PFPG Fee-only Advisors

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Market Gyrations

First-half 2016 market volatility presented us with two real-world stress-tests. The year commenced with the worst annual start in Wall Street history, as major equity markets dropped 10% to 16%, oil prices plunged, and fears of a global recession grew. Then beginning around mid-February, everything changed (though there was no clear catalyst for the turnaround). Oil prices spiked higher, stock markets rallied, and the dollar declined (serving as a tailwind for foreign equity returns).

The rally continued on the back of better economic news in the United States and the Federal Reserve's decision to not raise the federal funds rate. Markets also reacted positively to dovish European Central Bank actions, as well as additional monetary and fiscal stimulus in China.

In June, the relative calm in global stock markets ended abruptly when the United Kingdom surprised investors and central bankers by voting in favor of exiting the European Union. Overnight, stock prices fell and the British pound lost 11% against the U.S. dollar. We saw a flight to "safe haven" investments: gold, Treasury bonds, the Swiss franc, Japanese yen, and the U.S. dollar.

In the week following Britain's historic vote, global equity markets rose despite still significant uncertainty regarding the economic, political, and financial market implications of Brexit. By June 30, the MSCI All Country World ex U.S. Index was down only 1% while the Morningstar Moderate Target Risk Index, S&P 500 Index, and Barclays U.S. Aggregate Bond Index returns were positive and in the mid-single digits.

The gains in financial markets accelerated in July with the S&P 500 recording an all-time high on July 29 and the FTSE 100 (the UK's blue chip stock index) recovering from its nearly 9% drop on June 24 to produce a 10.3% return year to date in local currency.   Bonds continued their strong performance. Falling interest rates have been driven by economic growth concerns; central banks' ongoing rate policies, including government intervention (buying) in bond markets; and heightened demand for perceived risk-free assets in reaction to uncertainty surrounding Brexit's impact. They have been joined by expectations of imminent rate cuts from the Bank of England, potential additional bond buying by the European Central Bank, and a growing consensus that the Federal Reserve will further delay raising U.S. rates.

The sort of extreme market turmoil that we have witnessed year to date vividly illustrates why we construct diversified investment portfolios for PFPG's clients. It also points out the unpredictability of short-term market movements. Our approach is to carefully examine long-term risk and return potential and build portfolios that balance these considerations and are resilient across a variety of market scenarios.

We fully expect that the period leading up to the November election, coupled with the implementation of Brexit, will provide ripe conditions for additional investment volatility in the second half of 2016. Stay tuned, be patient, don't fret unnecessarily. And please read the next topic for an explanation of why people tend to think things are worse than they really are!

Why everything seems so awful

To put it simply, it's because bad news is constantly bombarding us from so many of our numerous media sources. Consider this perspective from *The Atlantic*'s recent article, "Why News Junkies Are So Glum About Politics, Economics, and Everything Else." In December, Americans named terrorism the nation's most important issue. However, since September 11, 2001, fewer than 100 people have died in jihadist attacks in the US – roughly the same number that die in motor vehicle accidents *every day*. A study cited in the BBC article "Psychology: Why bad news dominates the headlines" concluded that people are wired to be attracted to bad news (negativity bias), and presents an intriguing hypothesis about our belief systems.

Walking the fine line between being a well-informed concerned citizen and turning into Chicken Little is becoming more and more difficult. Media sources are adroit at playing on our fears to keep our attention. Even some local newscasters deliver shock value stories with wide-eyed breathlessness and hyperbolic adjectives so viewers stay on the edges of their seats. Do those of us in Maine really need the details about a terrible car wreck in the Midwest? If it all starts to weigh you down, just choose the news that you can use. And if you can't resist that daily peek at your portfolio, especially when the news is tumultuous, check out Ron Lieber's *New York Times* article "Zen and the Art of 401(k) Maintenance." You might just put all your electronic gadgets aside and have a tall iced tea out on the deck instead.

Report from Chicago

Tom attended the recent Morningstar Investment Conference in Chicago, and you can read some of his observations online by searching for the *Wall Street Journal'*s article "Financial Advisers Emphasize Diversification in Seeking Stability." In case you think investment conferences can't be fun, Tom also met comedian Darrell Hammond.

Have a happy summer,

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