Investment Manager Meetings Recap

September 18th, 2014

Investment Managers We Met With
Oppenheimer, Deutsche, Ivy, Transamerica, Blackrock, Franklin Templeton, Alliance Bernstein.

Macro Consensus

The US equity markets are continuing their run on a bull market that is now over five years old. They are also leading performance against other world equity markets; however, recently other areas of the world are catching up.

We have seen a much larger disparity of returns this year. This has not been the "rising tide raises all ships" like we had last year. Who would have guessed that the US Agg Bond Index would be outperforming the Dow Jones so far this year? The S&P 500 is up 8.29%, the Dow up 3.5%, the NASDAQ up 9.23%, and the US Barclays Aggregate Bond Index is up 3.68% (as of 09/17/2014).

Last quarter we were hearing that US equities were getting close to being fairly valued. This quarter we heard more managers saying that US equities are fairly valued, however still inexpensive when compared to US Fixed Income. Everyone we talked to still favors Equities over Fixed Income.

We asked a lot of questions as it relates to Domestic versus International Equities. The story remains the same as last quarter: International continues to show more opportunity than Domestic, however returns have still favored US stocks. Most managers are recommending to add to our International allocations.

There is still talk that we have not seen any kind of a meaningful pull back (10% is average per year) in the equity markets for the last three years. Several managers are cautious on this however feel it would be a buying opportunity and not a concern for a recession. None of the managers could point to what the cause of such a pullback would be.

We believe an energy revolution happening in the US. Consider this: 1) The US became the top global producer of crude oil and natural gas liquids in the 1st quarter of this year (Bloomberg, July 7, 2014) and 2) 84% of the US energy demand was produced domestically in 2013, lessening our reliance on unstable parts of the world (US Energy Information Administrators, June 2, 2014). When you consider this, you can start to understand why the markets were able to easily blow off the geopolitical conflicts of Russia/Ukraine and ISIS.

From our own SIG analysis via Morningstar, the average length of a bull market (going back to the 1930's) has been 108 months. We are now 65 months into this bull market. This suggests that we could have roughly four more years of positive growth. Many managers did agree that they saw no catalyst for a recession or bear market and are optimistic moving forward.

Fixed income was discussed at length as it relates to interest rates. US Fixed Income is facing major headwinds with rising interest rates on the horizon. Everyone still believes you need to own Fixed Income in your portfolio to reduce risk however felt it more important to consider getting income from other sources (Equities, REITs and MLPs).

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Thoughts on Our Portfolio

Similar to most quarters, the recommended changes that the managers had for us – based on their research – were very minor.

Earlier this year we moved money from the US Aggregate Bond Index to Strategic Income funds. This proved to be early. The US Aggregate has outperformed the Strategic Income funds year to date by a few percentage points. This reduced our performance by about 0.50% on average for our portfolios. We still believe this trade to be accurate, even though we were early. Just in the last 30 days, the US Aggregate is down (0.94%) while our Strategic Income funds are up on average 0.88%.

Several of our Themed- or Thesis-based investments have had large outperformances for the year. Janus Global Life Sciences & Technology Fund is up 23.16% YTD and 35.46% over the last 12 months. Our Energy Revolution play in Transamerica MLP & Energy Income is up 18.17% YTD and 28.35% over the last 12 months.

Potential Changes and Updates

The cash position that we have had over the last few months – due to taking profits and not finding immediate value – will be invested within the next few weeks.

We feel it is important to maintain a large position in our core passive holdings. Over the long-term this will keep client fees low and improve our tax efficiency in the portfolio. We will be adding to these positions. While Vanguard is the true low-cost provider, don't be surprised to see some iShare ETFs soon. They are still low cost and have additional tax efficiencies.

Final Thoughts

Nothing has changed to our overall thesis with having an overweight to equities, adding international, watching rates, keeping an allocation to our global themes (Energy, Dividends, Technology). We continue to be optimistic about the economy moving forward, however fully understand that a 10% correction could happen at any time.

We feel confident with our current positions and believe that the increased volatility will be positive for clients that are in the Accumulating Wealth Phase, however it could be a little more problematic for those that are in the Strategic Income Phase.

For those taking income out of their investments, we feel it is important to have a reserve account set up and that account should be funded for at least 10 months right now.

If an investor has some additional cash to invest, they would be wise to develop a consistent monthly contribution. However, if they see a 10% correction they should use that opportunity to add more funds at that time.