Financial Markets Update
Third Quarter 2017

The Uncommon Average

"I have found that the importance of having an investment philosophy – one that is robust and that you can stick with – cannot be overstated."
– David Booth

The US stock market has delivered an average annual return of around 10% since 1926. But short-term results may vary, and in any given period stock returns can be positive, negative, or flat. When setting expectations, it's helpful to see the range of outcomes experienced by investors historically. For example, how often have the stock market's annual returns actually aligned with its long-term average?

Exhibit 1 (on the next page) shows calendar year returns for the S&P 500 Index since 1926. The shaded band marks the historical average of 10%, plus or minus 2 percentage points. The S&P 500 had a return within this range in only six of the past 91 calendar years. In most years the index's return was outside of the range, often above or below by a wide margin, with no obvious pattern. For investors, this data highlights the importance of looking beyond average returns and being aware of the range of potential outcomes.

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Financial Markets Performance
3rd Quarter, 2017 (Source index and total return)

Stocks & Alternatives	
Large U.S. Companies (S&P 500)	4.48%
Small U.S. Companies (Russell 2000)	5.67%
Large Non-U.S. Companies (MSCI Dev Mrkts)	1.49%
Small Non-U.S. Companies (FTSE Sm Cap)	0.31%
Emerging Markets' Companies (MSCI Emerging)	11.39%
Commodities (Bloomberg Commodity Index)	2.52%
Bonds	
Long-Term U.S. Treasuries (Barclays U.S. Long Gov)	0.58%
Total U.S. Market (Barclays U.S. Agg Bond)	0.85%
Short-Term U.S. Treasuries (Barclays U.S. Short Gov)	0.28%

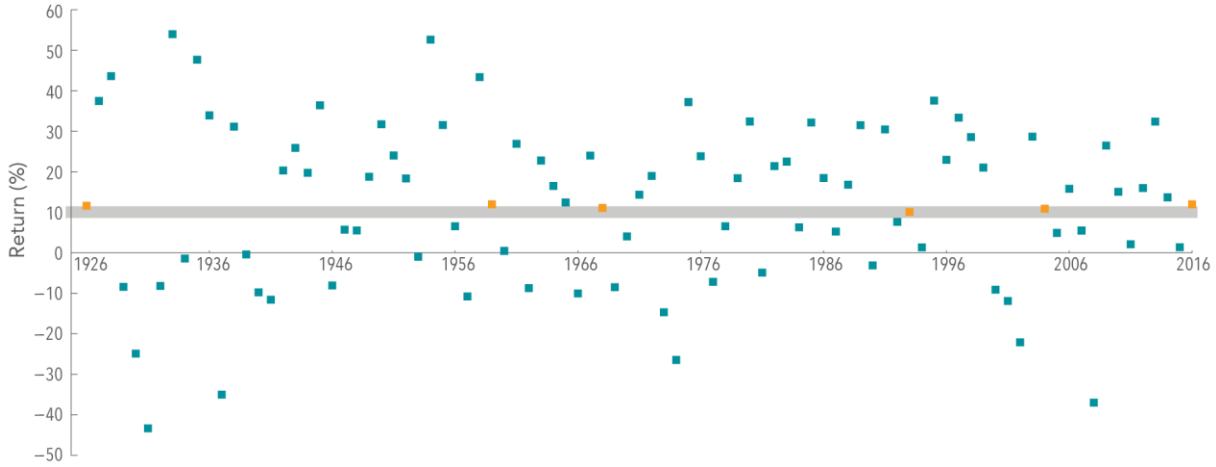
Financial Markets Valuation
Values calculated with preliminary data available as of Oct, 2017

U.S. Stocks (S&P 500)	
Price to Earnings (P/E) Ratio	22.04
Price to Book (P/B) Ratio	3.07
Earnings Yield	4.54%
Dividend Yield	2.01%
Corporate Earnings Retention Rate	55.64%
Bond Yields	
2 Year U.S. Treasury Note	1.47%
10 Year U.S. Treasury Note	2.33%
30 Year U.S. Treasury Bond	2.86%
Non U.S. Stocks (MSCI World ex USA All Cap)	
Price to Earnings (P/E) Ratio	17.41
Price to Book (P/B) Ratio	1.69
Earnings Yield	5.74%
Dividend Yield	3.2%
Corporate Earnings Retention Rate	44.08%

Economic Data
Values as of Sep, 2017 (Inflation and GDP annual changes)

US Inflation Rate (All Items)	2.23%
US GDP Real Growth Rate	3.0%
US Unemployment Rate	4.2%
US Industrial Utilization Rate	76.0%

Exhibit 1. S&P 500 Index Annual Returns

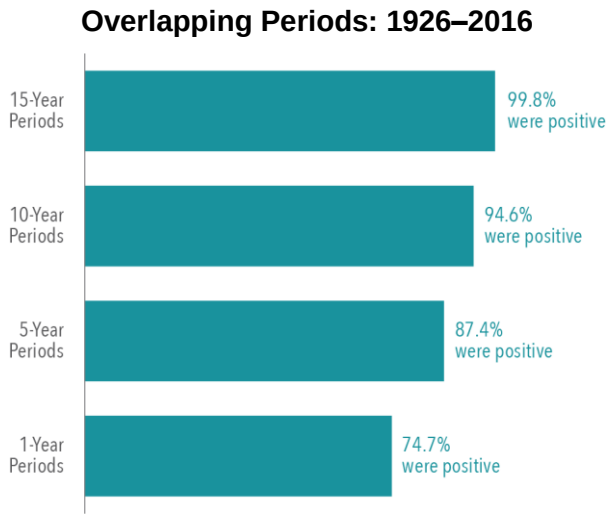


In US dollars. The S&P data are provided by Standard & Poor's Index Services Group. Indices are not available for direct investment; therefore, their performance does not reflect the expenses associated with the management of an actual portfolio. Past performance is not a guarantee of future results. Index returns do not reflect the cost associated with an actual investment.

Tuning in to Different Frequencies

Despite the year-to-year uncertainty, investors can potentially increase their chances of having a positive outcome by maintaining a long-term focus. Exhibit 2 documents the historical frequency of positive returns over rolling periods of one, five, 10, and 15 years in the US market. The data shows that, while positive performance is never assured, investors' odds improve over longer time horizons.

Exhibit 2. Frequency of Positive Returns in the S&P 500 Index



From January 1926–December 2016 there are 913 overlapping 15-year periods, 973 overlapping 10-year periods, 1,033 overlapping 5-year periods, and 1,081 overlapping 1-year periods. The first period starts in January 1926, the second period starts in February 1926, the third in March 1926, and so on. In US dollars. The S&P data are provided by Standard & Poor's Index Services Group. Indices are not available for direct investment; therefore, their performance does not reflect the expenses associated with the management of an actual portfolio. Past performance is not an indication of future results.

Conclusion

While some investors might find it easy to stay the course in years with above average returns, periods of disappointing results may test an investor's faith in equity markets. Being aware of the range of potential outcomes can help investors remain disciplined, which in the long term can increase the odds of a successful investment experience. What can help investors endure the ups and downs? While there is no silver bullet, having an understanding of how markets work and trusting market prices are good starting points. An asset allocation that aligns with personal risk tolerances and investment goals is also valuable. Financial advisors can play a critical role in helping investors sort through these and other issues as well as keeping them focused on their long-term goals.

The financial market summary above includes historical data and Callahan Financial Planning Company's internal analysis and is designed for informational purposes only. Scenarios described do not encompass all possible or probable outcomes and are not an indication of future results. Financial probability modeling is not a guarantee of future investment returns, and investing in stocks or bonds carries risks. Past performance does not guarantee or predict future results. Investment decisions should be made with the advice of your financial planner, consistent with your financial plan and the other aspects that make up your financial situation today.

Data sources for this report included Standard and Poor's, MSCI, Ibbotson Associates, and Dimensional Fund Advisors LP. This information is provided for educational purposes only. Diversification does not assure a profit or prevent risk of market loss. Indices are not available for direct investment. Index performance does not reflect expenses associated with the management of an actual portfolio. Historical stock performance is represented by the MSCI All Country World [Stock Market] Index (gross dividends) and Treasury Bills are represented by U.S. 1 month Treasury Bills.

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