

LOCAL FIRM, NATIONAL PROMINENCE

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**The Monthly E-Newsletter**

Kimberly Foss, CFP®, CPWA®  
PRESIDENT  
Empyion Wealth Management

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**The Road Ahead**

As investment advisors, we must be constantly monitoring the market landscape for developments—political, social, financial, military, or what have you—that we believe are going to have significant impact on our clients' assets, strategies, and plans. This is the type of "big-picture" view and thinking that informs our advice and helps us maintain our clients' investment posture in a way that maximizes long-term performance. Obviously, we aren't perfect. In fact, the one thing we really need—a copy of tomorrow morning's financial headlines—has proven stubbornly difficult to obtain! Or, as an old-time stockbroker once said, "It is very difficult to make accurate predictions, especially about the future."

However, it is possible to discern some big-picture themes that will clearly influence the markets. A recent report by a major mutual fund company points to some compelling trends

that appear to us as very likely to exert strong influence on the markets as a whole over the next twelve to eighteen months. In this edition of our newsletter, let's consider these "mega-trends" and the ways in which, we believe, they point to a near- to medium-term period of moderate or low growth, accompanied by low interest rates.

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## 1. Technology

Throughout history, advances in technology have typically been disruptive, in one way or another. When the first people figured out how to use fire, they achieved a major advantage over other groups competing for the same territory. When the Industrial Revolution developed, a huge shift in population patterns, from the agrarian countryside to large urban centers, altered the foundations of society. Today, we are seeing technology disrupt wide sectors of the economy as robotics, algorithms, and digitization reduce or eliminate jobs that formerly were done by humans. Not only that, but as the tech revolution continues to expand, companies are making fewer and fewer investments in factories, stores, and other brick-and-mortar assets, while expanding their emphasis on apps, online marketing, and other digitally based strategies. Overall, this trend has had and continues to have a dampening effect on capital spending by corporations.



Courtesy The Vanguard Group

## 2. Demographics

In much of the developed world, aging populations continue to hold down opportunities for economic growth. We are seeing this phenomenon clearly in the US, where the Baby Boomers—the largest population segment in history—are entering retirement in massive numbers. What happens when people retire? Typically, they switch from being net spenders to being net savers. Rather than snapping up consumer goods as they did during their peak earning years, Boomers are now using their money to bulk up their retirement accounts. This continuing trend will tend to produce a glut in savings, which, like excess supply in any other area, will decrease the value of the product. In this

case, that decrease will take the form of lower interest rates.

### 3. Globalization

We are seeing unprecedented momentum towards more and more free movement of capital and labor across borders. In fact, globalization, and the reactions against it, have featured strongly in recent elections, both in the US and abroad. If labor and capital continue their ability to move freely in order to seek their places of maximum value, we will see cheaper labor and cheaper goods leading to very low inflation.

While this can be good news to consumers in the

form of a lower overall cost of living, it also means that manufacturers will have very little room to increase their prices, which indicates lower profits and a lower rate of growth.

#### Globalization

The free movement of capital and products is increasing competition on prices and labor.

Increased trade makes use of comparative advantages in production



The end result?

Lower inflation

Courtesy The Vanguard Group

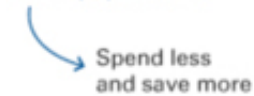
#### Demographics

Aging populations are weighing on growth in the developed world.

Economies with younger populations



Whereas older populations



Which can produce



Courtesy The Vanguard Group

### What Does This Mean for Investors?

Taken together, these investment themes may portend slow-to-modest growth and income opportunities for investors over the next twelve to eighteen months. Due to the limits on growth outlined above and also to the current stretched nature of equity valuations, large gains in stocks may be more difficult to come by. Concurrently, low interest rates, while generally favorable for companies that need to borrow in order to maintain or expand operations, are not likely to be a source of good news for savers and conservative investors, since fixed-income portfolios will not enjoy the generous interest rates that were seen in previous years. In the broad recovery from the global financial crisis of a few years ago, investors saw some very generous rates of return, as valuations ascended from depressed levels.

Current research, however, indicates that equity return rates of between 4 and 8 percent may be most realistic in the near to medium term, and some downward volatility can probably be expected along the way. For fixed-income portfolios, total return (interest plus price appreciation) of 1.5 to 2.5 percent is probably a reasonable expectation. To put these estimates in perspective, global equity returns, 1926-2016, averaged 10 percent, while global bond returns for the same period averaged 5.4 percent. In a diversified portfolio holding 60 percent equities and 40 percent fixed-income, investors can likely expect inflation-adjusted returns in the range of 3-5 percent during the period. This compares with global returns for a 60/40 portfolio of 5.5 percent, on average, 1926-2016.

What should we make of all this? Regarding equities, we would advise caution, but we are not bearish. In fixed-income, our outlook, while expecting only modest total return, is still positive.

Overall, we would expect global growth to continue at a slower rate, but not to stagnate.

As in any market environment, we will continue to advise our clients to maintain diversification appropriate to their investment goals and strategies. While we believe the investment outlook for the next several months—or years—is likely to offer a number of challenges, we continue to advocate for our long-standing focus on fundamentals: diversification, discipline, low-cost implementation, a carefully conceived strategy, and periodic review, with rebalancing as needed.

### ***Stay Diversified, Stay the Course!***



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Kimberly Foss, CFP®®, CPWA®®  
Empyrium Wealth Management, Inc.  
[www.empyriumwealth.com](http://www.empyriumwealth.com)  
(916) 786-7626  
(800) 787-7634

For more information on Emyprion Wealth Management, visit [www.empyrionwealth.com](http://www.empyrionwealth.com).

To learn more about Kimberly Foss, visit [www.kimberlyfoss.com](http://www.kimberlyfoss.com).