July 2016

CALDER INVESTMENT ADVISORS

Quarterly Update

Calder's Comments

What markets have taught us is that when we are sure something is going to happen be prepared for anything to happen. The Brexit vote is a great example. Consensus was that Great Britain would vote to stay in the European Union and the world would continue as is. What did happen is voters in Great Britain surprised the experts by voting to exit the European Union.

For a majority of the second quarter, the markets slowly drifted higher & lower without really getting anywhere. From the beginning of the quarter through June 23, the equity markets gained about 2%, all while exhibiting relatively low volatility. Then came the Brexit vote by Great Britain and stocks dropped more than 5% in two days. Things cooled off over the weekend and the markets stabilized to return 2% for the quarter.

Recent macroeconomic factors will add a level of uncertainty to the markets. Negotiations will begin to facilitate Great Britain's exit from the EU. New trade agreements will need to be ironed out which will probably be a long drawn out process. Governments around the world need to step up and enact successful economic policy initiatives and stop relying on central banks to provide artificial stability. Voters are fed up with lawmakers' inaction to enact improved economic policies. In the United States, the Federal Reserve has been "pushing on a string" with quantitative easing over the last several years and, as a result, all we have is slow economic growth and dangerous market valuations. What we are ending up with is a tangled mess that will be difficult for the central banks and lawmakers to unravel.

In our last quarterly newsletter, we talked about how we are asked all the time to predict the markets. Are we in a bull market? Should I invest in stocks or bonds? Will oil stay this cheap or will it go up? Are interest rates going up this year? What would an act of terrorism do to the market?
Our response was and still is, "We just don't know". But in order to move forward, we do have to our best to stay ahead of the markets. Currently, our market outlook continues to show that returns over the next 5-7 years will likely be below average. This outlook is based on numerous research resources that have provided us with good long term investing advice.

As your portfolio manager, it is most important that each client is properly allocated to an investment allocation that fits their specific risk level and investment strategy. We have partnered with Riskalyze to provide each of our clients' access to new on-line software that will help identify your specific risk preference.

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Fixed Income Investors: Face the Facts

All of the recent chatter about the future direction of interest rates has caused a great deal of angst amongst investors, many of whom are either saving for or spending their way through retirement and are desperately looking for reliable sources of investment income. The facts facing fixed-income investors today are harsh. Rather than ignore them or try to defy them by investing in some freshly minted cure-all, investors should stand and face them.

Fact 1: Interest Rates Are Low. We are most likely in the twilight of a decades-old secular bull market in bonds. Currently, the yield on the 10-year U.S. Treasury stood near 1.5%. After accounting for inflation, the real yield on the 10-year Treasury was about 0.5%. Interest rates are historically low. This is bad news for savers. Low yields portend low future returns; manage your expectations accordingly.

Fact 2: Interest Rates Will One Day (Maybe Soon) Head Higher. Based on current 30-day federal funds futures prices, market participants are betting that the Federal Reserve might raise the federal-funds rate sometime in late 2016. Of course, this is hardly a done deal. There will be plenty of economic data that will emerge in the coming months that could push back the timing of a rate hike. Also, if and when the Fed raises rates, there is no telling 1) the magnitude of the hike, 2) the timing and magnitude of subsequent increases, or 3) whether the rate hike could send the economy into a lurch and cause the Fed to subsequently reverse course. We are in uncharted waters.

Fact 3: Rising Rates Drive Bond Prices Lower. Bond prices have a seesaw relationship with interest rates. As rates go up, prices go down, and vice versa. When rates rise, it will place downward pressure on bond prices. Just how much pressure will chiefly depend on the magnitude of the rate increase and the bond or bond portfolio's duration (holding all else equal, there are other factors to consider, of course).

Facing these facts, some investors have been behaving badly. These circumstances have been a difficult pill to swallow for a growing class of investors that needs reliable sources of income now more than ever. Many investors are attempting to defy the

This graph of interest rates going back to the 1790s.
It is hard to believe, but we currently have the lowest interest rates ever.

Fixed Income Investors: Face the Facts (continued)

odds, reaching for yield and piling on risk in the process.

The Fed's policy has pushed many investors into smaller, more-volatile areas of the market. We've witnessed this in the mushrooming of assets in non-traditional (and much riskier) fixed-income strategies, such as high yield. In all of these cases, investors looking to protect themselves against one type of risk are simply loading up on another one. In the process, many seem to be forgetting the basic case for owning high-quality bonds in an appropriately diversified portfolio. They may serve some of investors' most crucial needs, specifically: capital preservation, diversification, and income generation.

As discussed earlier, the expected returns of a diversified portfolio of high-quality bonds today are, to put it lightly, unappealing. That said, bonds still play an important role in a diversified portfolio. Quality bonds are typically less risky than stocks and can act as a good diversifier of equity risk, even as rates change.

Past performance is no guarantee of future results. Diversification does not eliminate the risk of experiencing investment losses. Government bonds and Treasury bills are guaranteed by the full faith and credit of the United States government as to the timely payment of principal and interest. With corporate bonds an investor is a creditor of the corporation and the bond is subject to default risk. Corporate bonds are not guaranteed. High-yield corporate bonds exhibit significantly more risk of default than investment grade corporate bonds.

With Riskalyze We Can:

Capture Your Risk Number

The first step is to answer a 5-minute questionnaire that covers topics such as portfolio size, top financial goals, and what you're willing to risk for potential gains. Then we'll pinpoint your exact Risk Number to guide our decision-making process.

Align Your Portfolio

After pinpointing your Risk Number, we'll craft a portfolio that aligns with your personal preferences and priorities, allowing you to feel comfortable with your expected outcomes. The resulting proposed portfolio will include projections for the potential gains and losses we should expect over time.

Meet Your Retirement Goals

We will also review your progress toward your financial goals by building a Retirement Map.

When we are finished, you'll fully understand what we can do to increase the probability of success.

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By answering a short questionnaire of about 10 yes or no questions, we can quantify your risk preference and then compare the results of the questionnaire to your current portfolio. Based on changes in your risk profile, we can work with you if changes need to be made to your asset allocation.

If you haven't tried Riskalyze, try it today. We can use this software on money you have invested with us or any other investments you may have. Please contact us to set up a meeting to review your Riskalyze profile and review your total investment portfolio to make sure you are properly positioned. You can access Riskalyze by going to www.calderadvisors.com. At the top of any page on our site, you will see the text, "What's my risk number?" Click on that link and follow the promts.

We consider it a privilege to have you as a client. We want to work with you to navigate the current investment climate, help you make the necessary changes when your family situation changes, provide the proper analysis of your portfolio to ensure it reflects your current situation, ensure that you are on target for your retirement goals, and help you map out your retirement spending. Call us anytime if we can be of assistance.

Other Services from Calder Investment Advisors

- Comprehensive Financial Planning
- Life Insurance Analysis & Consulting
- Traditional, Roth & Rollover IRAs
- Stocks, Bonds, Mutual Funds & ETFs
- Retirement Income Planning
- Corporate Retirement Plans
- College Savings Accounts
- Social Security Timing

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