S&P 500 Index + 25% Barclays US Aggregate Bond Index
** 50% S&P 500 Index + 50% Barclays US Aggregate Bond Index

Five-Year Annualized Returns as of 03/31/16



* 75% S&P 500 Index + 25% Barclays US Aggregate Bond Index
** 50% S&P 500 Index + 50% Barclays US Aggregate Bond Index

IMPORTANT DISCLOSURE NOTICE

Past performance does not guarantee future results. Figures include the reinvestment of all dividends received and reflect cash and cash equivalents. Martin Capital Advisors, LLP (MCA) composite returns are net of all fees and expenses. From time to time, composite performance may reflect the use of margin investing and options, as well as material investments in bonds and cash, and volatility may differ from that of the benchmark. As of 3/31/2016, the MCA Flexible Growth/Balanced/Conservative portfolios' returns represent, respectively, 42/8/1 individual portfolios and 69%/27%/2% of all funds under management by MCA. Clients explicitly elect these management styles on their Personal Data Form. The MCA Flexible Growth Portfolios are managed for capital appreciation, and the MCA Balanced and Conservative Portfolios are managed for capital appreciation and income. Independent performance reporting is provided by CGM Investment Management.

MCA claims compliance with the Global Investment Performance Standards (GIPS). The GIPS standards permit non-compliant returns prior to 1/1/2000 to be presented with and linked to compliant returns post 1/1/2000. MCA performance for periods prior to 1/1/1999 is not yet GIPS-compliant, but has been linked to the subsequent GIPS-compliant performance for cumulative periods. MCA has been independently verified for the periods January 1, 1999 to December 31, 2015 by Dabney Investment Consulting Associates, Inc. The verification reports are available upon request. The listed composites contain all fee-paying accounts with an investment strategy as indicated by the composite title. Non-fee paying or nondiscretionary portfolios are excluded from the composites, but are included in the definition of total firm assets. Performance results are expressed in U.S. dollars. To receive a complete list and description of Martin Capital composites and a presentation that adheres to the GIPS standards, contact Robert Godines at (210) 694-2100, ext. 2, or robert@martincapital.com.

ADDITIONAL DISCLOSURE NOTICE

MARTIN CAPITAL ADVISORS, LLP (MCA) is a registered investment advisor based in Austin and San Antonio, Texas, founded in 1989. MCA specializes in managing customized equity and balanced investment portfolios with an all-cap equity strategy to grow capital, as well as balanced strategies to grow capital with less volatility.

MCA claims compliance with the Global Investment Performance Standards (GIPS®).

Returns are shown in U.S. dollars net of fees.

Leverage (margin) is not normally used except temporarily or at client request. Derivatives such as options may be used occasionally as a risk reduction measure.

The GIPS standards allow firms to link non-GIPS-compliant performance to their compliant history provided that no non-compliant performance is shown for periods beginning on or after 1 January 2000. Performance for periods prior to 1/1/1999 is not GIPS-compliant, but has been linked to the subsequent GIPS-compliant performance for cumulative periods.

Martin Capital Advisors, LLP has been independently verified for the periods January 1, 1999 to December 31, 2015 by Dabney Investment Consulting Associates, Inc. The verification reports are available upon request. Verification assesses whether (1) the firm has complied with all the composite construction requirements of the GIPS standards on a firm-wide basis and (2) the firm's policies and procedures are designed to calculate and present performance in compliance with the GIPS standards. Verification does not ensure the accuracy of any specific composite presentation.

MCA Flexible Growth Portfolios are invested in publically traded companies with the goal of maximizing long-term returns. These portfolios are classified as an all-cap core strategy, but predominately invest in large and mid-cap stocks, blending the characteristics of both growth and value investing. Each portfolio typically invests in 30 to 40 stocks that are rigorously selected to meet our core philosophy of investing in companies with an enduring competitive advantage that offer growth at a reasonable price. These portfolios are for investors who are willing to accept significant short-term volatility in the pursuit of superior long-term returns. The benchmark for this composite is the S&P 500 Index, which is an index of the 500 leading companies in the U.S. and is designed to reflect the risk and return characteristics of the large-cap U.S. equities universe.

MCA Balanced Portfolios are invested in equities and fixed income securities with a target asset allocation of 75% equities and 25% fixed income. These portfolios are for investors with a long-term investment horizon who seek to grow capital, but want to do so with less short-term volatility than the MCA Flexible Growth Portfolios. The equity investments in the portfolios are classified as an all-cap core strategy and are managed in the same way as the MCA Flexible Growth Portfolios. Fixed income investments include both individual and ETF fixed income securities. The benchmark for this composite is a blend of 75% S&P 500 Index and 25% Barclays U.S. Aggregate Bond Index, rebalanced monthly. The S&P 500 is an index of the 500 leading companies in the U.S. and is designed to reflect the risk and return characteristics of the large-cap U.S. equities universe. The Barclays U.S. Aggregate Bond index is made up of the Barclays U.S. Government/Corporate Bond Index, Mortgage-Back Securities Index, and Asset-Backed Securities Index, and only includes securities that are investment grade quality or better, have at least one year to maturity, and have an outstanding par value of at least \$100 million.

MCA Conservative Portfolios are invested in equities and fixed income securities with a target asset allocation of 50% equities and 50% fixed income. These portfolios are for investors who prefer to significantly reduce short-term volatility in their investments rather than maximize long-term returns. The equity investments in the portfolios are classified as an all-cap core strategy and are managed in the same way as the MCA Flexible Growth Portfolios. Fixed income investments include both individual and ETF fixed income securities. The benchmark for this composite is a blend of 50% S&P 500 Index and 50% Barclays U.S. Aggregate Bond Index, rebalanced monthly. The S&P 500 is an index of the 500 leading companies in the U.S. and is designed to reflect the risk and return characteristics of the large-cap U.S. equities universe. The Barclays U.S. Aggregate Bond index is made up of the Barclays U.S. Government/Corporate Bond Index, Mortgage-Back Securities Index, and Asset-Backed Securities Index, and only includes securities that are investment grade quality or better, have at least one year to maturity, and have an outstanding par value of at least \$100 million.

To receive a list of composite descriptions of MCA and/or a compliant presentation, contact Robert Godines at (210) 694-2100, ext. 2, or robert@martincapital.com.