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summaries

SIGMA INVESTMENT COUNSELORS

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Portfolio Insurance, Hedge Funds and Smart Beta – Beware of Wall Street!

With all due caution about making predictions in advance of a US presidential election as unusual as this one, we will digress and use this space instead as an opportunity to "get something off our chests." We have been confounded for the last ten years about the interest and resulting billions of dollars invested in hedge funds. As we now observe investors abandoning hedge funds en masse we feel a sense of redemption. Clearly we believe this is a positive development as we were never convinced of the merit of the investment strategies embraced by hedge funds.

Note that we have labeled hedge funds a strategy and not an asset class (as some "experts" deemed them). It was never clear to us how they could be categorized as anything but a strategy. An asset class has distinct and definable features. They are largely common stocks, bonds and cash equivalents. Alternative investments, in the proper vernacular, are commodities, real estate and gold. If an investor had an all common stock portfolio it was an equity portfolio. If all bonds, a bond portfolio. If a combination, it was called a balanced portfolio. When investing in equities, different managers follow different strategies – momentum, value, growth, etc. Looking at hedge funds, the differentiating factor is – yes, you guessed it - THE STRATEGY. A strategy does not define an asset class.

The investing world has finally concluded this, noting that many of these strategies have failed to produce the necessary returns to merit inclusion in portfolios. As a result, investors are liquidating their positions in them. Clients of Sigma were never exposed to these vehicles and as a result, did not experience the drag on investment returns.

The purpose in this discussion – to forewarn that Wall Street is in a constant mode of developing "products" to foist upon the public. The most recent was hedge funds. Many years ago it was portfolio insurance. Next we believe will be "smart beta". It's a fad. Be on the lookout. If an investment manager tries to push "smart beta" probe for evidence of likely success. Who knows what it will be after "smart beta" but the Wall Street fee machine never sleeps!

Getting off the soapbox and turning our attention to the financial markets broadly, we noted that in spite of a very rocky period for financial markets at the beginning of the year, and notwithstanding the aforementioned contentious presidential election

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season, financial assets continued to perform this year in a positive fashion, as evidenced by the table below.

Benchmark Returns As of 9/30/16	**YTD 2016**
Domestic Equities	
S&P 500 Large Cap	7.84%
S&P 400 Mid Cap	12.40%
S&P 600 Small Cap	13.88%
International Equities	
MSCI EAFE Developed Int'l	1.73%
MSCI Emerging Markets	16.02%
Bonds	
Barclays U.S. Aggregate Bond	5.79%

As history has shown time and again, financial markets tend to climb a "wall of worry" and this year appears to be no exception. However, much can change in a short period of time. We continue to monitor global economic and political trends to ensure our strategies are appropriate. Over the very long term, we remain constructive on the outlook largely because of the positive developments in the energy and technology sectors, which makes improvements likely in virtually all other economic sectors over the coming years.

Thanks again for your confidence and trust in Sigma Investment Counselors.

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