Mardi Gras/February 2015

Dear Clients and Friends:

Laissez les Bons Temps Rouler! Let the good times roll. Many of you may not know that I am a member of a Mardi Gras krewe in New Orleans. Let me rephrase that; I am a member of the Krewe of Endymion, the largest Mardi Gras krewe in New Orleans and I assume the world. Endymion is almost 50 years old and parades on Valentine's Day this year. It is hard to put into words how awesome the experience is of parading during Mardi Gras. Endymion parades with over 2500 members through the streets of mid city New Orleans and then the entire parade rolls into the Superdome for our Extravaganza with nearly 20,000 people. It is truly an extravaganza and this year our headliner is country superstar Luke Bryan, following the theme of our headliner last year who was Carrie Underwood. I could only handle something like this once per year, but I look forward to it all year. Here is a [little video] I took a couple of years ago to give you an idea. Mardi Gras is a season of excess, but more importantly it is a time to forget about what else is going on in the world and in life and just enjoy the moment. That will be welcome for me this year, because for advisors like me who preach diversification in portfolios, last year and even the year before were not a time where the good times were rolling. In fact, I may step out and say that 2014 was harder for some advisors than 2008 during the market crash. Allow me to elaborate.

It was the best of times; it was the worst of times

Be honest, and maybe I am shooting myself in the foot here, but how many times in the past year or so have you read or seen the news talking about the record highs in the market and wondered why your portfolio wasn't rocketing to the stars? The last 2 years have been the best of times without a doubt for US large cap stocks. The S&P 500 was up over 30% in 2013 and almost 13% last year. That makes 6 consecutive up years with very little volatility. Problem is that most investors (and advisors) do not want and should not want to only own US large cap stocks. Investors diversify and own small cap stocks, bonds, international stocks, commodities, international bonds, real estate etc. We have been preached to about the values of diversification in portfolios. Heck, it even won a

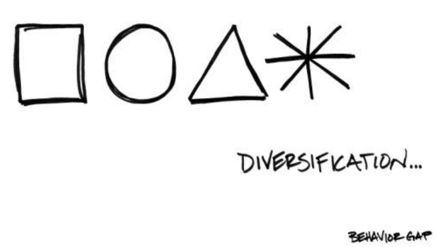
Nobel Prize. In my last newsletter we discussed the perils of making constant changes in portfolios. So in years like last year and the one before that, investors are not quite seeing the "record highs" the pundits on CNBC keep talking about. It is a scenario that is making everyone sit back and reevaluate their strategies. How many people will change and jump ship to invest in last year's winner. Where would you rather be? Adding to something that has gone up over 40% in 2 years or adding to an investment that is down or breakeven.

In investing, what is comfortable is rarely profitable
-Rob Arnott-Chairman of Research Affiliates & manager of PIMCO All Asset Strategies

For a little context, last year the GS Commodities Index was down -17.01% and -9.5% the year before, MSCI International EAFE Index was down -4.9% last year, MSCI Emerging Markets down -2.67% and Barclays Aggregate US Bonds were up 5.97%, but down just over -2% the year before. Additionally, even though the S&P 500 did so well last year, if you separate growth and value stocks in the index, growth stocks outperformed value stocks by nearly 50%. Meaning the market rose for stocks in anticipation of potential future growth and did not do as well for stocks that are statistically cheap. So, you see how the past couple of years could be one that has investors thinking that diversification is a hindrance to good investment performance. Those same investors who might now just want "market returns" are quick to forget that an investment in the S&P 500 in 2000 would take 13 years to get back to even.

The only investors who shouldn't diversify are those who are right 100% of the time
-Sir John Templeton

I am still a big believer in active management. Just like all cycles, the cycle of index investing trouncing active management may soon end. I continue see value in hiring managers with a strong track record of success and allowing them to work to grow capital and more important to work to not impair capital. Keep in mind that losing -30% you need a 43% gain to get back to even. Our diversification comes from choosing good managers, but also ones who are unique to each other. A normal portfolio is not one where all funds go up and



down at the same time. We prefer managers with an unconstrained approach to investing and the flexibility to invest in various asset classes and countries based on their view of the opportunity set.

"I'm not interested in minimum risk. I want long term gains without risk."

To substantially beat an index, a fund has to be very different from that index and because of that, funds will have periods of drastic underperformance. Unfortunately some investors' feel that they need to beat the index every year and is an unrealistic expectation. Often, those are the same investors who are not willing to lose more than 10% in a down year. You can't have the good without the bad.

Very much like [Men's Synchronized Swimming], long term investing success requires patience and diligence. Success does not happen quickly. Like any real sport (not men's synchronized swimming), it all comes down to the basics like blocking and tackling. One of those basics is the time value of money and the power of compound interest. What if I was to offer you an option; $1 million now or one penny today and then double that amount each day for a one month? Would you rather have the million or the doubling pennies? The vast majority of people choose the $1 million, which is the incorrect answer. In reality on day 10 the doubling pennies get you $5.12, day 15 it is $163, day 20 it is $5,242, but then on day 28 you get to $1,342,177 and over $5 million on day 30. Einstein said that compound interest is the most powerful force in the universe. It is those basic tenets like compound interest, diversification and asset allocation that will have a great chance of achieving your long term goals even with some short term frustrations.

As I look to my ride through the city of New Orleans throwing beads, blinking necklaces, footballs and many other trinkets to people yelling "throw me something mister", I can't help to think of a parallel to our markets. Mardi Gras season of excess ends on Fat Tuesday which is of course followed by Ash Wednesday and the start of Lent. The season of Lent is more solemn where we give up certain luxuries and repent our sins. Is the season of excess with US equity markets nearing its Lenten season or are the good times going to continue to roll? Time will only tell. In the meantime, sit back and enjoy a piece of King Cake and trust your long term strategy.