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Capital Market Commentary
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Benjamin Graham, who served as Warren Buffet's instructor at Columbia University, is widely regarded as one of the wisest professionals in the history of modern finance. He authored *The Intelligent Investor* in 1949 which many still consider the best book ever written about investing. He described investing, equity investing in particular, as the process of owning shares in a business. He did not pay much attention to daily fluctuations in the prices of the stocks of the companies he owned. In fact, one of his favorite sayings was, "In the short term, the stock market behaves like a voting machine, but in the long run it acts like a weighing machine." He meant that human emotion can dominate price action in the short run and cause erratic swings in prices, but that a company's true value will, in the long run, be reflected in its stock price based on its fundamentals. These words are as true today as they were 70 years ago.

We have seen the "voting machine effect" over the last three trading days and particularly today. This morning the DJIA traded down over 1,000 points in a matter of minutes to 15,370, putting the index down about 16% from its May 19, 2015 high of 18,312. It subsequently rebounded nearly 850 points by mid-day, only to close at 15,871.

At times like this, we best serve our clients by focusing on the following:

1) Limiting the amount of emotion in the investment process by understanding the facts surrounding current capital market and economic events
2) Maintaining the proper perspective between these facts and your portfolio

The recent market turmoil seems to stem from concerns that a persistent Chinese growth slowdown may be more enduring than investors foresaw. An approximate 9% export slowdown (year-over-year) and the lowest manufacturing index reading in six years contributed to China's decision to devalue its currency, which surprised markets. In addition, tumbling commodity prices are fueling fears of a global growth slowdown, led by China and other emerging market economies. China's Asia trading partners have felt the pressure to devalue their own currencies in order to remain competitive. This raises the concern that deflation will be exported to developed world economies from Asia.

Last week, investor's concerns grew after the S&P 500 broke its 200-day moving average and Chinese stock prices fell through a government stipulated threshold of support. These developments rattled most of the world's stock markets and investors question which tools are available to Central Bankers to stabilize the decline. Since most major developed economies have 0% short-term interest rates, and Europe and Japan are conducting quantitative easing, what remains in the Central Bank's arsenal?

On the positive side, recent economic data from the U.S and other developed economies has been generally positive. Consumers and businesses that use these inexpensive commodities should have greater buying power and more disposable income. The challenge is that many of the energy and raw material producing companies have large debt loads relative to the sale price of their commodities, which impinges the firm's ability to finance ongoing operations. The credit markets have reflected this by making debt refinancing more expensive and harder to achieve.

In terms of maintaining proper perspective, one must recognize market realities. One of these realities is that markets go down a lot faster than they go up. Another way to express the same sentiment is that “markets go up like an escalator but down like an elevator.” Market declines are a normal part of investing. As the accompanying chart from Yardeni Research details, the S&P 500 has experienced 11 double-digit declines since 1980. That means approximately every third year for the last 35 years, the stock market has experienced a double digit decline. The median values of these declines were 19% over 104 days. For perspective, this morning, we briefly realized a 16% decline over 97 days. We have not witnessed a decline greater than 10% since October 2011, almost four years ago. By historical standards, the market is overdue for a double digit decline. The market has been remarkably and uncommonly calm in its upward march for nearly 4 years. That is simply not how markets work.

	Number of Double Digit Drawdowns	Average Losses
1980s	4	-23.0%
1990s	2	-19.6%
2000s	3	-40.2%
2010s	2	-17.7%

Source: Yardeni Research

Volatile market corrections serve to remind investors that stocks are risk assets and carry what is called an “equity risk premium” for a reason. The reason stocks provide the types of long-term returns that they do is because their daily price swings can be volatile. To be compensated for assuming this volatility, investors demand higher returns from stocks. Investors with longer time horizons have realized this premium as stocks have provided a real return of 6% over the rate of inflation going back to the 19th century. However, the pattern of these returns is anything but linear. It never has been nor ever will be. For those who choose not to tolerate this volatility, bonds, which have an entirely different risk and return profile, are incorporated into portfolios to the proper degree to reduce volatility. We counsel our clients in order to find the right balance between both stocks and bonds for their specific needs and goals, which is the essence of investment counseling.

As always, we will continue to evaluate the markets and look for opportunities to improve the portfolios. We will continually evaluate the revaluation of risk and will continue to monitor the global economic picture and its impact on our portfolio holdings. Taking Ben Graham’s counsel, we will continue to construct portfolios based on sound diligent research, a clear understanding of the fundamentals, and aligning these portfolios with clients’ goals and objectives.