

RBF Weekly Market Commentary

July 28, 2014

The Markets

Anchors aweigh! Put thoughts of the Frank Sinatra and Gene Kelly movie aside. If the Naval Academy fight song is playing in your head, tune it out. The anchors being raised here are setting adrift perceptions that government bonds are always low risk investments.

Behavioral finance – a field of study that looks at behavioral and cognitive psychology in tandem with conventional economics and finance to explain why investors do what they do – tells us investors have been known to make decisions based on faulty reasoning. In some cases, they tend to classify new information based on experience or knowledge.

For instance, people who adhere to the idea U.S. government bonds are low-risk investments might be inclined to take in stride the news that geopolitical tensions pushed bond yields lower during the past two weeks. Who cares that yields are at a low for the year? Government bonds are not risky investments, right?

Not necessarily. While it's true that U.S. Treasury bonds are backed by the full faith and credit of the U.S. government, they are still subject to the unpredictable changes in the markets. One thing to remember is interest rates and bond prices interact like children on a seesaw. When interest rates go down, bond prices go up. When interest rates go up, bond prices go down. Bond prices generally have been going up since the early 1980s and rates are currently at very low levels. As economies recover and rates start to rise again, bond prices are likely to fall and could have a negative effect on the value of portfolios holding government bonds, particularly those with longer durations.

Bond yields have stayed low during recent years largely because of Federal Reserve monetary policy. President of the Federal Reserve Bank of St. Louis James Bullard recently said there is a mismatch between our macroeconomic goals and the stance of monetary policy. While this mismatch is not currently causing problems for the economy, it may in the future. This week, Fed officials are expected to discuss when and how to begin lifting rates from near zero – a level they've been at since 2008.

Data as of 7/25/14	1-Week	Y-T-D	1-Year	3-Year	5-Year	10-Year
Standard & Poor's 500 (Domestic Stocks)	0.0%	7.0%	17.0%	13.9%	15.0%	6.2%
10-year Treasury Note (Yield Only)	2.5	NA	2.6	3.0	3.7	4.5
Gold (per ounce)	-0.9	7.8	-2.4	-7.1	6.3	12.7
Bloomberg Commodity Index	0.0	2.8	1.2	-7.7	0.9	-1.1
DJ Equity All REIT Total Return Index	-0.7	17.8	10.7	10.9	21.7	9.9

S&P 500, Gold, Bloomberg Commodity Index returns exclude reinvested dividends (gold does not pay a dividend) and the three-, five-, and 10-year returns are annualized; the DJ Equity All REIT Total Return Index does include reinvested dividends and the three-, five-, and 10-year returns are annualized; and the 10-year Treasury Note is simply the yield at the close of the day on each of the historical time periods.

Sources: Yahoo! Finance, Barron's, djindexes.com, London Bullion Market Association.

Past performance is no guarantee of future results. Indices are unmanaged and cannot be invested into directly. N/A means not applicable.

‘VIDEO GAMER’ MAY SOON JOIN ASTRONAUT, ATHLETE, AND SUPER HERO on children’s lists of what they want to be when they grow up. Those who reach the top of the e-sport may do well financially since video game competitions can be quite lucrative.

Okay, first, let’s tackle the concept of e-sports. If you’re one of those people who have a hard time thinking of chess or poker as sports, the idea of video games as sports will probably throw you for a loop. However, last week ESPN.com featured The International – the fourth annual world championships of the popular video game ‘Defense of the Ancient 2’ (Dota 2). The event, which was held in KeyArena in Seattle, sold out. In addition, more than 300,000 people watched the event on a popular video game streaming website.

Total prize money for the tournament was \$10.9 million, a record for video game competitions and all the more remarkable because fans raised much of the prize money. That’s a big step up from the first championship. It was held in 2011 in Cologne, Germany and the teams competed for a grand prize of \$1 million.

The League of Legends championship, another big gaming competition, is coming up in October. Two teams will compete in Sangam Stadium in Seoul, South Korea for bragging rights, the Summoner’s Cup, and \$1 million in prize money. *USA Today* reported last year’s championship “was watched by more people than the NBA Finals, World Series, and BCS (Bowl Championship Series) National Championship [college football].” If that seems like a stunning statistic, consider this: 67 million people play League of Legends every month.

According to *PCWorld.com*, “Playing PC (personal computer) games has become a bona fide career option and right now business is booming... A confluence of events occurred at just the right time in 2010 to reinvigorate the PC’s strong legacy of hardcore competitive gaming. Most significantly, the PC’s return as professional gaming’s platform of choice is tied to the economic rise of Asia along with huge missed opportunities by console game manufacturers.”

Weekly Focus – Think About It

“The best time to plant a tree was 20 years ago. The second best time is now.”

--*Chinese Proverb*

Best regards,

Tony Kalinowski

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* Government bonds and Treasury Bills are guaranteed by the U.S. government as to the timely payment of principal and interest and, if held to maturity, offer a fixed rate of return and fixed principal value. However, the value of fund shares is not guaranteed and will fluctuate.

*Corporate bonds are considered higher risk than government bonds but normally offer a higher yield and are subject to market, interest rate and credit risk as well as additional risks based on the quality of issuer coupon rate, price, yield, maturity, and redemption features.

* The Standard & Poor's 500 (S&P 500) is an unmanaged group of securities considered to be representative of the stock market in general. You cannot invest directly in this index.

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* The 10-year Treasury Note represents debt owed by the United States Treasury to the public. Since the U.S. Government is seen as a risk-free borrower, investors use the 10-year Treasury Note as a benchmark for the long-term bond market.

* Gold represents the afternoon gold price as reported by the London Bullion Market Association. The gold price is set twice daily by the London Gold Fixing Company at 10:30 and 15:00 and is expressed in U.S. dollars per fine troy ounce.

* The Bloomberg Commodity Index is designed to be a highly liquid and diversified benchmark for the commodity futures market. The Index is composed of futures contracts on 19 physical commodities and was launched on July 14, 1998.

* The DJ Equity All REIT Total Return Index measures the total return performance of the equity subcategory of the Real Estate Investment Trust (REIT) industry as calculated by Dow Jones.

* Yahoo! Finance is the source for any reference to the performance of an index between two specific periods.

* Opinions expressed are subject to change without notice and are not intended as investment advice or to predict future performance.

* Economic forecasts set forth may not develop as predicted and there can be no guarantee that strategies promoted will be successful.

* Past performance does not guarantee future results. Investing involves risk, including loss of principal.

* You cannot invest directly in an index.

* Consult your financial professional before making any investment decision.

* Stock investing involves risk including loss of principal.

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