Welcome to 2016! As a preface to this letter, consider this: if you work with a financial advisor, it’s a good idea to know what they think, believe and stay up at night worrying about. Knowing that your values are aligned with theirs is a great starting point for a relationship of trust.

If you’re wondering about Life and Wealth Planning, our philosophy can be described as pragmatic, long-term optimism. In helping clients achieve their financial goals our advice is predicated on a simple concept: focus on things you can control; don’t focus on things you can’t control. Things that you can control include managing portfolio risk, planning for the future, taxes, diversification and minimizing expenses.

This is not to say you should ignore the things you cannot control. To understand your investments, and to remain calm when the news headlines turn scary, requires a global and long-term perspective. Trends can reverse in an instant, immediately rewarding big-picture thinking, diversification and patience.

FINANCIAL YEAR IN REVIEW

While 2015 was full of political tribulations, investment returns were mainly a reflection of slowing global growth. US Stocks (S&P500) eked out a slight gain of 1.4%. Markets in the rest of the developed world - Europe, the UK and Far East - were
essentially flat, ending the year down by 0.4% in dollar terms. Emerging Markets saw much greater volatility, especially in China and Brazil. As a group Emerging Market stocks fell by more than 14% in US dollar terms.

Hurting relative performance in overseas investments was the strengthening of the US dollar against most major currencies. While a strong dollar is welcome if you are planning to travel overseas, it pushes down the cost of imports while making American manufacturers less competitive. Indeed, US manufacturing momentum decelerated throughout 2015.

Despite weakness in manufacturing and energy, the service sector—which constitutes roughly seven-eighths of our economy—performed strongly, generating substantial improvement in employment. More than 2.6 million jobs were created in 2015, extending a strong run from 2014. The report also showed that 2015 will be the third year in a row with an average of more than 200,000 jobs created per month and that the overall unemployment rate has dropped to the pre-crisis level of 5%.

The collapse in commodity prices was another major theme in 2015. Amazingly, oil has fallen from $115/barrel in June 2014 to $33 today. Anyone who filled up their tank over the holidays was thankful for the return to 2004 gas prices. Increased consumer spending and record auto sales in 2015 suggest the effect of lower gas prices has been positive. Lower energy prices benefit companies as well, in the form of lower costs, which helps profit margins and potentially stock prices. Lower oil prices will also benefit countries dependent on oil imports, especially China, Europe, and Japan. As these economies continue to stagnate, lower energy costs will act as a much-needed stimulus.

But while this is positive for consumer spending, industry and oil importers, not everyone is happy. The balance sheets of oil companies and many oil exporting nations are in disarray. For example, Saudi Arabia, according to the IMF, needs to sell oil at around $106 a barrel to balance its budget. As a result, the Kingdom has so far spent $100 Billion from its rainy day fund. More broadly, the IMF’s Regional Economic Outlook report for the Middle East and Central Asia said “low oil prices will wipe out an estimated $360 billion from the region in 2015 alone.” On a positive note, this economic pressure may have accelerated constructive political change in Venezuela. Maybe other repressive regimes could be swept away in 2016 if they can no longer afford to placate their citizens with hand-outs. Unfortunately, political change outside the Western world is rarely orderly or bloodless so if cheap oil persists watch for possible upheaval in more fragile countries.

The reason oil prices have fallen so much is simply that the world is pumping out more oil than it needs. Case in point, the US has seen an explosion in alternative extraction technologies while China, the world’s biggest commodity importer, is experiencing an economic slowdown. The consequence to investors in 2015 was not only losses in energy stocks (down 21% for the year; worse overseas), but also a large swath of the bond market. According to JP Morgan, higher yielding, more speculative bonds, were down by 4.5% due in part to the struggles of energy companies who can no longer profitably sell their product.

The main Bond Market overall gained a mere 0.55% for the year. This weak performance was largely driven by volatility in interest rates which culminated in the Fed raising rates in December for the first time in more than a decade.

POLITICAL HIGHLIGHTS

Global destabilization seems to have increased in 2015 with turmoil in the Middle East and Russia continuing to have implications in the West. Terrorism touched many shores while ISIS gained ground. Syria depopulated creating a humanitarian refugee crisis the West has not fully begun to address.

Russia continued to make headlines, causing trouble on several continents while turning ever more inward and authoritarian. Winston Churchill once said that Russia is a riddle wrapped in a mystery inside an enigma. Unlike the West, Russia does not possess a democratic heritage and will not even countenance democracy in its backyard (Ukraine). Sadly, it may be generations before Russian’s desire for freedom overcomes their instinct of fear and a new chapter can begin.

The Middle East, however, may today be in the early, painful stages of just such a transformation. The seeds of today’s turmoil were planted by regimes that long promoted religious extremism as a counterbalance to Western influence. This extremism has now spun out of control and today, Syria, Yemen, Libya and parts of Iraq could be considered failed states: lawless and ungoverned. It’s stunning that a quarter of a million people have already died in the Syrian civil war alone.
THE OPTIMISTS VIEW

While it’s easy to become gloomy reviewing this past year’s headlines, there were also shining lights of human achievement to help balance the ledger. (The fact that the market actually stayed relatively resilient despite all the upheaval is one reason to be upbeat.) Here then are some highlights from 2015:

- 195 world nations agreed to the Paris Climate Accord, after getting crucial Chinese and American buy-in
- Landmark elections held in Argentina, Venezuela and Myanmar offer the hope of reversing years of destructive government
- The United State Supreme Court’s recognition of same-sex marriage
- The Eurozone remained stable and intact, having avoided a Greek exit
- Mark Zuckerberg announced plans to give away $45 billion worth of Facebook shares

Let’s also cheer an incredible year in the world of science. In 2015 the New Horizons satellite took close-ups of Pluto form 7,800 miles above its surface in a nearly flawless flyby. On planet earth, two seminal events in the history medicine occurred: a possible treatment was developed that uses the body’s own immune system to defeat cancer and a gene editing technology called CRISPR/Cas9. If these discoveries missed your radar this year, I urge to look them up. It’s an inspirational reminder of the cleverness of human beings.

One of the cleverest human beings living today is Lowell Wood who has more patents to his name than Thomas Edison. He’s come up with solutions for global warming, malaria and football concussions. Learning that a mutant genius inventor like Dr. Wood exists in this world is a revelation and another cause for optimism. His work reminds us that over the arc of human history, our capacity for creation eventually prevails over our capacity for destruction.

THOUGHTS ON THE YEAR AHEAD

The New Year is a popular time for making predictions. Every media outlet and financial institution brings out an expert who will provide their outlook and rationale. We have found that when most experts are in agreement, the majority is often wrong. This year however, there seems to be little agreement. Some experts think that our economy will continue to benefit from falling oil prices and that the rest of the world is finally perking up. Others are more gloomy, pointing out that corporate profits are slowing, China will add to economic uncertainty, and low oil prices will crush emerging economies dependent on exports. Here then goes our prediction: we think all the experts are right and that these cross-winds will negate each other leading to another subdued year in 2016.

What the Federal Reserve Bank does this year will also have a great impact on the year ahead. In 2014, the Fed, judging the economy to be on solid footing, ended its stimulus program. Since then global markets have been virtually flat. In 2016, a lot will depend on how quickly the Fed raises interest rates, as a quicker rate could put a break on growth.

Another reason for slowing US growth is simply the stage of the economic cycle that we are in. In 2009, at the beginning of the current cycle, we could look ahead to economic improvement via government stimulus. Today, we are in the mature part of this cycle - corporate profits are high and unemployment is low. For further growth to materialize, the economy would need a big shot in the arm.

The greatest opportunity for that “shot in the arm” in our opinion is a rebound in growth overseas. But, while a strong dollar should make foreign exporters more competitive, they face significant headwinds. Foreign markets have underperformed the US for 6 straight years. Europe has only recently adopted American-style stimulus, and Japan continues to be stuck in its long-term rut. The emerging world, always a volatile ride, has a long way to go to get back on track. China has already begun to take the painful first steps of shifting from a manufacturing to a services-based economy. Countries like India, Russia, and Brazil will also have to restructure their economies but change will come slowly.

As you might have heard, 2016 is also an election year. In general, presidential election years have little effect on the market. However, with so much polarization in this country, regardless of who is elected the next president, there will be a lot of people unhappy with the result and left thinking the country is heading in the wrong direction. If Hillary Clinton wins, most of her agenda will be stymied by a hostile Congress leading to another four
years of gridlock (which some would consider a good thing). If a Republican wins, they may follow through on promised tax cuts, which could lead to a huge jump in the deficit. Whether this approach leads to corresponding economic growth is an open question. Huge tax cuts under George W. Bush nationally (2003) and Sam Brownback in Kansas (2012) are today considered failures. In our opinion, a simplification of the tax code would a more constructive policy agenda.

According to the US census Millennials (those aged 19 to 35) have now surpassed Baby Boomers as the largest living American generation and in just five years they will make up half the workforce. Millennials are characterized by conservative spending habits, marrying and having children late, renting instead of buying a home, preferring to live in cities and not own cars. If the economy continues to strengthen there’s potential that Millennials could start making big-ticket purchases that contribute to economic growth. On the other hand, their student loan debt, the largest by cohort in history, could keep them from spending, which would be a drag on the economy.

**FOCUSBING ON YOUR PERSONAL ECONOMY**

**What does all this mean to you?** If you are a long term investor continue to focus on things you can control in your personal economy. This does not include trying to time the market or picking individual stocks. Study after study has shown that investors both amateur and professional have the odds against them at beating the market.

Planning and working with your advisor however can help you protect your family, save appropriately, and invest wisely. Here are a few things to keep in mind going into 2016:

- Retirement plan contribution limits to 401k plans and IRAs will stay the same for 2016. Aim to increase your retirement plan contribution percentage by a little bit every year.
- An Important Social Security claiming strategy for couple is going away as of this April. If you or your spouse has reached or will attain full retirement age (FRA) prior to April 30th, you still have time to explore whether the file and suspend claiming strategy is right for you.
- Medicare premiums are going up for retirees with incomes above $85,000 (and $170,000 for couples). You may be able to avoid future increases with prudent income and tax planning.
- If you make too much money to contribute to a Roth IRA, there is a backdoor method that may allow you to do so. Failing to follow the rules however can result in a tax bill so tread carefully.
- The Social Security tax will be levied on your first $118,500 of earned income. Once you hit that threshold, consider re-allocating those dollars into another savings vehicle.
- Income tax brackets go up minimally. Continue to be aware of where you stand and explore options for managing your income and deductions accordingly.
- As always, if you have a goal with a time horizon of less than 3 years, your safest investment bet is cash.

*Thank you for allowing us to share our thoughts. If you have any feedback for us, don’t hesitate to write us at info@lwp.com. Have a great 2016.*