CLEARVIEW WEALTH SOLUTIONS

Some economists have put the U.S. economy on recession watch as a result of last Friday's poor job numbers. Only 38,000 jobs were added to non-farm payrolls, a big miss to the 158,000 new jobs expected. More concerning is that jobs in the service sector contracted (by 77,000) for the fourth consecutive month. In cycles past, this has been a leading indicator of recession by about five months. On a more positive note, the unemployment rate fell to 4.7%, although that was mostly due to a half million people leaving the workforce. Wage growth grew at a healthy 2.5% clip in May.

Given the weak jobs number and likely slow GDP growth in the second quarter, the stock market will be increasingly dependent on earnings growth. Second half quarterly earnings comparisons year-over-year are easier than recent quarterly comparisons, but next year's 10% expected earnings growth rate is still a big hurdle. It looks as if the stock market will need more visibility into 2017 if it is to sustain an additional rally.

Why Balanced Portfolios Make Sense for Most Investors

A balanced account is a portfolio that has a mix of stocks and bonds. A cash reserve would likely also be included for sake of liquidity, especially for retirees. Investors expect to have a higher return over time with portfolios that have a greater allocation to stocks. In fact, over an extended period the highest returns come from an all stock portfolio. Further, most investors would also accept that an all stock portfolio will have more volatility than a balanced portfolio. Are these assumptions all correct? Yes. Let's review actual numbers going back to 1926.

1926 – 2013	GEOMETRIC ANNUAL RETURN	STANDARD DEVIATION	SHARPE RATIO*
100% LARGE COMPANY STOCKS	10.1%	20.2%	.33
70% STOCKS/30% BONDS	9.1%	14.4%	.39
50% STOCKS/50% BONDS	8.3%	11.2%	.43

*The Sharpe Ratio is a measure for calculating risk-adjusted returns. The higher the ratio the better the risk adjusted return.

Sources: Ibbotson SBBI, 2014 Classic Yearbook, Clearview Wealth Solutions

Taking a closer look at the numbers gives us interesting insights. For example, the 70% stocks/30% bonds mix returns only 1% less than 100% stocks yet has 28% less volatility or risk as measured by standard deviation. Standard deviation is a measure that is used to quantify the amount of dispersion of data points around the mean with a lower standard deviation indicating the data points are closer to the mean. A 50/50 mix has an annual return of about 1.8% less than the all stock portfolio but has 44% less volatility! The balanced portfolios have slightly lower returns but **much lower volatility**.

Which is the better bet? Which is the best risk-adjusted return? The Sharpe ratio calculation can help answer that. It is a statistical measure for calculating risk-adjusted returns. The higher the ratio the better the risk-adjusted return. **The table shows higher Sharpe ratios for the balanced portfolios compared to an all stock portfolio.**

Balanced portfolios offer another advantage in that they are less likely to have a big down year since stocks in the portfolio are buffered by the less volatile bond allocation. Compounding returns with big negative numbers (like 2008) hurts long term investment performance.

All stock portfolios remain appropriate for those investors willing to financially and emotionally withstand higher volatility along with the increased possibility of a big down year. However, based on the numbers, balanced portfolios provide much better risk-adjusted returns and are therefore the better bet for most investors.

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