



2017 Q2 MARKET COMMENTARY

Summer Doldrums or another Hot Summer

From wildfires in the West to the FAANG's on fire, so far this summer has been anything but slow. Throw in the latest tweet or clandestine meeting and we have the plot for our next book. While we will leave wildfires and politics to others, the FAANGs are something to talk about. For those of you who were around in the 60s, you may remember the 'Nifty Fifty,' or how about the Internet stocks of the late 90s? Today it's the FAANGs: Facebook, Amazon, Apple, Netflix and Google. Three of these weren't even companies during the last internet bubble, one was a survivor of that same bubble, and the last remade itself from a computer company to the world's largest company after almost going bankrupt earlier in the 90s. These are all names that get a lot of press and by many measurements are great companies. These companies also happen to be some of the biggest companies in the S&P 500, so they attract a lot of money from the 'index' investors. If you remember the discussion last quarter, the larger companies get more of the allocation just based on the size of the company. While it is not uncommon to have a relatively small number of stocks contribute 50% of the overall return, it also is difficult when many of those same stocks come with very high price to earnings ratios (P/E). The FAANGs haven't traded below 36.5 since the beginning of 2015, which makes them difficult to buy if you use any type of valuation component.

It may be that we are starting to see the tide change regarding the active vs. passive argument. Ned Davis Research recently published a piece that pointed to correlations coming down between individual stocks and the S&P 500 index. The lower the number, the easier it is for active managers to outperform their benchmarks. In fact, through the first 6 months of the year, over 50% of active fund managers are beating their benchmarks. Is this the start of a new cycle for the argument of passive or active? As you know, we are always looking for very smart people to help manage a specific piece of your portfolio, and if we can't find someone to do it better than the benchmark, we'll just buy the index.

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Speaking of hot, has anyone been paying attention to Cryptocurrencies? No that wasn't from the remake of The Mummy with Tom Cruise. It also doesn't have anything to do with ancient civilizations. Bitcoin was up 165% for the 1st half of the year, while Ethereum was up nearly 3,500% since the end of 2016. Ok, so what are you supposed to do with that information, since most people have not even heard of these things and those who have, can't explain what they are. The simple explanation is that these are digital currencies, like the dollar or yen, but nothing you can physically hold on to. They are in their infancy, but may be something that fundamentally changes our lives, much like the internet back in the 90s. They are driven by something call Blockchain, which is a decentralized validation process for potentially all forms of trade.

We've been talking about things that would power the next BIG bull market; things like Blockchain, Autonomous driving cars, Artificial Intelligence, major advances in health care and solving horrible diseases. These things are all coming within the next decade and many are bubbling under the surface, such that most people don't realize how close they are to becoming mainstream.

So where are we in the market today? The S&P 500 is up 9.3%, while the Russell Small cap index is up only 5%. Most international markets had a good first half, with the Developed markets up 14.2% and the Emerging markets up 17.2%. The US bond market was up a mere 2.3%, with high yield increasing 4.9% through June. As always, diversification is key to long term success, but that also means that you will never have all your money in the best or worst areas of the market and will get a blended return based on your individual risk tolerance.

As always, we encourage you to call or email if you wish to have a longer discussion surrounding these or any topics – and certainly we look forward to speaking with you. If you have friends or family that you would like to pass this along to, please do.

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