Mallard Financial Market Alert
January 21, 2016

In the first two weeks of January, the US stock market fell almost 8%, foreign stocks are down about 9%, and smaller US stocks are down about 10%. Energy stocks are down about 12%. The Chinese stock markets have fared even worse. One China stock fund we have used is down 16%. Some market analysts have begun to recommend that investors sell their stocks and jump over to quality bonds. What should you do?

At Mallard we have been reviewing the markets and the data and the analyses. While it is **always** possible that a sharp market decline is underway, we have concluded that this downturn is much more emotionally-driven downturn than economically-driven. As such, we feel that this presents more of an opportunity than a challenge.

On January 6th we issued our quarterly **Market Review and Outlook**, with its 2016 predictions. You can find it at http://www.mallardfinancial.com/documents/160106mktreview.pdf. It presents the evidence of continued, yet very modest, economic growth, with fair prices for today's stocks.

The US economy has been enjoying VERY steady economic growth since 2010, and this is fully expected to continue through 2016. Due to very low interest rates, low gas prices and low unemployment, consumers should have money in their pockets, and 68% of the US economy is consumer consumption. In addition, housing and auto sales continue their steady recovery.

On January 15th Paul presented the **quarterly conference call**. You can find his opening comments at http://www.mallardfinancial.com/documents/160115conferencecall.pdf. The comments acknowledge the challenges that 2016 has brought, but again presents reasons for confidence in the overall global stock and bond markets and global economy.

US stocks are cheap on both an absolute and relative basis. At the end of 2015, the PE ratio based on forward earnings for the S&P 500 were average, and this month's decline has brought that ratio into the inexpensive range. Furthermore, given how expensive bonds are, and how inflation is greater than money market yields, on a relative basis **STOCKS ARE ATTRACTIVELY PRICED**.

China has shared the headlines with oil prices this year, and the China news is worrisome. Some of it is self-inflicted. Their internal stock markets can be dominated by local investors who are typically VERY short-term oriented. The authorities introduced circuit-breakers to slow and stop trading when markets tumbled, and the introduction itself caused these day traders to sell and trip the circuit breakers.

Importantly, while no one trusts the economic numbers coming from the Chinese government, and everyone agrees that economic growth in China is slowing, **there are several reasons to temper fears**. Despite the growth rate declining, the Chinese economy is still growing, and at a rate that the US would love to enjoy. Furthermore, the Chinese government and central bank have extensive resources to continue to help prevent a hard landing, resources that include over $3 trillion in foreign exchange reserves and 1-year central bank policy interest rates of over 7%. Furthermore, trade from the US to China makes up 7% of our exports, and less than 1% of our economy (and the same for Europe's GDP). **The magnitude of the fear-driven market decline is simply not economically justified.**

Drops in the price of **oil** and rises in the value of the US dollar drove 2015 stock market results. Once the price of oil stabilizes, wherever it stabilizes, the global economy will adapt and move forward. The stabilization did not occur in 2015, and hasn't yet happened in 2016, but it will happen. The price plunge has not been tied to a plunge in demand (which would indicate weak global economic growth), but rather a glut in supply. While oil prices had a large negative impact on stock prices in the 1970s, that was from high oil prices. At some point, investors are going to recognize that there are many more winners from low oil prices than losers. In the meantime, those winners are trading at low prices.

Similarly, the **US dollar** will stabilize at some point, and could retreat. The stabilization alone will help US companies, and a retreat could provide a welcome tailwind. Stabilization in the US dollar is likely in 2016, removing one of 2015's headwinds.

The same Leading Economic Indicator that turned downward in 2006 ahead of the 2008-2009 economic downturn has been rising very steadily since mid-2009. This is a measure that is very broad and comprehensive in its scope. JP Morgan's Global Market Strategist, Dr. David Kelly, notes that you cannot take a big-picture view without a wide-angle lens. Investors (and many market analysts) this month are looking at one factor and using it to draw global conclusions. While this approach makes great headlines, it leads to bad decisions.

We recognize that the wide range of market opinions can be alarming to you. For this reason, **we are sending this Market Alert out to you, with these four guiding points:**

First, if you would like to talk, to share concerns, ask questions, send an email to any or all of Mallard's Investment Committee (paul@mallardfinancial.com, ryan@mallardfinancial.com, kenny@mallardfinancial.com). We are pleased to provide a sounding board, explain the reasons for our views, and otherwise assist you.

Second, our tried-and-true approach of **disciplined, methodical, quarterly rebalancing** is well-suited to almost all market environments, including ones with 10% declines. Our approach automatically and systematically purchases more stocks when their prices are cheaper, and does so by removing the emotions, and letting the data drive the decision-making. Clients who are rebalanced in January are benefitting from the recent stock market decline, and if it stays down through March, the rest of our clients will obtain the same benefits.

Third, if you would like to 'step it up' a notch, you can opt in to our **Drop and Give Me Five™** program, in which we purchase a global stock fund with 5% of your portfolio (from cash and bonds) if the stock market has dropped 5% or more since your last rebalance. We have been busy the past two weeks locking in the current lower prices for these purchases for the clients who enrolled since we created this program last year. To opt in, you should contact us and let us know that you want to sign up for the **Drop and Give Me Five™** program.

Fourth, you may be unswayed by our view that we have an opportunity now to buy cheaper stocks. You may be losing sleep over the warnings of an imminent crash. If this describes you well, then you should consider having us implement the **Firewall Investing™** program for you. We created this program in early 2009, as the markets were plummeting. The program is based on dual promises. Mallard promises to not purchase any more stocks in your portfolio (even if they seem cheap to us, we know that this can cause you undue stress, so we won't do it). In return, you promise that you won't ask Mallard to sell any stocks from your portfolio. We remind you that you have years and years and years of withdrawals currently invested in cash and bonds in your portfolio, and you don't **need** to sell stocks. As was the case from 2009 forward, leaving your stocks alone enables them to recover, and recover nicely. If you 'can't take it anymore,' please contact us and ask us to implement the **Firewall Investing™** program for you. The program helps clients avoid one of the most common investing mistake of selling low.

Please review some of the resources that we regularly make available to you at Mallard's website, at http://www.mallardfinancial.com/literature/. Again, please don't hesitate to reach out to us if you have questions or concerns. If you feel that you would like to utilize one of the two programs we have created, please contact us.

It has been a very rough start to 2016. Together we will weather this storm.