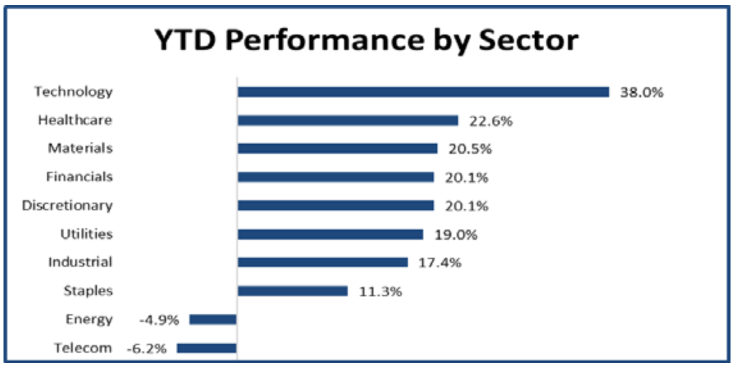
THE PRIVATE CLIENT GROUP
WEALTH MANAGEMENT

~ BE PATIENT AND STAY THE COURSE ~

'Tis the season of gratitude. During the holidays, many of us reflect on the things we are most thankful for…, our families, friends and health are common choices. Additionally, we are thankful for periods of investment growth. 2017 (as least so far) has been an excellent year for investors. Not only have domestic and international markets appreciated nicely, they have done so with minimal volatility – little fluctuation in value.

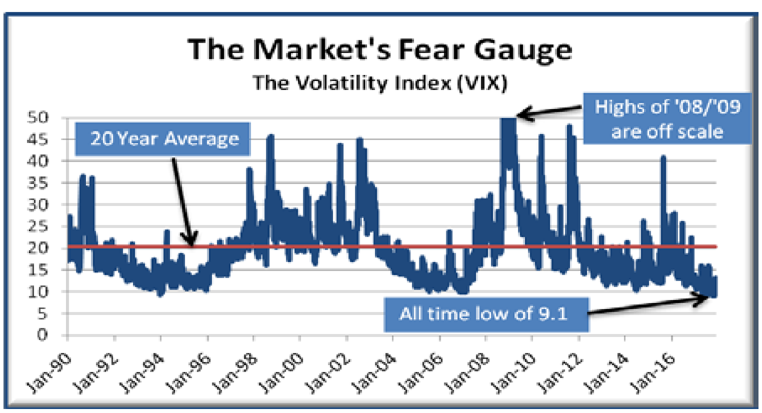
That being said, on a cyclically adjusted basis, investors are now willing to pay a price of $31.58 for each dollar of earnings across companies in the S&P 500 index. Such an outlay is nearly triple the decidedly miserly price of $11.91 at the market's depths 8½ years ago. Aside from the sheer shock value of such numbers, one interesting observation is that nearly half of the stock market's gains have come not from economic or corporate growth, but from nothing other than the willingness of investors to pay far more for stocks. Upon closer scrutiny, it becomes obvious that one sector, technology, has been the major driver behind growth this year.



Data Source: Bloomberg and Goldman Sachs; Sector ETFs

Zooming in even further, the FAANG (Facebook, Amazon, Apple, Netflix and Google) gang of stocks are up 47% on average year-to-date. When one considers that these 5 stocks currently account for almost 10% of the S&P 500 index and over 30% of the Nasdaq 100 index, the potential shortcomings of these market indexes, and the heightened risk when passively investing in these indexes, is accentuated.

What makes this market ascent even more unique is the simultaneous relative absence of market volatility as evidenced by the VIX Index on the graph below. This metric, often dubbed the market's "fear gauge," has declined to an all time historic low - less than half of its 20 year average.



Data Source: Chicago Board Options Exchange

To emphasize this measure of diminished investor concerns, simply take note of the historic daily and weekly volatility versus what we've experienced so far this year.

Daily Volatility (S&P 500)

Range	Number of Days	
	Avg. '88 - '16	2017 (YTD)
+/- 0.5%	129	46
+/- 1.0%	65	8
+/- 1.5%	32	2
+/- 2.0%	17	0
+/- 2.5%	9	0
+/- 3.0%	5	0

Data Source: Morningstar / Summit Calculations

Weekly Volatility (S&P 500)

Range	Number of Weeks	
	Avg. '88 - '16	2017 (YTD)
+/- 1.0%	31	13
+/- 1.5%	22	4
+/- 2.0%	15	0
+/- 3.0%	7	0
+/- 4.0%	4	0
+/- 5.0%	2	0

Data Source: Morningstar / Summit Calculations

This muted volatility is an anomaly that will ultimately prove fleeting. Market behavior, in other words, is likely to "revert" back to historic norms. When it does, and when the market declines by 3% in a day, or 5% in a week, which currently translates to a decline of over 725 points or 1,211 points respectively on the Dow, realize that this is not out of the norm from a percentage standpoint – note that the numbers are simply larger given the growth of the index. In other words, ***when the markets decline by what seem to be large amounts, keep your perspective.*** Typically, markets experience 5% corrections 3 times a year, 10% corrections once a year, and bear markets (20% corrections) once every 3-4 years. This unusually long period of tranquility will be disrupted as more normal cyclical patterns reemerge.

So, how should investors respond to this mix of ingredients? The first step is to understand the fundamentals as they are.

- We are in the later innings of the economic ball game.
- Market volatility will return.
- Annual returns for the next few years are highly unlikely to match those of the past few years.
- We are re-entering an environment where active investing looks far more attractive.

This knowledge helps one form reasonable and realistic expectations. Although important, this is only part of the battle. The next step, provided one has a well-diversified, risk appropriate portfolio, is to do nothing. ***That's right, outside of rebalancing to maintain targets and tightly managing the implementation of a well-constructed portfolio, do nothing.*** This is exceptionally challenging as it runs counter to our hard wired biological instinct of fight or flight. Faced with a threat, our ancestors needed a response to survive. Our portfolios do not. To help, consider the following:

- A broadly diversified portfolio (i.e. containing more than just stocks) is designed to weather the ups and downs of various asset classes. Diversification within the portfolio results in some assets doing better when others are doing poorly. The goal is to use volatility (i.e. declines) in any particular asset category as an opportunity to buy low and sell high. ***Volatility should be embraced as an opportunity, not a weakness.***

- Market timing is basically impossible since it requires not one, but two, low-probability decisions – precisely when to get out and when to get back in. The fact there is no reliable way to determine either point in time leads people playing this game to do so out of emotion, not science. As shown below, the results are dismal.

Data Source: Dalbar, Inc.

In the end, it is simply not possible to time markets, so take the strategy off the table.

Has the current economic recovery been among the longest in history? Has the U.S. stock market recovered dramatically? Are valuations stretched and is stock market volatility uncharacteristically low? Without a doubt, the answer to each question is an emphatic YES. Knowledge of these facts serves to keep us emotionally centered and well-grounded as to likely future developments. These facts are not, however, a call to action. Investment success never has and never will be dependent on "getting in and getting out." Case in point, nearly all of these cautionary observations could have been made, and were made by market pundits, at this time last year. Investors tempted to take action by selling their portfolio or by hoarding cash would have missed out on the healthy gains this year. You may be asking yourself, “Alright, this was just one year, what about the past 20?” Well, the 60/40 portfolio in the above graph performed admirably over the past two decades - a period that included not one but two catastrophic stock market declines. It delivered results far beyond those of the average investor and comparable to the domestic equity market. It also did so with about half of the volatility or "down-side risk" of stocks. ***Such a positive portfolio outcome was not born out of herculean portfolio actions or well-timed bets, but because none were attempted.*** Simply stated, a well-diversified portfolio works for those with patience. The investment markets are prewired to deliver return, not necessarily every time, but definitely over time. Patience is necessary; stay the course.

Thank you for your trust and confidence in us. Thank you for appreciating the benefits of a long-term working relationship – our clients have been working with us for, on average, well over a decade. Thank you for taking our advice, even when it goes against what may *feel* right. Thank you for being a patient investor, I know it’s not always easy. And thank you for choosing us as your partner on this journey.