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EYE ON THE MARKET

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COMMENTARY ON SPECIFIC MARKET ISSUES AND ACTIONABLE IDEAS TO CONSIDER

LATE SUMMER FUN:
The Boss, Concerts, and Investing

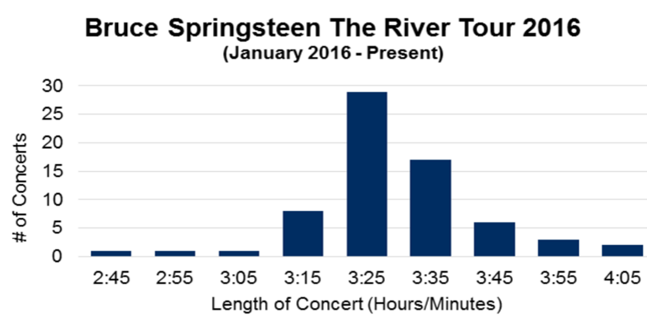
August is typically a slow month for the financial markets as busy families shuffle "back-to-school" preparations with late summer vacations. For music lovers, it is an opportunity to enjoy the closing acts of the season, hoping for an above-average concert experience, just as investors hope for above-average performance in their portfolios.

BORN TO RUN

A colleague and friend of Eye on the Market ("EotM") recently attended a Bruce Springsteen concert. She commented on how engaged Bruce was with the both the audience and the E Street Band, picking and choosing what songs to play to heighten the experience of the show. In a similar manner, an active investor picks and chooses what securities to own and in what quantity, attempting to improve the performance of the portfolio and increase the likelihood of financial success. While both Bruce and the active investor may have the best intentions of heightening their experience, sometimes the audience (and the market), doesn't appreciate it.

Those attending Springsteen's "The River Tour 2016" can expect an average concert length of 3.25 hours with Chart 1 illustrating the distribution of concert times for his tour thus far. As a ticket holder, you'd hope to attend one of the shows on the right-hand side of the distribution, getting more bang for your buck than catching a shorter show on the left-hand side. Does the risk of Springsteen having a short set keep fans away from his concerts? Probably not. With over 40 years of tour history and an enormously loyal fan base, the venues should always be full.

Chart 1



Source: BruceBase and Raymond James

HUNGRY HEART OR I'M ON FIRE

The above serves as a metaphor for how our investor can think about the distribution of returns on an investment. She would certainly want to know what the average return would be, but more importantly, she would want to know if the returns tended to be more positive, more negative, or equally distributed. Her ultimate goal is to maximize her exposure to returns on the far right side of the distribution while avoiding the lowest returns on the left.

When considering active vs. passive management, investors must consider what is more important, avoiding losses or capturing gains. EotM firmly believes that risk mitigation is essential, as it is very hard to recover from a permanent impairment of capital. While there are many merits for taking a passive, index-based approach, there must be a willingness and ability from the investor to accept both winners and losers of the overall market. On the other hand, active managers argue that, through manager expertise, they can avoid securities on the left side of the distribution while capturing those on the right.

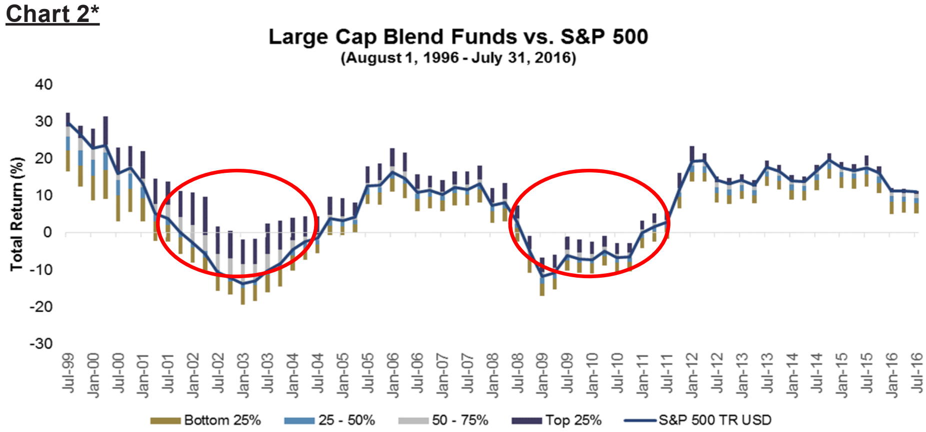
GLORY DAYS

It is hard to argue with the fact that over the last few years, the **average** fund in Morningstar's Large Blend Category (emphasis added) has not performed well relative to the S&P 500 Index. Large Blend is the most widely saturated category, with $1.9T in assets under management as of July 31, 2016. This is approximately $700B more in assets than the next largest category. There are countless explanations as to why active management has underperformed since the end of the financial crisis, including a seven-year bull market, high fees, too many managers chasing the same stocks, and lack of breadth.

EotM looked back over the last 20 years to see if active managers have been able to minimize an investor's exposure to the left side of the distribution. As Chart 2 indicates, during both the bursting of the technology bubble and the financial crisis, many actively managed strategies were able to avoid the worst of the left hand side of the distribution. This is evidenced by areas circled in red, as many active managers were able to generate total returns in excess of the index during these periods. Had the investor taken a passive approach, she would have experienced a sharper decline in her portfolio during these periods. Given that most investors attempt to avoid losses, this could have resulted in her selling at an inopportune time.

Our investor needs to be disciplined in establishing a long-term asset allocation. This involves careful consideration of goals, objectives, and most importantly risk tolerance. The broad market will rise and fall over the course of time. By staying disciplined, she can attempt to capture above-average returns (the right tail of the distribution) and avoid, or at least reduce her exposure to below-average returns (the left tail of the distribution).

Chart 2*



"Our investor needs to be disciplined in establishing a long-term asset allocation. This involves careful consideration of goals, objectives, and most importantly risk tolerance."

*Source: Morningstar Direct and Raymond James. Morningstar's Large Blend Category: consists of portfolios that are fairly representative of the overall U.S. stock market in size, growth rates, and price. Stocks in the top 70% of the capitalization of the U.S. equity market are defined as large cap. The blend style is assigned to portfolios where neither growth nor value characteristics predominate. These portfolios tend to invest across the spectrum of U.S. industries, and owning to their broad exposure, the portfolios' returns are often similar to those of the S&P 500 Index. The S&P 500 Index is a market-capitalization weighted index of 500 stocks, and is generally considered representative of the U.S. stock market.

SIDE NOTE

While Bruce Springsteen has had many memorable tours, he hasn't made the list of the top five highest grossing tours (in terms of revenue). The highest revenue-grossing tour of all time was the U2 360° Tour which generated gross revenues of $736MM. Bruce Springsteen's highest grossing tour was his Wrecking Ball World Tour in 2012 – 2013, which generated gross revenues of $355.6MM.

Investors should carefully consider the investment objectives, risks, charges and expenses of mutual funds and ETFs before investing. The prospectus contains this and other information about mutual funds and ETFs. The prospectus is available by contacting the fund family and should be read carefully before investing.

Diversification and strategic asset allocation do not ensure a profit or protect against a loss. The process of rebalancing may carry tax consequences.

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Past performance does not guarantee future results. There is no assurance these trends will continue.