ABL Money Management Update

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# 4th Quarter 2016 - POPULARITY CAN PROVE COSTLY

Alan B. Lancz & Associates, Inc. started 2016 on a defensive note after a strong year-end rally exposed investors to high valuations. We focused on telecom and utilities to start the year, and after the worst calendar year start for equities in history, these two sectors (along with consumer staples) stood out. As part of our risk management strategy, while both the telecom and utility sectors continued to rise into this summer, partial profit taking was warranted, which then allowed us to focus on the depressed cyclicals that presented the favorable risk-to-reward we seek in an investment.

**The average investor, and many institutions, favored high flyers with Nike, GoPro, Fitbit, First Solar, Shake Shack, Gilead, Starbucks, Under Armor, and Tesla, on many Wall Street buy lists. Many of these investor favorites were bought at new highs as valuations soared into the year end 2015 rally. Those investors that followed the herd in buying these high flyers all showed losses last year, even after another impressive year-end rally in 2016. In fact, the average loss in 2016 of the above most popular companies was over 35%.** One year ago, investors shunned energy, which was the worst performing sector in 2015, and favored healthcare with its defensive characteristics in the midst of continued anemic economic growth. Not surprisingly, healthcare was the only sector to lose money in 2016, and energy's 23.7% advance outpaced every sector for the year. The only other sector garnering over a 20% return was the financials, with their post-election surge in the 4th quarter. We were fortunate to recommend **Bank of Nova Scotia (BNS)** as a dual play with their huge exposure in the energy arena, depressing its shares even more than any other quality candidate in the already depressed financial sector. Both BNS and **International Paper (IP)** advanced well over 40% for us while our other Favorite from last year, **Qualcomm (QCOM)** returned over 35%. Not only were these three favorites down less when the stock market plunged the first six weeks of 2016 but were up substantially last fall, well before the year-end rally. For 2017 Alan B. Lancz and Associates, Inc. expects more volatility in both directions as investors go from a "nothing can go wrong" start of the year to periodic bouts of despair that progress is not as immediate as current buyers anticipate. **It will be another year where following the herd will prove painful with too many investors not understanding the risk being taken with so many of these new high flyers.** The difference between now and our words of warning from the summer of 2007 is that we are still finding solid bargains with strong total return potential, just like our three favorites from last year. Investors just need to focus on accumulating quality companies that are out-of-favor and offer exceptional risk-to-reward due to their low expectations.

Like last year, we go into the new year with low fixed income exposure, having taken profits in the long end and now focusing on select short-to-intermediate term opportunities. We are finding more attractive alternatives in some of the depressed foreign total return vehicles as many of their U.S. counterparts have already advanced beyond our disciplined buy limits during the 4th quarter rally. In addition, we initiated positions in a few inflation hedges while expectations were still low, like Treasury Inflation Protected Securities (TIPs), and even accumulated select precious metal investments as this area declined to new lows post the U.S. presidential election. The 4th quarter bailed out a lot of investors from material losses. We expect the investors that take advantage of the upcoming volatility rather than being played by it will continue to do well into the new year. For our Sound Investing investors primarily in 401(k) plans, we were fortunate enough to have added to positions of Maris & Power Small Cap Fund (MSCFX) before it closed to new investors, as small caps were among the leaders in the post-election rally. It is always rewarding to have purchased before a large move as an investor class becomes a favorite.

# MARKET UPDATE | 4th QUARTER 2016

| EQUITY INDICES | 4TH QUARTER | 1-YR (12/31/16) |
|---|---|---|
| S & P 500 | 4.2% | 12.0% |
| D.J.I.A. | 9.3% | 16.5% |
| NASDAQ | 2.8% | 8.9% |
| Russell 2000 | 9.8% | 21.3% |
| International Stocks (*MSCI* EAFE NR USD) | -0.7% | 1.0% |
| Emerging Mkt Stocks (*MSCI EM PR USD*) | -5.2% | 8.6% |
| China (CSI 300) | 1.6% | -11.2% |
| Germany (DAX) | 8.5% | 6.9% |
| Japan (NIKKEI 225) | 15.9% | 2.4% |
| India (SENSEX) | 3.2% | 3.5% |

*Global Indices returns exclude dividends and are in local currency except where noted otherwise

| U.S. EQUITY SECTORS | 4TH QUARTER | 1-YR (12/31/16) |
|---|---|---|
| S&P 500 Utilities | 2.2% | 18.2% |
| S&P 500 Telecom | 8.3% | 23.5% |
| S&P 500 Consumer Staples | -1.0% | 5.4% |
| S&P 500 Materials | 3.2% | 16.7% |
| S&P 500 Industrials | 8.0% | 18.9% |
| S&P 500 Energy | 8.2% | 27.4% |
| S&P 500 Information Technology | 2.6% | 13.9% |
| S&P 500 Consumer Discretionary | 3.8% | 6.0% |
| S&P 500 Health Care | -3.5% | -2.7% |
| S&P 500 Financials | 22.2% | 22.8% |

| FIXED INCOME AND VARIOUS OTHR ASSET CLASSES | 4TH QUARTER | 1-YR (12/31/16) |
|---|---|---|
| Real Estate (*DJ US REIT*) | 5.4% | 3.4% |
| Interm-Term Bond (*Barclays Interm. Gov/Credit*) | -3.6% | 2.1% |
| High Yield Bond (*BofA/ML Hi Yld Mst II*) | -10.6% | 4.7% |
| Muni Bond (*Barclays 7 Yr Muni*) | 0.4% | 4.4% |
| Short-Term Bond (*Barclays 1-3Yr Gov/Credit*) | -1.2% | 0.9% |
| Commodities (*Bloomberg Commodity*) | 2.8% | 11.8% |
| Master Limited Partnerships (*S&P MLP*) | 1.6% | 12.5% |

3/31/16. Performance includes dividends, except where noted otherwise.

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