Fall 2016

360 Insights

Quarterly Investing and Financial Perspectives

Presidents and Your Portfolio

by **Alex Potts**, President and CEO, Loring Ward

What's Inside

As we approach Election Day on November 8, there will be endless debate, prognostication and media hype. But even before a single vote has been cast, the potential results are already being priced into stocks around the world.

While elections do have real consequences and can certainly impact individual companies, in aggregate they tend to be less important than many of the other factors that drive stock prices.

How much influence will the next president have on the price of Apple's phones and computers, Nike's apparel, Disney's entertainment or Starbucks coffee?

What matters more: who becomes president or whether a company's product is any good?

Every company on the major stock exchanges carries its own risks, profits, losses, management and strategies that actually have a much greater impact on its share price than a presidential election.

It is actually the *uncertainty* of the actions of a future president and Congress that could affect stock prices today.

Let's think for a moment about a large, retail company that we all own within our diversified portfolios and imagine these scenarios…

Uncertainty: Will the president (with Congress) change taxes? **Possible effect:** This could hurt profits if individuals can't afford to buy their products. If taxes decrease, people may spend more money. Or the company could produce something innovative or realize new efficiencies that drive profits despite higher taxes.

Uncertainty: Will the president and Congress make it more expensive for companies to keep profits overseas? **Possible effect:** If yes, this may hurt the price of that company; if no, it may help. But European regulators may go after foreign earnings as well, making offshoring less appealing.

Uncertainty: Will the president increase import tariffs? **Possible effect:** This could hurt if companies can't produce their products as cheaply. However, it could help U.S. manufacturers. If tariffs are unchanged, the company and shareholders stay happy. If tariffs are reduced, the company could become even more profitable.

With each moment of uncertainty, there may be a different effect on the company price. With millions of people buying and selling the stock every day, this information gets processed between the buyers and the sellers and shows up in the current price. However, by the time the uncertainty is known, new buyers and sellers are now worried about the next set of uncertainties!

Many will contend that presidents have very little effect on the long-term prices of goods and products sold.[1] But, advertisers, filmmakers, TV and radio stations are among the winners to date. The Wesleyan Media Project recently estimated that more than $408 million has been spent on political advertising… and that was only through May of 2016!

Did I mention that this information is factored into the price of those companies?

[1] "Alternative Estimates of the Presidential Premium," Sean D. Campbell and Canlin Li, Finance and Economics Discussion Series, Divisions of Research & Statistics and Monetary Affairs, Federal Reserve Board, Washington, D.C.

There Is Always a Reason to Sell…Unless You Want to Achieve Your Goals

by **J. William G. Chettle**, VP, Loring Ward

The problem with good advice is that it tends to be boring, especially when it comes to your portfolio.

This is a good thing.

For investors, excitement can be your worst enemy. Excitement generates headlines; it causes people to be greedy or fearful; it drives volatility and speculation — all resulting in too many people compromising their financial futures.

If you've been invested over the past 15+ years, you've certainly lived through more than your share of excitement. In the period from 2000 to 2015, we experienced two bear markets, the Great Recession, war, terrorism and 11 of the 20 worst days in the stock market since 1950!

Did you stay invested, or did you listen to the headlines? Were you globally diversified, or did you try to guess which stocks or sectors or countries would outperform?

This chart shows how two portfolios did during this "exciting" 15-year period. Both portfolios are owned by couples in retirement making regular withdrawals from their portfolios to sustain their lifestyles. They are both smart and prudent and stayed the course during this tumultuous period. However, the Smiths invested in a portfolio that tries to mimic the S&P 500. On the other hand, the Johnsons invested in a globally-diversified, index-type portfolio that is 65% stocks/35% bonds and includes allocations to small and value stocks in the U.S. and abroad, as well as U.S. REITs and emerging markets.

Both couples start with a $500,000 portfolio and withdraw 5% of the initial value ($25,000 of initial $500,000 starting value) on January 2 each year. This withdrawal is increased 3% each year to help the couples' incomes keep pace with inflation.

Your goals and comfort with risk will determine what portfolio is right for you, but the Johnsons prefer a moderate portfolio since it is right in the middle between a conservative, mostly-bonds portfolio and an aggressive, all-stock portfolio.

As the chart at the right shows, over this time period, the 65/35 asset class portfolio mix of the Johnsons had an annualized rate of return around 5.64%, while the Smiths' S&P 500 returned just 4.06% a year. And the Johnsons' portfolio experienced much less volatility (shown as "Risk" in the chart) as well.

Return & Risk for Moderate and S&P 500 Portfolios

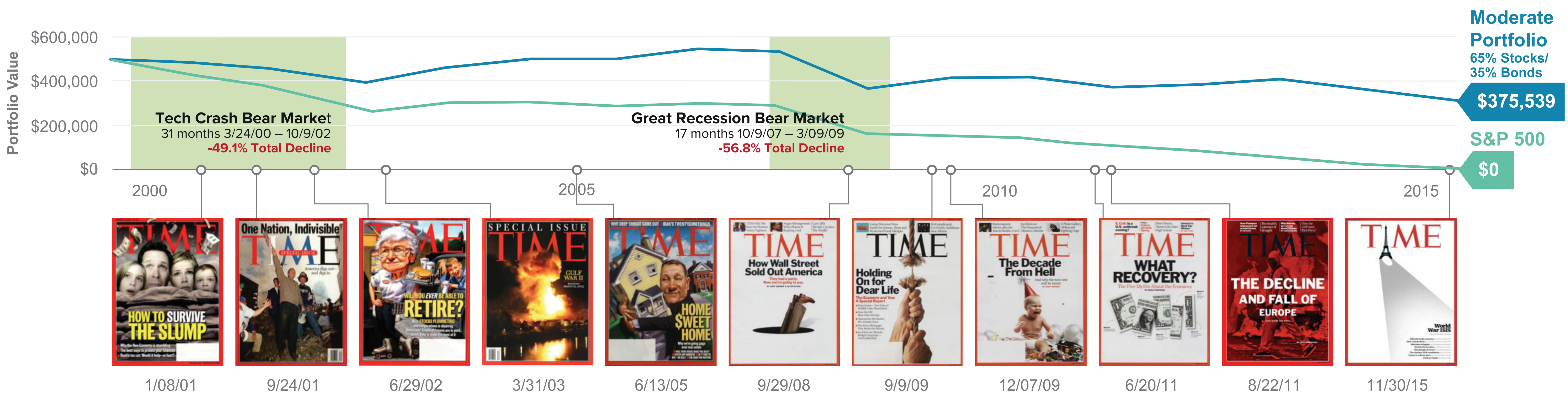
	Johnsons' Moderate Portfolio	Smiths' S&P 500 Portfolio
Return	5.64%	4.06%
Risk (Std. Deviation)	12.95%	18.64%

Lowering volatility is important for investors, especially those making regular withdrawals, because it can keep your money working for you longer. And this is exactly what happened for the Johnsons.

By 2015, they still had $375,539 in their portfolio (and this is after withdrawing $503,922 in income).

Meanwhile, in 2015 the Smiths ran out of money.

It isn't difficult to be a better investor: Diversify globally, don't try to beat the market, don't panic…and save excitement for the non-investment parts of your life.



Source: Morningstar Direct 2016. Hypothetical value of $500000 invested on January 1, 2000 and kept invested through December 31, 2015. Withdraw is 5% of initial hypothetical value ($25,000 of initial $500,000 starting value) taken out at start of each year, growing by 3% per year. Allocation is 100% S&P 500 TR, and 65/35 Mix represented by: 2% Cash & Cash Alternatives (BofAML US Treasury Bill 3 Mon TR USD), 16% US Short Investment Grade Bonds (BofAML US Corp&Govt 1-3 Yr TR USD), 17% Global Short Bonds (Citi WGBI 1-5 Yr Hdg USD), 15% US Stocks (Russell 3000 TR USD), 12% US Large Value Stocks (Russell 1000 Value TR USD), 8% US Small Neutral Stocks (Russell 2000 TR USD), 14% International Large Value Stocks (MSCI World Ex USA Value NR USD), 7% International Small Neutral Stocks (Dimensional International Small Cap Index (2000), MSCI World Ex USA Small Cap NR USD (2001-2015)), 5% Emerging Markets Stocks (MSCI EM NR USD), 4% US REITs (DJ US Select REIT TR USD). The performance data quoted represents past performance. Past performance does not guarantee future results. Indexes are unmanaged baskets of securities that are not available for direct investment by investors. Index performance does not reflect the expenses associated with the management of an actual portfolio. Stock investing involves risk including loss of principal. Securities of small companies are often less liquid than those of large companies. As a result, small company stocks may fluctuate relatively more in price. International and emerging market investing involves special risks such as currency fluctuation and political instability, and may not be suitable for all investors. Bonds (fixed income) are subject to market and interest rate risk if sold prior to maturity. Bond values will decline as interest rate rises, issuer's creditworthiness declines, and are subject to availability and changes in price. REIT investments are subject to changes in economic conditions and real estate values, and credit and interest rate risks.

Invest for the Long Term

by **Payel Farasat**, M.Sc.FA,
Chief Investment Officer, Loring Ward

This is the last article of a four-part series to help you understand our investment approach — and why it matters to you.

Long-term perspective, discipline and patience are the most important ingredients of portfolio success. But emotional, short-term behaviors like panic selling at lows and elated buying at highs can have detrimental long-term consequences, including dramatic portfolio underperformance.

Consider the daily returns of the Dow Jones Industrial Average (DJIA) from 1991 to 2015. A $1,000 investment over that period would grow, assuming dividend reinvestment, to $12,016. But if you were out of the market on the 10 best days, your $1,000 investment would have grown to just $6,141. This illustrates the value of staying in the markets for the long run rather than jumping in and out of the market.

Another important element of a long-term plan involves rebalancing your portfolio periodically to keep it allocated to your desired mix of stocks, bonds and other factors of return such as small and value stocks.

Imagine investing in a simple "60/40" portfolio 30 years ago: 60% invested in the broad U.S. stock market and 40% in short-term corporate and government bonds. Now, let's examine three different approaches to rebalancing and see how well this portfolio does in each case.

The table below shows the return and risk (as measured by standard deviation of returns) of the stock and bond markets in which we are investing.

Market Conditions for Hypothetical 60/40 Portfolio

Market	Index	Return	Risk
Stocks	Russell 3000 Core Index	9.00%	17.35%
Bonds	BofAML 1-3 Yr Corp/Govt Index	5.00%	1.72%

Case 1: No Rebalancing

This approach would have generated an average annual return of 7.8%, but with a fairly high risk of 12.3%. When you don't rebalance, your portfolio becomes "stock heavy" because over longer horizons stocks tend to grow more than bonds. Over our hypothetical 30-year period, the allocation to stocks drifted to 85% of the portfolio at their highest point. Of course, at a higher stock percentage, you will be in a different (higher) risk profile, and you'll be exposed to more volatility.

Case 2: Monthly Rebalancing

If we assume a 1% transaction cost for rebalancing back to target each month, this portfolio returned 7.7%. However, the risk of this monthly-rebalanced portfolio was cut significantly — from 12.3% down to 10.4%.

Case 3: Quarterly Threshold Rebalancing

If we rebalance the portfolio back to 60/40 each quarter, taking action only when the mix is outside a pre-determined threshold — say, more than +/-4% — we see our return move up to 7.9% and our risk decline to 10.4%. The advantage of this approach is that transaction costs are cut by an estimated 66%.

Rebalancing in and of itself does not provide enhanced returns. The real benefit of rebalancing is keeping you in your chosen risk profile. If your portfolio drifts to a higher stock exposure than you intended, a sharp, temporary market drop may cause unexpected losses in your portfolio. Young investors may be able to wait for the temporary market correction to recover, but those closer to or in retirement may not.

Sticking with your plan can help you stay invested in a variety of market environments. Your Advisor can work closely with you to help you stay focused on the long term and help you achieve your goals.

Indexes are unmanaged baskets of securities in which investors cannot directly invest; they do not reflect the payment of advisory fees or other expenses associated with specific investments or the management of an actual portfolio.