EMERALD ASSET ADVISORS, LLC

Investment Strategists for Successful Families

April 7, 2017

Thank you for reading GreenThought$. It is our privilege to provide you with our insight on current financial market events and our outlook on topics relevant to you.

First Quarter 2017: Investment Market Summary

We are pleased to report that it was another positive quarter in the global equity markets. Despite the legislative setback in the U.S. Congress, which was unable to proceed with the first major initiative of the new administration (the repeal and replacement of the Affordable Care Act), the post-election stock market rally continued unabated. As of 3/31/17, the S&P 500 index (representing large domestic equities) was up 6.07%, and the MSCI EAFE index (representing foreign equities) was up 7.25%. Bonds managed to hold their ground, for the most part, notwithstanding another interest rate increase by the Federal Reserve (and more on the horizon). Barclays U.S. Aggregate Bond index was up 0.69%, Barclays Global Aggregate ex-U.S. (foreign bonds) was up 2.81. Gold was also up 8.64% (S&P GSCI Gold Spot Price), so were some other commodities. Both aluminum and lead rose 16%, however crude oil declined about 6% (source: Bloomberg).

While the stock market is the one catching most of the attention, the bond market is just as important, and for more thoughts on the state of affairs in that corner of the finance, please read on below.

THE BOND BULL MARKET AND YOUR PORTFOLIO

If you follow the financial news at all, you’re aware of the many articles and strategists advising you that the bull market in bonds is dead and to protect your money, you’d better remove or lessen your bond market exposure. A Google search of bond bull market over will yield results such as:

Is the bond bull market over? - Business Insider 2/1/17
Is the bond bull market over? - Barclays Wealth 1/12/17
R.I.P bond bull market - Bloomberg 12/15/16

Has the bond market, at least in the U.S., been in a bull market for the last 35 years? Absolutely. In the following chart of the U.S. 10 year Treasury yield, that spike you see was on July 1, 1981 when the bond closed the day with a yield of 15.84%. Because prices move inversely to yields, bond prices hit their low on that day. Ever since then, yields have dropped in a saw-tooth pattern as they hit a low of 1.37% on July 5, 2016, as bond prices hit their high.

So why is everyone so sure that the bull market is over, and that yields can’t continue their decline? After all, there have been plenty of periods in the last 35 years when yields rose, only to drop afterwards. Part of the thinking is that in the last few years as central banks around the world lowered interest rates in an effort to jumpstart their economies, yields were pushed down to levels that seemed to make no economic sense, even reaching negative levels! Imagine lending money to the government (which is what you’re doing by buying government bonds) and having to pay THEM (the German or Swiss Treasury) for the privilege? As global economic conditions have rebounded and interest rates have started to normalize, and some signs of inflation beginning to re-appear, the assumption is that bond yields will continue to climb. As a side note, there was a Bloomberg study that looked at economists predictions for where interest rates would end the year, in the period of 2007 through 2015. They only had to be within 50 basis points, or half a percent. That’s the equivalent of the broad side of a barn in the interest rate world. Would it surprise you to know that the accuracy rate was only 17%? Or that in 2008 and 2011, 0% got it right? And in 2014 only 2% got it correctly? Just another reminder that none of us has a crystal ball, and economic prognostication is not an exact science.

At Emerald, mindful of the track record of economists who spend much of their time studying these things and still get it wrong, we try to stay agnostic on the direction of rates. But being agnostic does not mean we’re going to ignore the risks. If a mutual fund is appropriate, we look for a manager that will position the portfolio to take advantage of both rising rates and falling rates. In some instances we may buy individual bonds or build bond ladders using exchange traded funds (ETFs). There are also areas of the bond market that many investors might not normally consider, such as emerging markets debt. There are funds that invest in this space yielding over 5% with a total return for this quarter of over 4%. Municipal bonds are another area that we consider, with some investments paying over 5% of tax free dividends, albeit with the help of leverage. Yet another investment that trades somewhat similarly to bonds are variable rate preferred stocks, and they also look worthy of consideration, at this time.

Our message is that stories about the imminent death of the bond bull market may or may not be true, but we feel there are still opportunities in fixed income. If headlines in the financial press are making you nervous (and there is never a shortage of sensational news, i.e., the financial world is coming to an end and the only solution is to buy a product from the promoter of such news), please give your Emerald advisor a call to discuss.

Regards from the Emerald Team

Disclosure
Green Thought$

The information herein has been obtained from sources believed to be reliable, but Emerald Asset Advisors, LLC ("Emerald") does not warrant its completeness or accuracy. Prices, opinions and estimates reflect Emerald's judgment on the date hereof and are subject to change at any time without notice. Any statements nonfactual in nature constitute current opinions, which are subject to change. Projections are not guaranteed and may vary significantly.

Currency trading may involve significant risks, including market risk, interest rate risk and country risk. Funds or strategies that use leverage or shorting may experience substantial losses. The investment strategy presented is not appropriate for every investor and individual clients should review with their financial advisors the terms and conditions and risk involved with specific products or services. As with all investments, past performance does not guarantee future results.

Clients are urged to compare the custodian's account statements to the advisor's supplemental statements. Please contact us if you do not receive statements from your custodian.

As of August 2016, Schwab no longer sends month-end statements for those accounts where there has been no activity for the preceding month; these accounts will be receiving quarterly statements.

About Emerald

Emerald Asset Advisors, LLC is a Registered Investment Advisor (RIA) founded in 1998. For more information, please visit our website.
Visit our Web site »