Lifetime Financial Advisors, Inc.

LFA Newsletter

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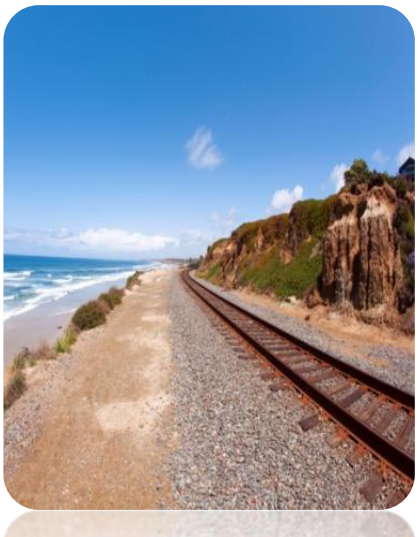

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Eight years ago, the world suffered a huge economic setback caused by the subprime mortgage debacle and subsequent full-blown credit crisis. This was NOT just another ebb and flow of the business tightening-growth cycle.

For a discussion of the important and distinguishing elements of credit crises compared to the more typical economic contraction-expansion sequences, we look to a prophetic book written by economists Carmen Reinhart and Kenneth Rogoff. Entitled *This Time is Different: Eight Centuries of Financial Folly*, it was published in 2009, just after the economic collapse. The book correctly warned that the subprime mortgage situation would emerge as a full-scale credit disaster, not merely a cyclical business slowdown. Having collected and analyzed data going back more than 800 years, the authors provocatively demonstrated that credit-crisis collapses are far different, and the recoveries far more prolonged, than the corresponding events of normal business cycles.

At an average annual growth rate of 2.1%, the U.S. recovery has indeed been slow, but remarkable in some ways. The unemployment rate, for example, was below 5% in pre-crisis 2008, increased to 10% in late 2009, and has since returned to the sub-5% level.

On the following page we summarize the turbulent year that was 2016 and our response to it. Later in this newsletter we offer our thoughts on some potential challenges that may crop up in 2017. Our concluding section reveals some of the measures we take to manage your portfolio.

The global economy remains unpredictable and ever-changing, but throughout the ups and downs we remain cognizant of the fact that you have charged us with the responsibility for watching, guarding, and overseeing your investments. We take this responsibility very seriously, and are grateful every day for the trust, confidence, and reliance you have placed in us.

Very Sincerely,

Your LFA Team

2016 – Surprise Happened…Again and Again…

…and Persistence was Rewarded

Confidence in the Eurozone has continued to be undermined by political risks, the rise of nationalism, and the European Union's (EU's) struggle to deal with Brexit. These threats to the stability and prosperity of the region tend to overshadow other important questions, such as the future of Greece, the EU's immigration crisis, and difficulties in its banking sector.

The fate of Japan is what European economies are trying to avoid. GDP growth in Japan was a dismal 0.5% in 2016 as the economy continued to be constricted by an aging workforce and tight immigration controls.

Other geopolitical events—a coup d'état in Turkey, the ongoing civil war in Syria, heightened uncertainty related to the U.S. presidential election—created turmoil and anxiety in financial markets during the seasons of 2016.

Winter: In January, the Dow Jones Industrial Average got off to the worst-ever start of any year. Stock prices fell 15%, oil prices collapsed; the Chinese economy slowed dramatically and threatened to take the rest of the world down with it.

As is typical and expected when there are market disturbances and increased volatility, the number of calls from anxious clients increased. Our reason for being is to help you remain purposefully committed to your investment goals, and accepting that the perturbations in the market are generally short-lived. We responded to your calls during the first quarter turbulence by urging patience and continued focus on a long time horizon.

Spring: Better data arrived and investors felt some relief as the Fed announced that it would follow a slow and measured path to higher interest rates.

Summer: The United Kingdom surprised the world by voting to leave the European Union. Fallout from this "Brexit" vote threatened global growth.

Fall: Surprise continued as Donald J. Trump won the U.S. presidential election. Simultaneously, the year ended with one of the worst routs for bonds but the best performance for the Dow Jones Industrial Index since 2013.

All told, investors had a bumpy, gut-wrenching ride in 2016. Many were fearful, but investors who remained focused and committed to their goals, who resisted the temptation to "panic sell" during the downturns, were rewarded as the global economy improved during the latter part of the year.

The Dow Jones Industrial Average is comprised of 30 stocks that are major factors in their industries and widely held by individuals and institutional investors.

Looking Forward – Uncertainty Continues

President Trump has proclaimed himself to be “The Great Disrupter”, an agent of change. If he is intent on upending the status quo, then there will inevitably be disturbances—in the social, political, economic, and business realms. What the effects of these disruptions might be is anybody's guess, but we should prepare ourselves for a bumpy ride until we find out.

Volatility is something we have to live with if we want any chance of returns higher than those offered by "risk free" investments. The one consolation is that volatility is the friend of the long-term professional investor. The active managers with whom we align ourselves embrace volatility and take advantage of the opportunities it creates.

We are watching a broadly expensive market; the third most expensive market ever. A recent New York Times article reported, “In early January 2017, the Standard & Poor’s 500-stock index traded at about 26 times the earnings that the constituent companies reported in the previous year…One reason that investors are willing to pay so much is that they see even less value in other assets.”

Why is the domestic stock market so buoyant today? The markets rallied with the election of Donald Trump, believing that the new administration will implement more business-friendly policies. The hope is that tax cuts, less regulation, and fiscal stimulus policies that target infrastructure spending and favorable corporate tax reform, if employed correctly, may provide room for more earnings growth in the market and may support wage growth.

What could go wrong? When imprudently applied, stimulus can create inflation and resultantly higher interest rates. The Fed has announced that it may increase rates two or even three times in 2017. Slow and gradual growth in interest rates is unlikely to upset our economy, but rapid inflation, geopolitical turmoil or a trade war could force the Fed to act more aggressively. This has the potential to derail economic growth, which in turn has the potential to shake the stock and bond markets. The markets absorb and factor in that which can be known with any degree of certainty, but markets do not like surprises.

In addition to the unknowns inherent in the new presidential administration, we can see further potential challenges. The U.S. dollar remains very strong, which puts a drag on our exports, negatively impacting corporate profits and the market. A strong dollar could also reduce employment opportunities in the export sector.

Next, there are several events in Europe which may have significant impacts on the global markets. National elections in several European countries, most notably France and Germany, could lead to more volatility, and European bank debt is back on everyone’s radar. Italian and Greek debt, both sovereign and corporate, is being sold by everyone except the European Central Bank. Once the ECB begins to unwind these bond purchases, debt pressures will escalate further. The terms “ITALEXIT” and “GREXIT” are being used with increasing frequency by pundits.

Inflation is still another possible impediment to growth. It has been edging upward with November’s 3.5% which represented the highest inflation rate in more than two years.

Fasten your seat belts!

The Standard & Poor’s 500 Index is a capitalization weighted index of 500 stocks designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries. The S&P 500 is an unmanaged index which cannot be invested into directly.

"Systematic investing will pay off ultimately, regardless of when it is begun, provided that it is adhered to conscientiously and courageously under all market conditions."

Benjamin Graham, the Father of Fundamental Investing

The Power of Financial Planning

Whatever happens this year, one prediction won't disappoint: we can be certain of more uncertainty. Given the list of possible roadblocks and the even longer list of unknowns that may be thrown at us this year, it is obvious that there are many factors we cannot control.

To the greatest extent possible, we attempt to add multiple layers of preservation to your portfolio in a cautious, prudent and disciplined manner. We maximize diversification through the use of many types of investments. We have faith in the strength of our conviction that the very best place to achieve wealth over the long run is by owning stock of companies we believe are of high quality, well-managed businesses. We carefully select and align ourselves with active managers who are consistent and reliable in ferreting out the companies in which to invest.

We attempt to dampen volatility through prudent portfolio construction, proper allocation of various investments, and risk management. We add still more layers of preservation by not timing the market or by making big bets in particular sectors.

Although our most fundamental tenet revolves around the belief that successful investing covers a long span of time, we do also recognize that you may have short-term financial needs as well. The power of financial planning lies in working closely with you to develop a comprehensive, personalized allocation strategy to align your short-term and long-term financial obligations and goals with dedicated assets for dedicated time periods. This cannot be implemented by any "robo-planner" or off-the-shelf software kit.

Beyond helping you work towards positive long-term returns to meet your long-term goals, the other result we seek is for you to have the confidence that your financial game plan is solid. In the face of glaring headlines and market volatility, we cannot stress enough the importance of focusing on the big picture.

We are grateful for your trust and the partnership we have created working together over the many years. As always, please contact us if you have any questions or concerns, and best wishes to you and your loved ones.