2015

Is Diversification Dead?

Larry W. Carroll, CFP®

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## 2014 Returns by Asset Classes

<table>
<thead>
<tr>
<th>Asset Class</th>
<th>Return</th>
</tr>
</thead>
<tbody>
<tr>
<td>REITS</td>
<td>28.0%</td>
</tr>
<tr>
<td>S&amp;P 500</td>
<td>13.7%</td>
</tr>
<tr>
<td>10-Year US Treasury</td>
<td>11.0%</td>
</tr>
<tr>
<td>Barclays Agg</td>
<td>5.8%</td>
</tr>
<tr>
<td>US High Yield</td>
<td>3.0%</td>
</tr>
<tr>
<td>Global Allocation</td>
<td>2.0%</td>
</tr>
<tr>
<td>World Bond</td>
<td>1.7%</td>
</tr>
<tr>
<td>Gold</td>
<td>1.0%</td>
</tr>
<tr>
<td>MSCI EM</td>
<td>-2.2%</td>
</tr>
<tr>
<td>Non-US Govt Bonds</td>
<td>-3.0%</td>
</tr>
<tr>
<td>Japanese Equities</td>
<td>-3.0%</td>
</tr>
<tr>
<td>Non-US Equities</td>
<td>-4.0%</td>
</tr>
<tr>
<td>MSCI EAFE</td>
<td>-4.9%</td>
</tr>
<tr>
<td>European Equities</td>
<td>-9.0%</td>
</tr>
<tr>
<td>Commodities</td>
<td>-17.0%</td>
</tr>
</tbody>
</table>

Source: JP Morgan, Bank of America
Cumulative Returns during Lost Decade (12/31/99 – 12/31/09)

Source: JP Morgan, Bank of America
Sector Breakdown 2014

Utilities: 29.0%
Health Care: 25.3%
Technology: 20.1%
Consumer Staples: 16.0%
Financials: 15.2%
S&P 500: 13.7%
Industrials: 9.8%
Consumer Disc.: 9.7%
Materials: 6.9%
Telecom: 3.0%
Energy: -7.8%

Source: JP Morgan
Report Card for 2014

I gave you 6 Investment Themes for 2014

1. Positive for US Stocks
   - S&P 500 13.7%  A+

2. Gold Miners over Gold
   - Gold -2.2%  F
   - Miners – GDX -12.4%  I’m done

Source: Morningstar
Report Card for 2014

3. Municipal Bonds Outperform
   Taxable 5.8%
   Municipals 9.1%

4. Hybrids and Spread product again
   BarCap Agg 6.0%
   Preferred 16.3%
   Convertibles 7.7%
   High Yield 2.0%
   Floating Rate 0.8%
   Emerging Debt 6.7%

5. Europe outperforms the US
   S&P 500 13.69%
   MSCI Europe -8.7% USD
               (+4.1% LCL)

Source: Morningstar, Forbes.com
6) Investors respond to taxes  A
   Municipals
   Stocks
   Anecdotal Evidence

Overall: C+
Business Cycle Stages

Pring Turner's Six Business Cycle Stages

Economic Contraction | Economic Expansion

- Buy Bonds
- Buy Stocks
- Buy Inflation Sensitive
- Sell Bonds
- Sell Stocks
- Sell Inflation Sensitive

Stage 1 | Stage 2 | Stage 3 | Stage 4 | Stage 5 | Stage 6

Source: Pring Turner, January 29, 2014
2015 Predictions

1. Positive for US Stocks (again)
2. Stocks Outperform Bonds
3. Hybrids and Spread product again
4. Europe outperforms the US (currency hedged)
5. Oil stays below $65 per barrel for the entire year
6. Increased Dividends, Increased Buybacks, Increased M&A
The future may look different.
# US Stocks vs. World Stocks

<table>
<thead>
<tr>
<th>Period</th>
<th>S&amp;P 500</th>
<th>MSCI ACWI</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 year</td>
<td>13.7%</td>
<td>4.2%</td>
</tr>
<tr>
<td>3 Year</td>
<td>20.4%</td>
<td>14.1%</td>
</tr>
<tr>
<td>5 Year (2010 - 2014)</td>
<td>15.5%</td>
<td>9.2%</td>
</tr>
<tr>
<td>2001 – 2009</td>
<td>0.0%</td>
<td>2.2%</td>
</tr>
</tbody>
</table>
Energy Revolution – 2014

U.S. Natural Gas Production, 1990-2035

History 2010 Projections

- Shale gas: 49%
- Tight gas: 21%
- Non-associated offshore: 7%
- Coalbed methane: 1%
- Associated with oil: 7%
- Non-associated onshore: 9%
- Alaska: 2%


Source: Fidelity
## Stock Volatility

<table>
<thead>
<tr>
<th>Type of Decline</th>
<th>Average frequency</th>
<th>Average length</th>
<th>Last occurrence</th>
<th>Previous occurrence</th>
</tr>
</thead>
<tbody>
<tr>
<td>-5% or more</td>
<td>About 3 times a year</td>
<td>47 days</td>
<td>December 2014</td>
<td>October 2014</td>
</tr>
<tr>
<td>-10% or more</td>
<td>About once a year</td>
<td>115 days</td>
<td>October 2011</td>
<td>July 2010</td>
</tr>
<tr>
<td>-15% or more</td>
<td>About once every 2 years</td>
<td>216 days</td>
<td>October 2011</td>
<td>March 2009</td>
</tr>
<tr>
<td>-20% or more</td>
<td>About once every 3½ years</td>
<td>338 days</td>
<td>March 2009</td>
<td>October 2002</td>
</tr>
</tbody>
</table>
Stock Volatility

Odds of Experiencing Stock Market Volatility

100%
Annual Returns and Declines

S&P 500 Intra-year Declines vs. Calendar Year Returns

Despite average intra-year drops of 14.2%, annual returns positive in 27 of 35 years*

Source: JP Morgan, December 31, 2014
Stock Volatility...But...
Other Thoughts

1. Russia May Be The Key
2. Risk Takers Should Own Technology and Healthcare
3. Bond Buyers Beware
4. It Gets More Difficult
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- Past performance is no guarantee of future results. Indices are unmanaged and cannot be invested in directly.

- The S&P 500 ® is a market-value-weighted index of 500 stocks that is generally considered representative of the US large cap equity market. The index is unmanaged and not available for direct investment.

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Questions