CLEAR CREEK ADVISORS

# BULLS ON PARADE

Market Review **OCTOBER 2017**

The US stock market hit a record low in March of 2009. Since the bottom of the trough, the US stock market has risen for nearly nine years. Lately, US stocks may have found another leg in the already long bull market. There are a couple of reasons supporting stocks.

First, implied volatility indexes are flashing all signals 'go' for US stocks to go higher. An implied volatility index measures how much stock prices are likely to swing in the next year. Based on investor perceptions, implied volatility is the gauge of fear or complacency on Wall Street. Historically, from 2009 to 2015, implied volatility has averaged around twenty at the close of September. Implied volatility now trades around half of its historical average. This sends the signal that there is not much fear out there right now.

Second, the number of stocks that made a new 52-week high and new 52-week low was 205 and 12, respectively, on the last trading day of the previous month. Again, a comparison with the historical record provides helpful perspective. The average number of 52-week new highs is 59 in comparison to 118 new lows on the last trading day of every September from 2013 to 2016. In fact, if the new high and new low data from 2016 is removed from the sample, the average number of new highs drops to 38 and the number of new lows rises to 150. Arguably, this current phase of the already long bull market was already in occurrence during the latter part of 2016.

The bull market in the United States has been underway for many years now. For investors wanting to buy into a newer bull market early, and since 'there is always a bull market somewhere', what other options might there be among developed stock markets? As one of the largest global stock markets, Japan has experienced a sizable run up — and for good reason.

Some analysts estimate that Japanese stocks are currently undervalued. They find that Japanese stocks trade at a 35% price multiple discount to other comparable developed world stocks. Additionally, the Japanese central bank is aggressively buying Japanese stocks in baskets known as exchange traded funds. The Bank of Japan's purchases amount to $53 billion per year and many believe that Japan's central banking agency is now a material owner of Japanese stocks. The saying 'don't fight central bank policy' has taken on a whole new meaning.

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Non-domestic investors of Japan equities are right to be cautious. The Japanese stock market has been in a twenty-year plus secular bear market ever since the Japanese stock market crash of 1990. Between the 1990s and the present, there were many false signals suggesting that the bearish trend of Japanese stocks was about to reverse into a bull market. If a buy-and-hold investor had bought in on one of those signals hoping to catch an early bull market in its infancy, they would have almost certainly lost money after the Japanese stock market threw back its short-lived gains.

One-year gains made by some of the world's largest stock markets have been impressive. US stocks are up roughly 17%; European stocks around 13%; and Japanese stocks now storming into the lead with over a 22% gain. The benchmark Australian and Canadian stock markets, however, have lagged compared to the rest of the developed world. One-year gains on Australian and Canadian stock markets are now approximately 3.5% and 7.5%, respectively. Despite the underperformance of stock markets in these two countries, the interest rates of the two economies are at extreme lows similar to the interest rates in other parts of the developed world. Perhaps the Australian stock market in particular is about to catch the next bull market fever that has already spread into so many other stock markets around the world?

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## Market Movers

Most interest rate sensitive assets sold down on rising interest rates in September. Global interest rates on benchmark government bonds were already low at the beginning of the month. The yields on some countries' debt fell even further to make new annual lows. However, after a short period of time, global interest rates pulled backed higher and finished the month near the year's average yields. The investment team is pleased that global stock markets are performing well and delivering so much wealth creation for our clients. Although, our forecast for global stocks remains 'bullish', we continue to monitor the investment universe for prudent ways to manage our portfolios. The Core Allocation strategies maintain their strong performance relative to the primary benchmarks, Morningstar's World Allocation and Tactical Allocation category averages.

| *Asset Categories* | *Monthly* | *YTD* |
|---|---|---|
| US STOCKS | 4.01% | 10.52% |
| FOREIGN STOCKS | 1.55% | 23.94% |
| US BONDS | 0.0% | 3.31% |
| FOREIGN BONDS | -0.08% | 7.76% |
| HARD ASSETS | 0.01% | 3.23% |
| HYBRIDS | 0.90% | 9.67% |

*DATA USED IS SOURCED FROM MORNINGSTAR®

**US STOCKS** rose higher to lead all category averages. Small Caps (IJR) and Mid-Caps (IJH) reversed prior losses by making gains this month of approximately 6% and 3.5%, respectively. Large Caps (IVV) remain the year's best performers with full year gains above 13% and our portfolios responded nicely. Also, our portfolio tilts towards Mid-Cap Value and Small Cap Blend stocks added to portfolio performance last month.

**FOREIGN STOCKS** performed well in September. Large Developed (VEA) and Small/Mid International (VSS) stocks rose 2.1% and 2.7%, respectively. Emerging Market stocks (VWO) lost some momentum in September and posted a small loss. Still, Emerging Market stocks remain a leading category this year. Small/Mid International stocks, however, have risen by 25% for the year and are closing in on Emerging Market stocks fast. Our sizeable foreign allocation has yielded strong results for our investors.

**US BONDS** of high quality issuers lost market value last month. Riskier bond offerings like High Yield Bonds (JNK) and Bank Loans (BKLN) made some small gains. High Yield Bonds have provided the best annual returns so far. The low-grade category has made a total annual return of 5.9% on contracting risk spreads. The Core Allocation strategies placed an emphasis on High Yield Bonds at the beginning of the year which benefited the returns from our bond allocation.

**FOREIGN BOND** performance was mostly flat in September. Emerging Market Bonds (PCY) have made total returns of over 9% this year. Emerging Market Bonds represent the only foreign bond holding in the Core Allocation strategies this year. The decision to bias Emerging Market Bonds for yield enhancement and diversification reasons has done well for the strategies.

**HARD ASSETS** produced modest losses in September except for Energy. Energy prices have now made three consecutive monthly gains but the energy category remains down 11% for the full year. Our allocation to Master Limited Partnerships (AMJ) as a representative for energy assets in the Core Allocation strategies, however, is down only 6% for the same period.

**HYBRIDS** etched out small gains last month. Convertible Debt (CWB) and Variable Preferred Stock (VRP) have both returned nearly 10% this year. We remain favorable on this category due to the fact that both offer the Core Allocation strategies with enhanced fixed returns and less downside risk.