rebalance IRA

Market Review

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Rebalance IRA's Chief Investment Officer, Mitch Tuchman, along with Sally Brandon, Vice President of Client Services, present the Summer 2017 *Market Review Conference Call*. Listen In!

Summer 2017

Pelotons and portfolios

A peloton is a large group of bicyclists who move together in a pack. If you watch any part of the Tour De France, you see that in the front of the pack a strong rider "pulls," a term for shielding the wind for the rest of the group. The lead rider must work up to 25% harder to help the peloton, while the other riders enjoy drafting behind this lead rider. Once the lead rider becomes exhausted he pulls back into the group, letting the next rider move forward to take a pull. Cyclists call this "pace lining," and they know that by working together they will, over the length of the race, achieve a significantly higher speed than riding alone. Even Lance Armstrong in his heyday could not come close to holding an individual pace that could match the speed produced through the shared work of the peloton.

At **Rebalance IRA**, we sometimes use the concept of a bike peloton to illustrate how asset allocation works.

Asset classes behave similar to the Tour de France cyclists. For a season, one asset class will be out front, outperforming. But over time that asset class tires and drops back, in a sense, to regroup. Another asset class moves forward to pull your portfolio closer to your retirement goal. By maintaining your target exposure to all of your asset classes through disciplined rebalancing, you benefit like a cyclist in the peloton, always enjoying the work of a strong asset class that is leading your portfolio forward and having the power of the group that outperforms any individual.

A shocking fact

Studies have documented that the way a portfolio is designed, how one spreads one's money into different investing buckets or asset classes, accounts for 90% of a portfolio's return over time. This leaves a paltry 10% of performance tied to security selection and market timing. That is why a firm's skill in designing portfolios, coming up with the right investment "mix" of asset classes, is what really separates the professionals from the amateurs.

But when you turn on CNBC or listen to the financial talking heads on AM radio, you don't hear cogent discussion on asset allocation. Rather, what you do hear is so-called "experts" waxing eloquent about their current prognostications on the market's direction or which stock to buy or sell –– market timing and stock selection advice. As the finance media spins like a whirling dervish over these matters, many investors wring their hands wondering if they should buy or sell, get in or get out. And everything focuses on the U.S. stock market. All the while, real returns are being determined by the investor's ability to identify and rebalance asset allocations amongst the best investing assets around the world.

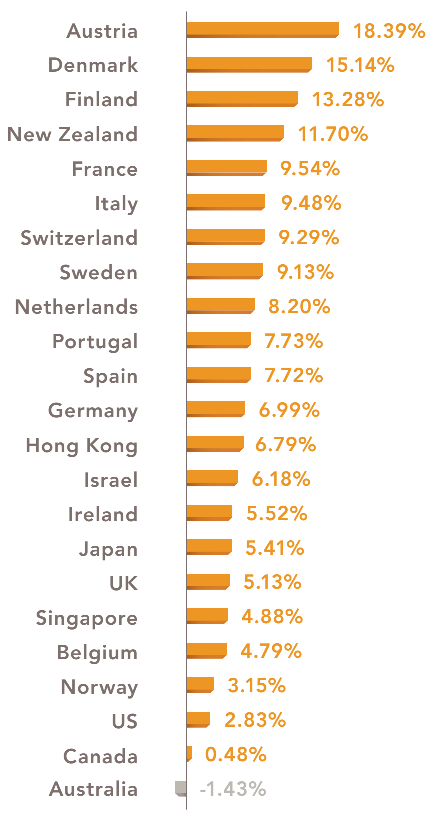
Greece leading the race – up 34%

Just like pace lining in a biking peloton, asset allocation works like clockwork for **Rebalance IRA** clients. From 2000 – 2010, U.S. stocks barely kept pace with inflation. However, for the first few years of this decade (2011-2016), U.S. stocks have led the pack. In 2017, as U.S. valuations have risen, lower cost Foreign Developed and Emerging Market stocks are taking the lead and pulling returns for **Rebalance IRA** portfolios. Even with bonds in the investment mix, Diversified Growth and Balanced Growth, the two most common **Rebalance IRA** portfolios, have grown 8.5% and 7.6% respectively through the second quarter of 2017, according to our backtesting methodology.

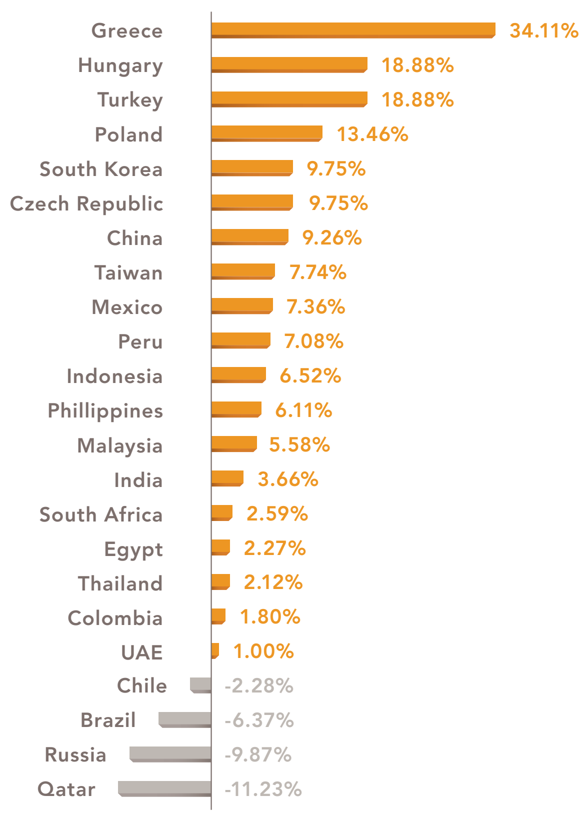
Let's put a finer point on all of the "riders" in the **Rebalance IRA** peloton. In the second quarter, Austria and Denmark recorded the highest country performance in developed markets, while the U.S. was one of the lowest. In emerging markets, Greece, Hungary, and Turkey posted the highest country returns. When Greece was having troubles, it dominated the headlines. Isn't it ironic that when Greece's stock market is up 34% in a single quarter that it is not even a topic of conversation? Wall Street and the media make money stocking fear and greed. And right now Greece serves no purpose to them.

Second Quarter Returns By Country: Developed and Emerging Markets

Ranked Developed Market Returns



Ranked Emerging Market Returns



Hats off to you

By embracing **Rebalance IRA**'s sophisticated asset allocation strategy of diversifying across U.S. and foreign stocks, real estate and several types of bonds, one benefits from lower risk, and over time, better returns. Over the years, through our Firm's disciplined and incremental rebalancing process, we continually have added exposure to international stocks.

For those of you who might have expressed concerns about holding international stocks over the last few years, we applaud you. As the U.S. market led the peloton, you stayed the course with the **Rebalance IRA** investing process, which led to trimming U.S. equities and purchasing more International equities. You now reap your rewards.

The **Rebalance IRA** Investment Committee works with two broad asset classes for the basic building blocks of our client's retirement portfolios: Growth and Income. During the second quarter of 2017, these asset classes performed as follows:

Growth Asset Classes*	Q1 2017 Returns	Q2 2017 Returns	YTD 2017 Returns
U.S. Total Market (VTI)	5.7%	3.1%	8.9%
U.S. Small Cap (IJR)	0.9%	1.4%	2.3%
Emerging Markets (VWO)	11.2%	2.6%	14.1%
Foreign Developed (VEA)	8.0%	6.4%	14.9%
International Small Cap (VSS)	9.3%	5.4%	15.2%
U.S. Real Estate (VNQ)	0.8%	1.7%	2.6%
Foreign Developed/Emerging (VEU)	8.6%	5.6%	14.6%

Income Asset Classes*			
High-Yield Dividend Equities (VYM)	3.2%	1.2%	4.5%
US Corporate Bonds (VCIT)	1.3%	2.3%	3.6%

Income Asset Classes*	Q1 2017 Returns	Q2 2017 Returns	YTD 2017 Returns
High-Yield Corporate Bonds (HYG)	2.3%	2.0%	4.4%
US Preferred Stocks (PFF)	5.1%	2.4%	7.6%
Emerging Market Bonds (EMB)	4.0%	1.8%	5.8%

*Returns displayed representing the major asset classes of **Rebalance IRA** portfolios include dividends as measured using the ETFs shown in parenthesis.

Growth Asset Classes

U.S. Stocks. The total U.S. stock market continued to rise steadily in the second quarter, in part due to better sales figures from improving foreign markets. Most sectors rose, with the exception of energy due to falling oil prices and telecommunications on competition. The so-called "Trump bump" continues to be a factor, raising concerns about what might happen if pro-growth policies stall in Congress. Nevertheless, corporate earnings growth is real and remains positive. A tight labor market has not yet translated into inflation. Large-cap stock valuations, while higher than normal, mostly remain within historic ranges.

Small Cap Stocks. After leading the "peloton" for several years, small cap stocks have taken a breather in 2017 relative to prior years and also relative to larger U.S. stocks. A combination of slowing growth, inflated valuations, a weakness in the U.S. dollar and higher debt loads has caused the lag. When markets are volatile, small cap stocks tend to have bigger swings and we stand prepared to rebalance and add to this asset class at the right time.

Real Estate Stocks. Homebuilders are beginning to feel the pinch of demand as low unemployment, low mortgage rates and low supply converge. In some parts of the country, bidding wars over mid-priced homes are once again commonplace. However, commercial real estate might be overextending itself. Big banks have begun to tighten lending requirements for new projects, for instance.

Large European, Japanese & Asian Stocks. A falling U.S. dollar made foreign stocks relatively more attractive. The greenback declined by 4.9% in the quarter relative to comparable currencies. Part of the previous rise of the dollar was a bet on quick action from the U.S. Congress on a raft of pro-growth policies, an outcome now in doubt. (The dollar remains at the high end of its historical valuation in any case.) However, the rebound in global currencies also is due to a general improvement in economic conditions abroad. Lower price-to-earnings (PE) ratios for foreign developed-country shares also boosted investor demand.

Emerging Market Stocks. A weaker dollar did not necessarily help emerging economies as much. Yet attractive valuations, accommodative monetary policies, and improved political and economic conditions led investors to dip a toe back into the global equity pool. A weaker dollar helps companies holding dollar-denominated debt, and profits abroad are more valuable to U.S. investors as those earnings are converted into dollars, feeding demand for emerging shares.

Income Asset Classes

U.S. Corporate Bonds. The Federal Reserve took a long-anticipated step toward tightening, a strategy so plainly foretold that we instead saw yields drop across the board. A cautious Fed might follow through with another rate hike during the year, but even so, rates remains historically very low and inflation seems in check. A lot depends on the job market, which sits at a multi-decade low yet has failed so far to register the kind of steady wage increase economists expect. Only when wages rise convincingly could inflation reignite.

High Yield Corporate Bonds. Falling oil prices put pressure on junk bonds issued by energy sector firms. Nevertheless, the default rate on high-yield corporate debt is not significant. A slow but steady U.S. expansion, should it continue, suggests that demand for high-yield will remain for the foreseeable future. That might be more of an indicator for cash on the sidelines than quality, yet an oversubscribed market doesn't necessarily imply a crash, either. Volatility has slackened since the 2016 election and oil seems sustainable at current barrel prices, two positive factors for high-yield debt.

Emerging Market Bonds. A stronger China and improved corporate earnings helped buoy investor demand for emerging market debt. A fall in oil prices weakened returns from oil-exporting nations such as Russia and Brazil, but the decline did not turn into a shock and lower oil has helped other emerging nations along the way. Rising U.S. interest rates could draw away investors from the relatively higher risk implied by emerging economies, but the rate trend at home appears to remain slow and steady for now.

High Yield Dividend Equities. Low volatility has helped push growth stocks into high gear, distracting investors from the more "middle lane" returns of dividend stocks. Bear in mind, however, that volatility can return. Low overall interest rates continue to make quality dividend-paying shares a good relative risk and an important component of our portfolios.

Preferred Stocks. Our Firm recently added this asset class to the **Rebalance IRA** Income portfolios. These securities are somewhere between common stocks and bonds and have characteristics similar to each in different ways. Preferred stocks are called "preferred" because of their seniority compared to common stocks when it comes to being paid back during a bankruptcy. Banks and other financial institutions issue most preferred stocks, leading to oversized exposure to that sector. The **Rebalance IRA** Investment Committee continues to like the risk/reward, however, because of the high dividends paid out.

The Rebalance IRA Investment Process

Rebalance IRA portfolios are diversified into thousands of stocks and bonds in the United States and more than 45 foreign countries. Market cycles will continue. Research going back decades, much of it done by members of the **Rebalance IRA** Investment Committee, shows that using those cycles in a prudent manner is the most effective long-term strategy for retirement investing.

By systematically rebalancing our clients' portfolios, we are able to take advantage of market gyrations. Trimming what has gotten rich, and adding to what has soured, enables us to take advantage of market ups and downs, rather than becoming paralyzed by it. **Rebalance IRA** proprietary portfolios rely on multiple ways to deliver returns to our clients that are commensurate with the risk taken.

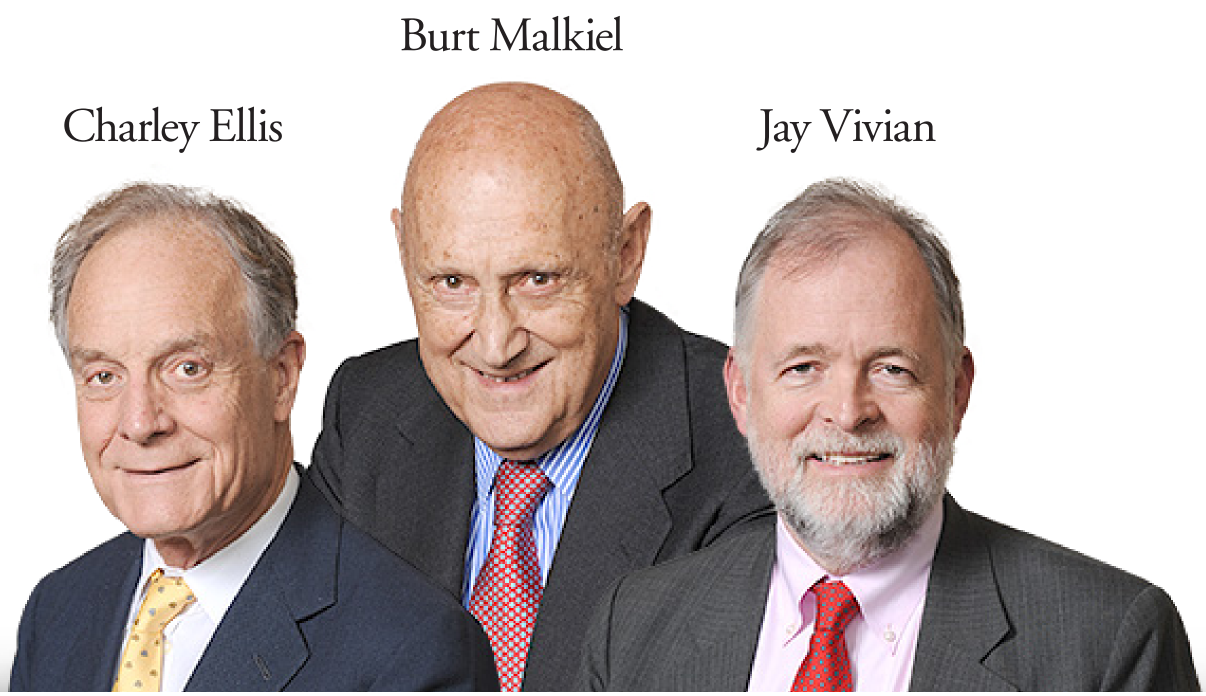
The **Rebalance IRA** Investment Committee has created a vigilant and disciplined rebalancing process that assures that our client portfolios are managed using the best practices of sophisticated endowments and pension funds. We will alert you when we are about to trim winning asset classes, and buy more of the losing asset classes, so that you can better understand how we are managing your money.

Your portfolio is premised on the dialogue that we have with you to understand your situation, risk tolerance and liquidity needs. Our goal: to help you reach your retirement investing goals with the lowest assumed risk possible.

We value your trust and look forward to many years of prudent and profitable investing. And, if at any time you would like to talk, please feel free to send us an email or give us a phone call.

Very truly yours,

Your **Rebalance IRA** Team



The Rebalance IRA Investment Committee

Burton Malkiel, Charles Ellis and Jay Vivian comprise the **Rebalance IRA** Investment Committee. They are renowned for creating and implementing sophisticated investment methods used today by elite pensions and endowments. The Investment Committee actively develops, oversees and sets policies for the portfolios offered to **Rebalance IRA** clients. Their core ideas include diversification across multiple types of assets on a global basis and disciplined portfolio rebalancing. They also advocate techniques for keeping investment fees low.

Professor Malkiel is an emeritus Princeton University economics professor, a former board member of The Vanguard Group, and the author of the investment classic *A Random Walk Down Wall Street*.

Dr. Ellis was for three decades the managing partner of Greenwich Associates, the leading investment advisor to large pools of institutional capital around the world. He was Chairman of the Investment Committee of the famed Yale Endowment, and he has served on the governing boards of The Vanguard Group, Yale, Harvard, NYU Stern, Exeter, the Whitehead Institute, and the Robert Wood Johnson Foundation.

Jay Vivian is the former Managing Director of the IBM Retirement Funds, responsible for over $100 billion in IBM investment funds for more than 400,000 employees worldwide.