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# THE GLOBAL INVESTMENT PULSE

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## ANALYZING PRICE-TO-EARNINGS RATIOS (P/E)

**By Louis P. Stanasolovich, CFP®, CCO, CEO and President of Legend Financial Advisors, Inc.® and EmergingWealth Investment Management, Inc.**

Here's a pop quiz to test your investment smarts: Since 1870, the average Price/Earnings (P/E) ratio of stocks in the S&P 500 Index has been about 15.00. True or false?

If you said True, you're right. The average P/E for the past 150 years has been approximately 15.00–based on the most common type of P/E that tracks trailing net earnings for the last four quarters (Earnings for the last 12 months are divided by the current price of the stock. This is also known as a trailing 12 months P/E.).

Analyzing Price-To-Earnings Ratios (P/E), *continued on page 14*

## USER BEWARE: ONLINE CHARTS CAN BE WRONG

**By Louis P. Stanasolovich, CFP®, CCO, CEO and President of Legend Financial Advisors, Inc.® and EmergingWealth Investment Management, Inc.**

Investors often research information on mutual funds, Exchange-Traded Funds and stocks by utilizing online charting services. These services are often offered as free services from Websites such as Bloomberg, Google and Yahoo.

Here's the rub though: These services often don't take into account distributions from mutual funds and Exchange-Traded Funds. Distributions from those types of investments generally include dividends and capital gains. With regard to stocks, it is usually dividends. Charts that adjust for historical distributions illustrate the true economic performance for the shareholder over time, while those that do not, not only are just plain wrong, but are very misleading. In fact, it is similar to reviewing the cost basis of a mutual fund without the dividends and capital gain distributions and evaluating the performance based upon that partial information.



## UNDERSTANDING THE INCOME TAXATION OF MUTUAL FUND DISTRIBUIONS

**By James J. Holtzman, CFP®, CPA, Legend Financial Advisors, Inc.® and EmergingWealth Investment Management, Inc.**

Investors have a number of misconceptions about income taxation when it comes to mutual fund distributions. This article will clarify many of these issues.

Mutual fund distributions are not taxable when a mutual fund is owned within a tax-deferred account (Ex. IRAs, Roth IRAs, Simple IRAs, 401(k)s, 403(b)s, and other retirement plans, etc.).

1. Mutual Fund distributions can be taxable as long- or short-term capital gains for taxable accounts (individual, joint, UGMA/UTMA, corporate, trust, etc.). Certain distributions may also be designated as dividends as well. It is also possible to have certain distributions be designated as a return of capital. Appropriate income taxation applies whether or not the distribution is reinvested or taken in cash.

Understanding The Income Taxation Of Mutual Fund Distributions, *continued on page 6*

## DOW POWER: THE DOW JONES INDUSTRIAL AVERAGE

**By Diane M. Pearson, CFP®, PPC™, CDFA™, Legend Financial Advisors, Inc.® and EmergingWealth Investment Management, Inc.**

The Dow Jones Industrial Average (DJIA, or the Dow, as it's commonly called) can be a valuable leading economic indicator. Typically, a rise or fall in its value of 20.0% or more is generally considered to precede corresponding movements in the business cycle.

The Dow represents share prices of 30 blue chip industrial corporations, chosen because their operations cover the broad spectrum of industrial America. The index is Price-Weighted–meaning the actual prices of each stock determines its weight in the index. This means if Company A's stock price is $100.00 per share and Company B's stock price is $50.00 per share, then Company A is worth twice and its weighting is twice as much as Company B's in the index. The names of all 30 corporations are probably familiar

Dow Power: The Dow Jones Industrial Average, *continued on page 6*

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## LOUIS P. STANASOLOVICH, CFP®, EDITOR

Louis P. Stanasolovich, CFP® is founder, CCO, CEO and President of Legend Financial Advisors, Inc.® (Legend) and EmergingWealth Investment Management, Inc. Lou is one of only four advisors nationwide to be selected 12 consecutive times by Worth magazine as one of "The Top 100 Wealth Advisors" in the country. Lou has also been selected 12 times by Medical Economics magazine as one of "The 150 Best Financial Advisors for Doctors in America", twice as one of "The 100 Great Financial Planners in America" by Mutual Funds magazine, four times by Dental Practice Report as one of "The Best Financial Advisors for Dentists In America" and once by Barron's as one of "The Top 100 Independent Financial Advisors". Lou was selected by Financial Planning magazine as part of their inaugural Influencer Awards for the Wealth Creator award recognizing the advisor who has made the most significant contributions to best practices for portfolio management. He has been named to Investment Advisor magazine's "IA 25" list three times, ranking the 25 most influential people in and around the financial advisory profession as well as being named by Financial Planning magazine as one of the country's "Movers & Shakers" recognizing the top individuals who have done the most to advance the financial advisory profession.

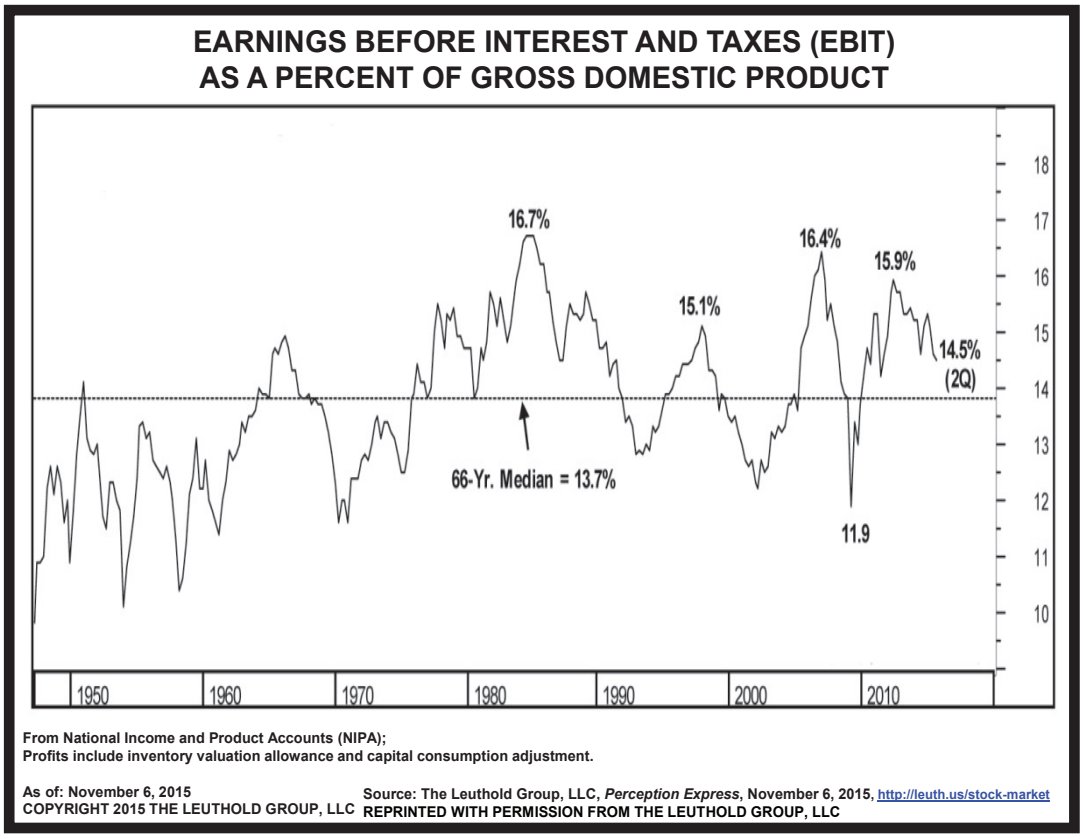
# PROFIT MARGINS: REVERSION CAN BE MEAN

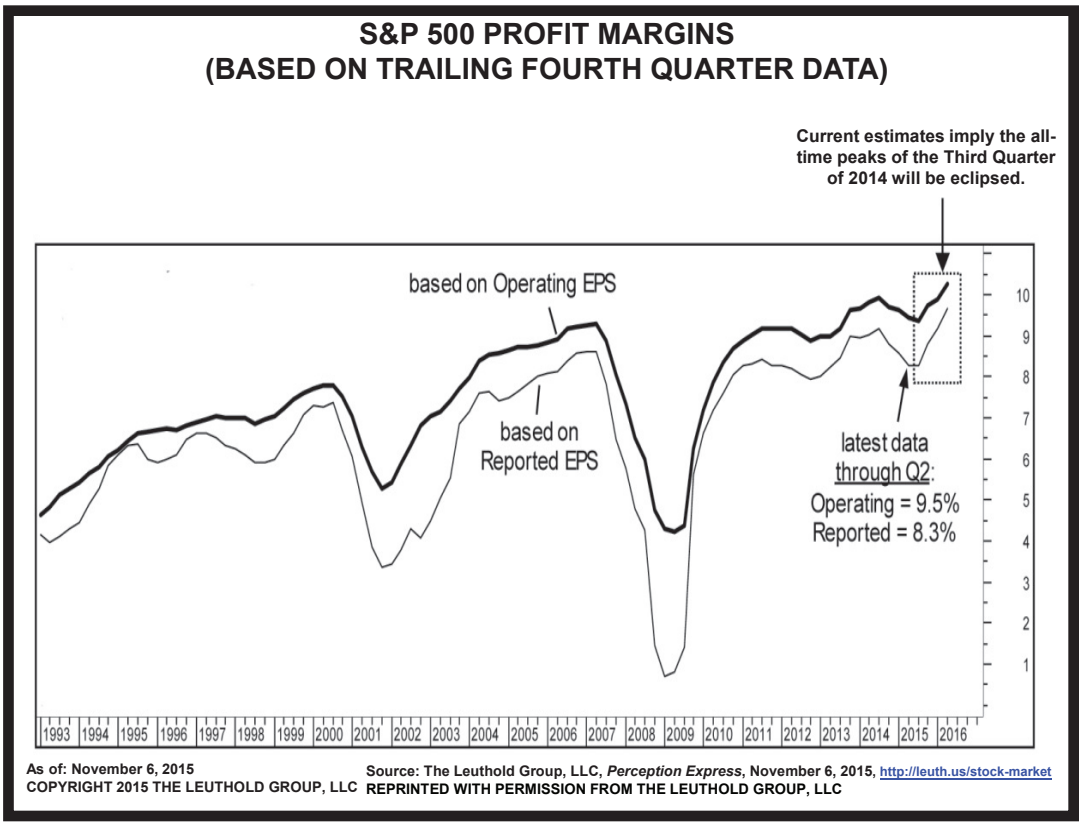
By Doug Ramsey, CFA, CMT, Chief Investment Officer, The Leuthold Group, LLC

While "new era" thinking is nowhere near as pervasive in this market cycle as it was in the late 1990s, we still hear plenty of it when it comes to the subject of profit margins. Yes, we are as impressed as anyone with the ability of the big S&P 500 companies to continually squeeze profit gains out of modest sales declines. Investors are on high alert for any sign of wage pressure that might eventually put the pinch on profit margins. However, profit margins have already been crimped where it matters most–at the operating line. In the second quarter, National Income and Product Accounts (NIPA)'s Earnings Before Interest and Taxes (EBIT) margin fell to a new four-year low of 14.5%, down almost a point and a half from the early 2012 cycle peak. What's more, that 2012 cycle high never challenged the 2007 peak operating margin of 16.4%, let alone the 1984 all-time high of 16.7%.

NIPA net profit margins did break out to all-time highs in this cycle (reaching 10.1% in the fourth quarter of 2011), but we have emphasized that steep declines in interest expense and corporate income taxes were the main drivers of that breakout. The chart below entitled "Earnings Before Interest and Taxes (EBIT) As a Percent of Gross Domestic Product", shows that a capitalistic, reversion-to-the-mean process remains at work on companies' operating lines. It is reassuring, in a way. (See "Earnings Before Interest and Taxes (EBIT) As a Percent of Gross Domestic Product" chart to the top right.)

The popular storyline remains that margins will expand to even higher highs (a new "permanent plateau?"), lifted by free trade, capital-for-labor substitution (robotics and other technology), labor-for-labor substitution (open borders), and the like. In fact, Street analysts are betting heavily on that outcome over the next four quarters, with S&P margins on both Operating Earnings Per Share (EPS) and Reported EPS both projected to eclipse the highs of last year's third quarter (See the chart "S&P 500 Profit Margins" to the bottom right.). We would take the underside of that bet, if our fantasy football league weren't already drawing regulatory scrutiny.




**Source: This article was excerpted from "Margins: Reversion Can Be Mean", by Doug Ramsey, CFA, CMT, Chief Investment Officer, The Leuthold Group, LLC, (*Perception Express*, November 6, 2015), http://leuth.us/stock-market**

# REASONS FOR HISTORICAL STOCK MARKET DECLINES

1. June 1948 to June 1949. Stocks decline 20.6%. A world still trying to figure out what a post-war economy looks like causes a second U.S. recession with more demobilization. Inflation surges as the economy adjusts. The Korean conflict heats up.

2. June 1950 to July 1950. Stocks fall 14.0%. North Korean troops attack points along the South Korean border. The U.N. Security Council calls the invasion "a breach of peace." U.S. involvement in the Koran War begins.

3. July 1957 to October 1957. Stocks fall 20.7%. There's the Suez Canal crisis and Soviet launch of Sputnik, plus the U.S. slips into recession.

4. January 1962 to June 1962. Stocks fall 26.4%. Stocks plunge after a decade of solid economic growth and market boom, the first "bubble" environment since 1929. In a classic 1962 interview, Warren Buffet says, "For some time, stocks have been rising at rather rapid rates, but corporate earnings have not been rising, dividends have not been increasing, and it's not to be unexpected that a correction of some of those factors on the upside might occur on the downside."

5. February 1966 to October 1966. Stocks fall 22.2%. The Vietnam War and Great Society social programs push government spending up 45.0% in five years. Inflation gathers steam. The Federal Reserve responds by tightening interest rates. No recession occurred.

6. November 1968 to May 1970. Stocks fall 36.1%. Inflation really starts to pick up, hitting 6.2% in 1969 up from an average of 1.6% over the previous eight years. The Vietnam War escalates. Interest rates surge; Ten-year Treasury rates rise from 4.7% to nearly 8.0%.

7. April 1973 to October 1974. Stocks fall 48.0%. Inflation breaks double-digits for the first time in three decades. There's the start of a deep recession; unemployment hits 9.0%.

8. September 1976 to March 1978. Stocks fall 19.4%. The economy stagnates as high inflation meets dismal earnings growth. Adjusted for inflation, corporate profits haven't grown for eight years.

9. February 1980 to March 1980. Stocks fall 17.1%. Interest rates approach 20.0%, the highest in modern history. The economy grinds to a halt; unemployment tops 10.0%. There's the Iran hostage crisis.

10. November 1980 to August 1982. Stocks fall 27.1%. Inflation has risen 42.0% in the previous three years. Consumer confidence plunges, unemployment surges, and we see the largest budget deficits since World War II. Corporate profits are 25.0% below where they were a decade prior.

11. August 1987 to December 1987. Stocks fall 33.5%. The crash of 1987 pushes stocks down 23.0% in one day. There is no notable news that day; historians still argue about the cause. A likely contributor was a growing fad of "portfolio insurance" that automatically sold stocks on declines, causing selling to beget more selling–the precursor to the fragility of a technology-driven marketplace.

12. July 1990 to October 1990. Stocks fall 19.9%. The Gulf War causes an oil price spike. A short recession follows. The unemployment rate jumps to 7.8%.

13. July 1998 to August 1998. Stocks fall 19.3%. Russia defaults on its debt, emerging market currencies collapse, and the world's largest hedge fund goes bankrupt, nearly taking Wall Street banks down with it. Strangely, this occurs during a period most people remember as one of the most prosperous periods to invest in history.

14. March 2000 to October 2002. Stocks fall 49.1%. The dot-com bubble bursts and 9/11 sends the world economy into recession.

15. November 2002 to March 2003. Stocks fall 14.7%. The U.S. economy puts itself back together after its first recession in a decade. The military preps for the Iraq war. Oil prices spike.

16. October 2007 to March 2009. Stocks fall 56.8%. The global housing bubble bursts, sending the world's largest banks to the brink of collapse. It is the worst financial crisis since the Great Depression.

17. April 2010 to July 2010. Stocks fall 16.0%. Europe hits a debt crisis while the U.S. economy weakens. Double-dip recession fears are raised.

18. April 2011 to October 2011. Stocks fall 19.4%. The U.S. government experiences a debt ceiling showdown, U.S. credit is downgraded, and oil prices surge.

19. June 2015 to August 2015. Stocks fall 11.9%. China's economy grinds to a halt; the Fed prepares to raise interest rates.

**Source: This chart was excerpted from "Inflation Is Real", by Harold R. Evensky, CFP®, AIF®, Chairman of Evensky & Katz / Foldes Financial Wealth Management, (*Newsletter*, Volume 8, No. 5 - November 2015), www.EK-EF.com**

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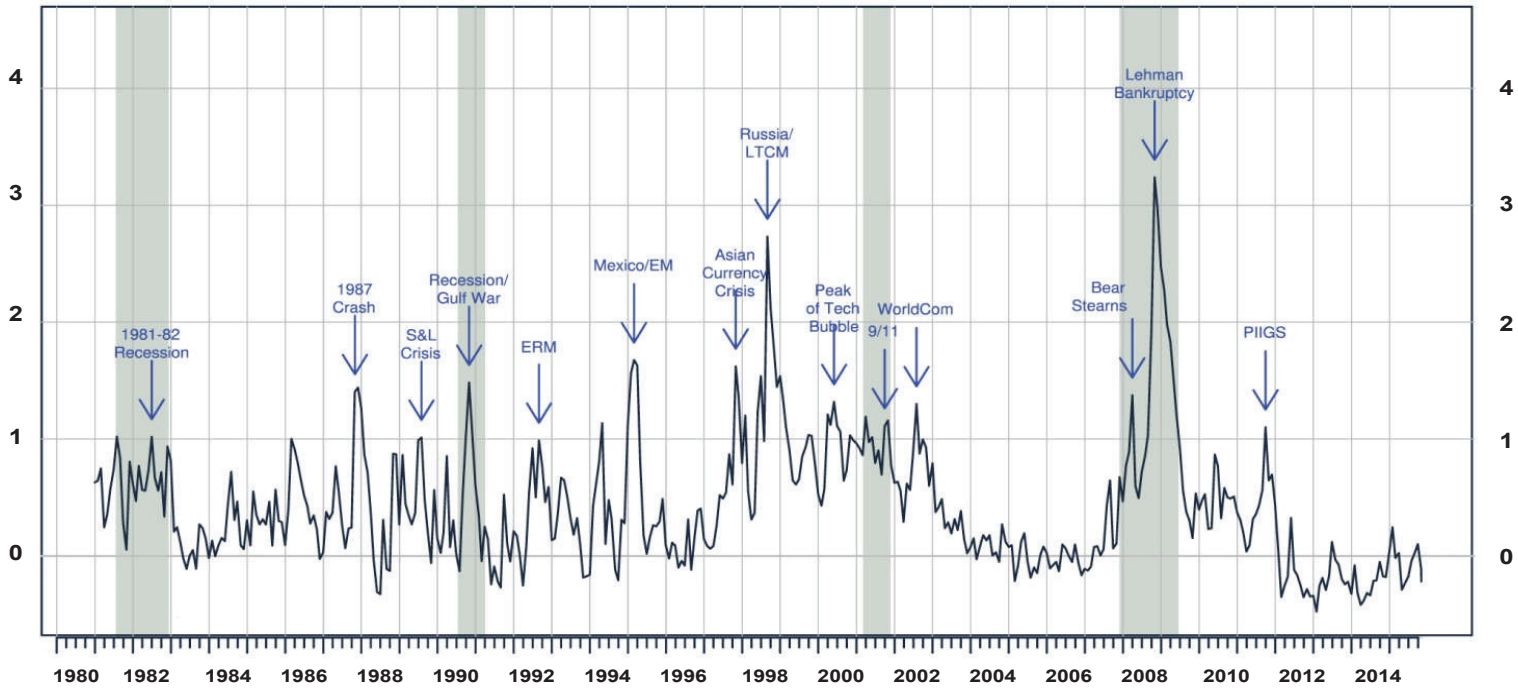
# MONTHLY RISK AVERSION INDEX (RAI)
## RISK DECREASES – STILL NEAR ALL-TIME LOWS

**Note: The Risk Aversion Index combines ten market-based measures including various credit and swap spreads, implied volatility, currency movements, commodity prices and relative returns among various high- and low-risk assets.**

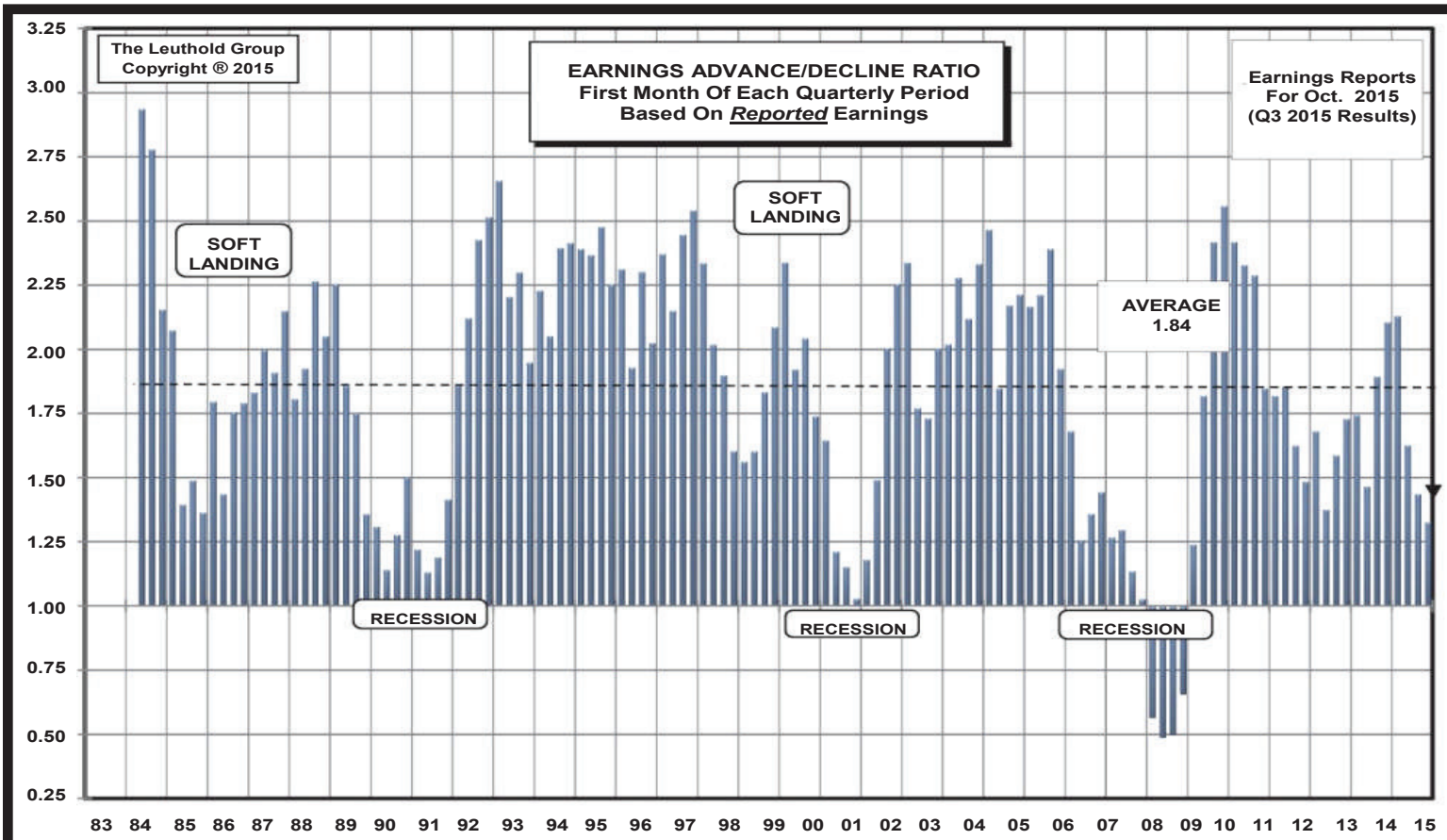



As of: November 6, 2015



Source: The Leuthold Group, LLC, *Perception Express*, November 6, 2015, http://leuth.us/bond-market






As of: November 6, 2015

Source: The Leuthold Group, LLC, *Perception Express*, November 6, 2015, http://leuth.us/market-internals

Understanding The Income Taxation Of Mutual Fund Distributions, *continued from page 1*

2. The Net Asset Value (NAV) or share price of a mutual fund is reduced by the amount of the distribution. If reinvested, this means the investor will own more shares at a lower price, but the market value of the account remains the same. If the distribution is received in cash, then the mutual fund shares will have a lower price, which will total the original value minus the amount of the cash distribution.

3. The cost basis of the mutual fund is increased by the amount of the reinvested distribution because reinvested distributions are treated as a new purchase. It is important to remember to keep track of reinvested distributions for the life of the holding. This information will be needed when shares are redeemed.

4. Reinvested distributions are treated as a purchase for wash sale purposes. Wash sale rules discourage people from selling securities just to take a tax loss. The rules disallow the loss from selling shares of a security if an investor buys shares of the same (or similar) security within 30 days of the sale.

It is often asked, "Why do we make a capital gain distribution when the NAV for the fund is flat to down for the year?" Actually, it may be the best time to make a distribution. Remember, that mutual fund companies are trying to sell the companies they own after they have gone up, and then use that money to buy stock in companies that haven't gone up yet (the time to harvest the crop is after it has stopped growing). In effect, the managers should be making distributions and paying taxes after the good years, not during them. It may be a little counterintuitive, but it makes sense when one thinks about it. Even though the Internal Revenue Service (IRS) operates on a one-year calendar cycle, the economy and the markets do not; therefore, nor should investors since they are long-term owners.

The bottom line is, if a fund company makes money from buying stocks low and selling them high, investors will pay taxes on the gains. It's simply a matter of whether an investor pays the tax in the years money is made, or in the years that they don't.



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Dow Power: The Dow Jones Industrial Average, *continued from page 1*

to almost every American; among them are: AT&T, Coca Cola, Exxon, General Electric, American Express, Home Depot, IBM, Intel, McDonalds, Merck, Microsoft, Proctor & Gamble, and Wal-Mart.

The Dow is the most closely followed index, perhaps because it was the first, and because its handful of blue chip companies reflect stock market activity with surprising precision. The companies that make up the Dow are more financially stable by virtue of their size and because of public interest in their shares. A corporation must also meet minimum qualifications, such as capital investment and trading activity in its shares. In addition, most of the companies that make up the Dow are listed on the New York Stock Exchange (NYSE).

It has been suggested that fluctuations in the Dow precede those in the economy because investors buy shares of stock in order to take advantage of future profit potential and will bid up stock prices when that potential looks promising. Generally speaking, many believe the broad line of industrial companies represented by the Dow enjoys an improvement in earnings directly reflecting the expansionary phases of the business cycle, but may suffer a decline in earnings when the economy slips into a recession.

As a result of the corporations making up the Dow effectively representing the backbone of industrial America, their fortunes are closely tied to swings in the business cycle. Thus, the Dow's movement potentially shifts in anticipation of the cycle as investors gauge not only the profit potential of these corporations, but also future cyclical prospects for the economy as a whole.



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## ABOUT THE FEDERAL RESERVE BOARD

### A QUOTE FROM U.S. GLOBAL

U.S. Federal Reserve Board (Fed) officials have recently been drawn from just two backgrounds—the first: academics and the second: former employees of Goldman Sachs. The announcement that Neel Kashkari will become president of the Federal Reserve Bank of Minneapolis marked the third Goldman Sachs alumnus in a row to be picked to become a Fed bank president. Of the 17 Fed officials in office next year, all but three will have professional backgrounds as academics or been employed by Goldman Sachs. This poses a serious risk of groupthink (like thinking) within the Fed. The narrow range of backgrounds may lead to a central bank that is thin on expertise when it comes to the responsibilities that extend beyond monetary policy.

**Source: This article was excerpted from "The Bullish Case for Aussie Gold", by Frank Holmes, CEO and Chief Investment Officer, U.S. Global Investors, (*Advisor Alert*, November 13, 2015), www.usfunds.com**



PULSE

# 2015 PERFORMANCE YEAR-TO-DATE

## January 1, 2015 to October 31, 2015
## (10 months)

| | Year-to-Date Total Return |
|---|---|
| Consumer Price Index (Inflation) | 1.29% |
| 90-Day Treasury Bills Index-Total Return | 0.02% |
| Barclays Aggregate Bond Index-Total Return | 1.14% |
| HFRX Global Hedge Fund Index | -1.63% |
| S&P 500 Index (U.S. Stock Market) | 2.70% |
| MSCI EAFE Index (Developed Foreign Equities) | 2.68% |
| MSCI Emerging Market Index (Equities) | -9.22% |
| Newedge CTA Index (Managed Futures) | -1.23% |
| Dow Jones–UBS Commodity Index-Total Return (USD)** | -16.20% |
| Dow Jones U.S. Real Estate Index-Total Return (USD)** | 1.22% |
| Gold Bullion | -3.61% |

Compound and Total Returns include reinvested dividends. Newedge Index is equally-weighted.
** USD = U.S. Dollar

Source: Bloomberg Investment Service

As of: October 31, 2015

## SECULAR BEAR MARKET WATCH

**April 1, 2000 to October 31, 2015**
**(15 years and 7 months)**

| | Annual Compound Return | Total Return |
|---|---|---|
| Consumer Price Index (Inflation) | 2.13% | 38.92% |
| 90-Day Treasury Bills Index-Total Return | 1.68% | 29.69% |
| Barclays Aggregate Bond Index-Total Return | 5.41% | 127.28% |
| HFRX Global Hedge Fund Index | 2.50% | 47.01% |
| S&P 500 Index (U.S. Stock Market) | 4.10% | 87.11% |
| MSCI EAFE Index (Developed Foreign Equities) | 3.27% | 65.22% |
| MSCI Emerging Market Index (Equities) | 6.20% | 155.31% |
| Newedge CTA Index (Managed Futures) | 5.26% | 122.52% |
| Dow Jones–UBS Commodity Index-Total Return (USD)** | -0.76% | -11.26% |
| Dow Jones U.S. Real Estate Index-Total Return (USD)** | 11.02% | 410.13% |
| Gold Bullion | 9.47% | 309.99% |

* Compound and Total Returns include reinvested dividends. MSCI Indexes do not include dividends prior to 2002. Newedge Index is equally-weighted.
** USD = U.S. Dollar

Source: Bloomberg Investment Service

As of: October 31, 2015



Note: During Secular Bear markets U.S. Stocks have historically returned a little more than inflation or a little less than inflation—plus or minus 1.50%—and generally last between 15 to 25 years. The last Secular Bear market (1966 to 1982) lasted 17 years and underperformed inflation by approximately one-half of one percent per year. The other Secular Bear markets since 1900 were 1901 to 1920 and 1929 to 1949. In both cases, the U.S. Stock market outperformed inflation by approximately 1.50% per year. All of the aforementioned performance numbers are pre-tax.

The performance of the U.S. Stock market so far in the current period (April 1, 2000 to the present) certainly appears to indicate that we are in a Secular Bear market. Long-term returns (over the next 10 years) for the S&P 500 will probably be slightly worse than the last 15 years and 7 months. Current 10 year normalized P/Es (long-term valuations) indicate approximate annual compound returns of slightly less than 3.00% over the next 10 years. Of course during the next 10 years, returns during various periods will be significantly higher and lower than the expected return. For example, the more the stock market rises in the near term, the less returns after that period will be and vice versa.

# 21ST CENTURY DOES NOT PROMISE AS HIGH RETURNS AS 20TH DID

## Forward-Looking Real Returns Are Low For Both Main Asset Classes

**By Louis P. Stanasolovich, CFP®, CCO, CEO and President of Legend Financial Advisors, Inc.® and EmergingWealth Investment Management, Inc.**

The top chart below indicates long-term forecasted real (after inflation) returns for stocks and bonds for the next ten years moving forward since 1900. Obviously, the numbers as of the end of 2014 are some of the lowest in history as indicated by the low percentile number.

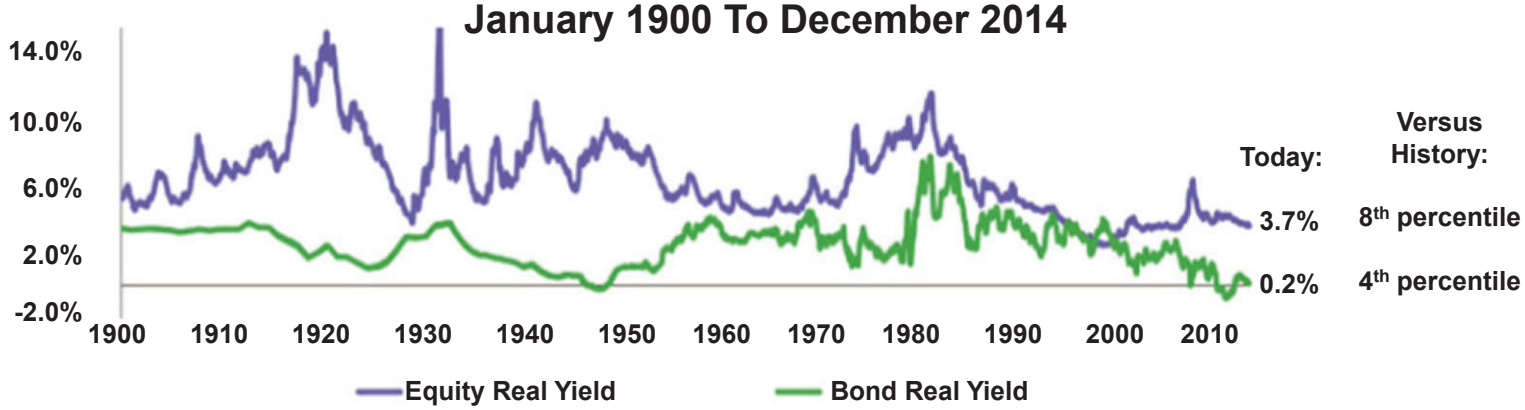
Also, the 60.0% equities and 40.0% bonds (bottom chart) forecasted return number indicated is the lowest in history.

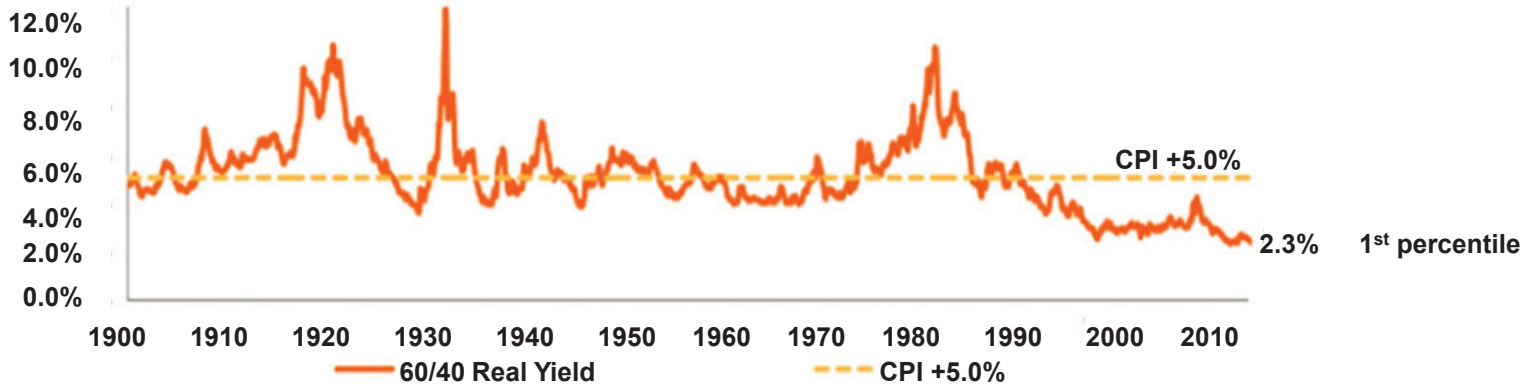
Passive (index management) on a buy and hold basis could be disastrous to one's portfolio.



## EXPECTED REAL RETURN OF U.S. STOCKS, BONDS AND A 60/40 PORTFOLIO

### January 1900 To December 2014




**Concluding Thoughts: Valuations are high and forward 10-year annualized returns look to be in the 2.0% to 4.0% range (returns annualized before inflation is factored in). Therefore, the S&P 500 is likely to decline significantly during the next recession to obtain such low long-term returns.**

Stocks are represented by the Standard & Poor's 500 Index since 1957, and bonds are represented by long-dated Treasuries, The 60/40 Portfolio is 60.0% Stocks and 40.0% bonds. The equity yield is a 50/50 mix of two measures: 50.0% Shiller E/P +1.075 and 50.0% Dividend/Price +1.5%. Bond yield is 10 year real Treasury Yield over 10 year inflation forecast as in Ilmnen (2011). Scalars are used to account for long-term real Earnings Per Share (EPS) Growth.

As of: August 31, 2015



Source: AQR, Robert Shiller's Website, Kozicki-Tinsley (2006), Federal Reserve Bank of Philadelphia, Blue Chip Economic Indicators, Consensus Economics via CMG Capital Management Group, Inc. *On My Radar*, September 11, 2015, www.cmgwealth.com

## HISTORICAL VALUATIONS, GROWTH VERSUS VALUE
## U.S. LARGE, MID AND SMALL CAP STOCKS

**All growth stock and value stock style categories, except small growth and mid-growth, appear expensive when compared to the Historical Averages (1982 to date) and the Percent Above/Below Historical Average Valuation sections in the chart below. Large, Medium, and Small Growth Stock categories again appear cheaper relative to the Value categories than the historical averages as evidenced by the Today's G/V* Ratio versus the Historical Average G/V* Ratio.**

| | Median Price-To-Earnings (P/E) | | Historical Averages 1982 to Date | | Percent Above/Below Historical Average Valuation | | Today's | Historical Average | 2000 Extreme |
|---|---|---|---|---|---|---|---|---|---|
| | Growth Stocks | Value Stocks | Growth Stocks | Value Stocks | Growth Stocks | Value Stocks | G/V* Ratio | G/V* Ratio | G/V* Ratio |
| Large-Cap | 20.3x | 12.9x | 19.8x | 10.7x | 2.0% | 20.0% | 1.57 | 1.97 | 5.80 |
| Mid-Cap | 22.8x | 13.4x | 23.3x | 11.9x | -2.0% | 13.0% | 1.70 | 2.09 | 9.30 |
| Small-Cap | 25.0x | 13.3x | 27.5x | 12.0x | -9.0% | 11.0% | 1.88 | 2.45 | 12.50 |

* Growth To Value

The more reasonable valuations didn't stick around for very long—Growth still relatively undervalued.

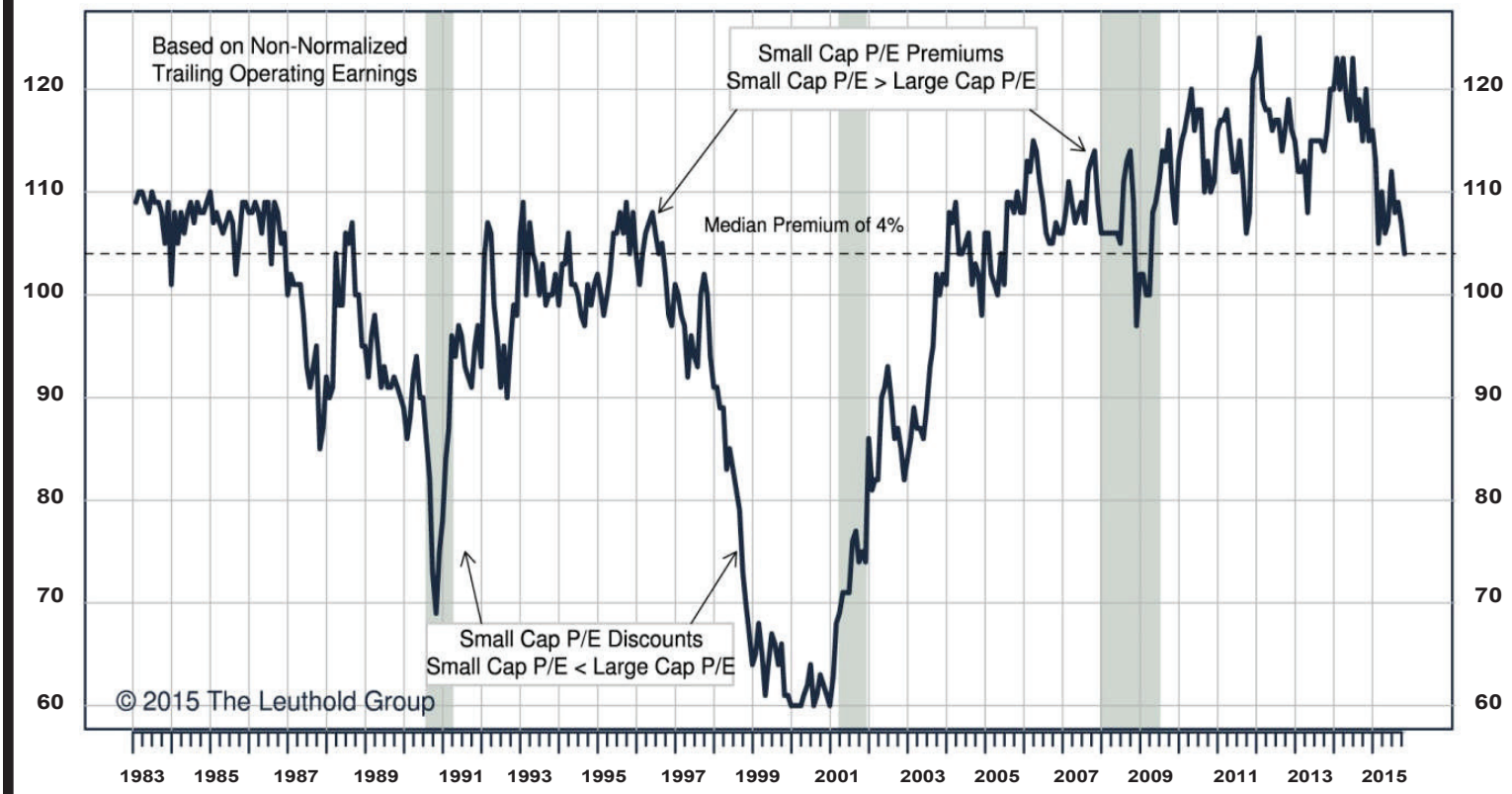
As of: November 6, 2015



Source: The Leuthold Group, LLC, *Perception Express*, November 6, 2015, http://leuth.us/market-internals



## SMALL CAP TO LARGE CAP HISTORICAL PRICE TO EARNINGS (P/E) RATIO
## Small Caps Are Still More Expensive – 9.0%

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Source: The Leuthold Group, LLC, *Perception Express*, November 6, 2015, http://leuth.us/market-internals

## THE FED, DRAGHI AND THE EUROPEAN CENTRAL BANK (ECB)

**By Stephen B. Blumenthal, Founder and CEO, CMG Capital Management Group, Inc.**

This is how extreme the European Market Bond Market pricing has become (as of November 15, 2015):

1. In Germany, the one year government bond yield closed on November 12, 2015 at -0.33%;

2. The two-year bond closed at -0.35%;

3. The seven-year is the first maturity that pays a positive yield at +0.12%;

4. The ten-year is +0.61%.

Now Compare the U.S. Treasury securities:

1. The two-year is +0.87%;

2. The five-year is +1.71%; and,

3. The ten-year is +2.33%.

Would you rather own U.S. 10-year Treasury notes yielding 2.33% or German 10-year bonds yielding 0.61% or 10-year Italian bonds (currently rated BBB by the S&P–the lowest possible investment grade rating) yielding 1.63%?

The U.S. is contemplating raising interest rates–it appears (66.0% probability) likely in December. Europe, though, is going the other way. As Mario Draghi, president of the European Central Bank, just signaled, the European Central Bank (ECB) is likely to continue with negative interest rates and extend and enlarge their own Quantitative Easing (QE), by printing Euros and buying bonds and other publically-traded investment assets.

Such moves don't stand in isolation. There is a ripple effect both locally and globally. Since the European Union (EU) is a trade union, other European countries are forced to depress their interest rates (to depress their currencies) in order to compete on trade: Worldwide–Denmark, Sweden, Switzerland, Australia and New Zealand are all easing. In order to position themselves more favorably (also to compete for a greater share of global trade), China too is easing and so are India, Korea, Indonesia, Hungary, Poland, Russia, Turkey and Mexico. Japan is likely to jump right back into the mix in the near future. In short, we are in the middle of a global currency war.

Zero bound interest rates are no longer simulative enough. Negative interest rates are new a reality. Globally, about $1.9 trillion value of intermediate-term bonds are now trading at negative interest rates (Source: Bloomberg).

Madness! Yet, that number is probably going to go higher. Globally, countries and corporations have borrowed from the future and spent for today. The economic system is in for an unstable state in both the intermediate term and long run. A stronger U.S. Dollar means the payback on the $9.6 trillion in U.S. Dollar denominated borrowings by foreigners goes up. (To put this in perspective, the U.S. housing crisis was only $1 trillion.) They took those low interest loans when U.S. interest rates were lower than their own borrowing rates and they believed then that U.S. Federal Reserve Board (Fed) policy would further depress the U.S. Dollar. We were in the early days of QE (2010) then. They had not yet started their own QE programs.

That dynamic has flipped. The U.S. Dollar is up approximately 25.05 in the last two years and another 15.0% move makes the loan payment due, $11 trillion. It was a bad bet. Some borrowers (many?) will chose to default. As a result, a condition of currency wars combined with underlying systemic instability exists and there will likely be consequences. Thus, we investors must focus on risk protection.

Global recession looks highly-probable. More QE is likely to come. That may further push recession down the road. We don't know for sure though.

The Economist noted that approximately 60.0% of the world's population and economic output is linked to the U.S. Dollar (Some foreign currencies are pegged in some form to the U.S. Dollar). Some want to de-link as the stronger U.S. Dollar makes their exports more expensive.

In the late 1920s, there was a melt-up in the U.S. market. Global capital was racing to the United States. Confidence was lost. Both the currency and the markets melted up. We know what soon followed (The Great Depression). A repeat is probably not likely, however, global capital flows matter. Despite an overvalued market, it could become more overvalued. Eventually, the currency wars of the late 1920s came back to bite the United States. Recession and Depression followed. The U.S. economy, unlike yesteryear, is now dependent on the world economy.

**Source: This article was excerpted from "Poking at the Beehive", by Stephen B. Blumenthal, Founder and CEO, CMG Capital Management Group, Inc., (*On My Radar*, November 13, 2015), www.cmg-wealth.com**



PULSE

## ON THE FEDERAL RESERVE RAISING INTEREST RATES
## A QUOTE FROM U.S. GLOBAL

Historically, Federal Reserve tightening cycles typically unfold in two distinct phases. The first phase begins with a surprise moment where the reality of rate hikes sinks in and bonds sell off. The second phase is one where short-term rates grind higher, but long-term bond yields stabilize or even decline. For example, in the last tightening cycle, bond investors suffered losses totaling 5.4% between March and May 2004. However, by the time the Federal Reserve hiked rates for the first time in June 2004, U.S. Treasuries had already resumed their bull market.

**Source: This article was excerpted from "The Bullish Case for Aussie Gold", by Frank Holmes, CEO and Chief Investment Officer, U.S. Global Investors, (*Advisor Alert*, November 13, 2015), www.usfunds.com**



PULSE

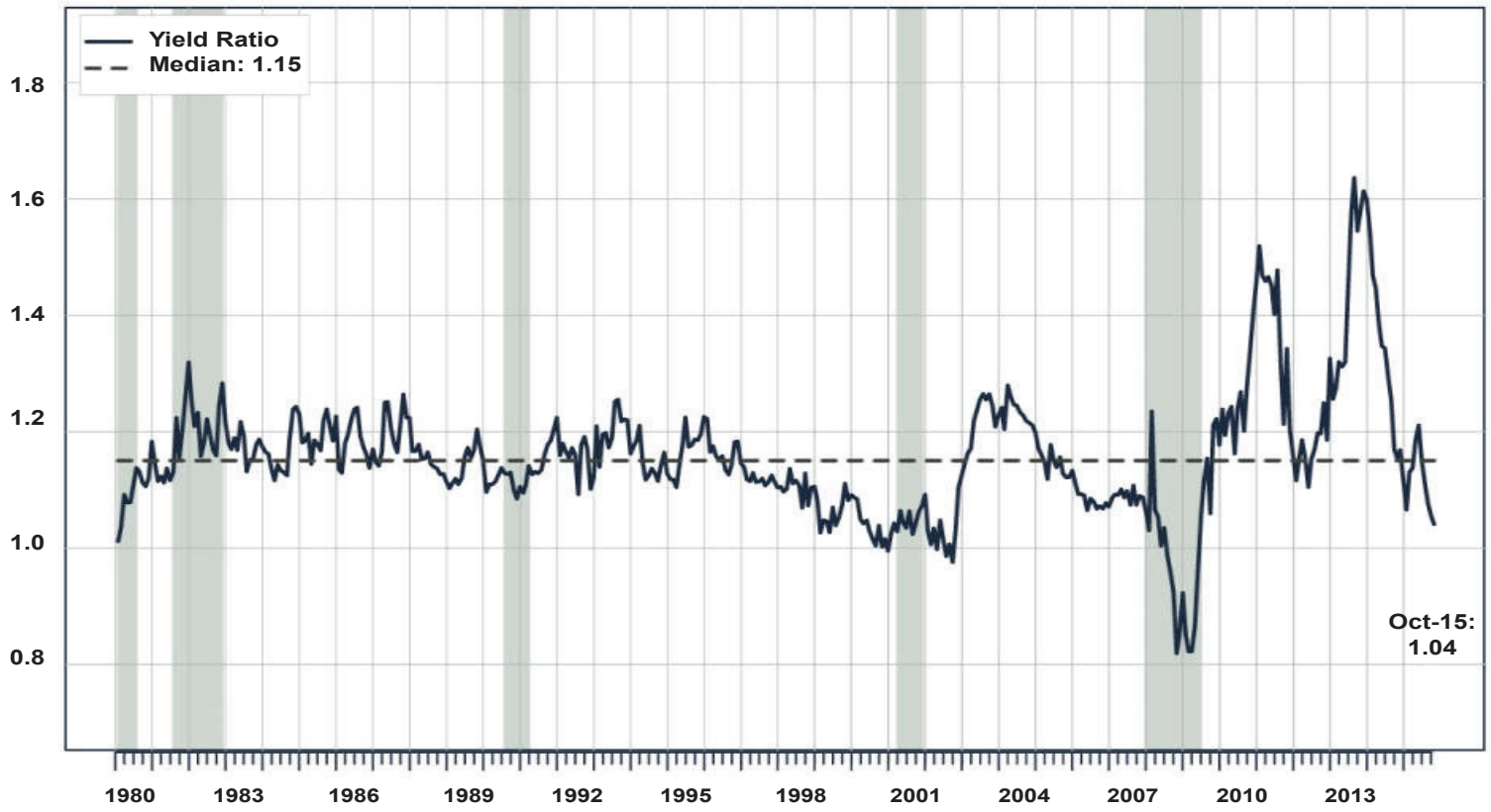
## BARCLAYS U.S. HIGH YIELD BOND MINUS TREASURY BOND YIELD

### High Yield Bond Yields Fall Back


As of: November 6, 2015


Source: The Leuthold Group, LLC, *Perception Express*, November 6, 2015, http://leuth.us/bond-market


## MUNIS TAX EQUIVALENT YIELD / BARCLAYS U.S. CORPORATE BOND YIELD




As of: November 6, 2015


Source: The Leuthold Group, LLC, *Perception Express*, November 6, 2015, http://leuth.us/bond-market

However, if you guessed False, you're also right. That's because there are many ways to compute P/E ratios. Any given stock can have a handful of different P/Es depending on which definition you use.

**Comparing Apples To Apples:**

Analyzing a stock's P/E can provide clues to its relative value, but it can also lead an investor astray if invalid comparisons are made. In addition to a trailing 12 month's P/E ratio, there is a forward P/E ratio. With this type of ratio, analysts estimate a company's earnings for the coming year and determine "forward" P/E–also known as a "leading" or "projected" P/E.

Robert Shiller, renowned Yale professor, has also compiled a P/E ratio called the P/E 10 (This figure is utilized for the S&P 500 as a whole, but not individual stocks.), which has often been referred to and discussed at great length over the last decade or so. P/E 10 utilizes earnings of the S&P 500 for the past 10 years, which are then adjusted for inflation to the present totaled and then divided by the present price of the S&P 500. The resulting figure provides a more accurate depiction of the long-term value of the stock market whereas other P/E methods focus on very short-term results and can be heavily influenced by exceptionally low or high earnings periods. Many academics and professionals also believe that professor Shiller's P/E 10 figure provides a more accurate forecast of future returns over the next decade than other P/E ratios.

When you assess P/E, it's usually best to focus on trailing net earnings. Why? Analyzing solid historical data is usually more reliable than comparing forward P/Es estimated by analysts (a fluid number that's subject to revisions). This is especially true if your goal is to determine how a particular stock has stacked up against its peers in terms of market valuation.

It is also important to compare P/E between stocks in the same industry. Using P/E to evaluate stocks in two different sectors can result in a faulty analysis.

**Rethink "Cheap" Stocks:**

Using P/E valuation methods when analyzing stocks can lead to misinformation as well. It's easy to scan the business section of the newspaper for stocks with a low P/E. Is a stock a good buy if it is cheap? Not always. It's important to remember that a stock with a low P/E is cheap for a reason.

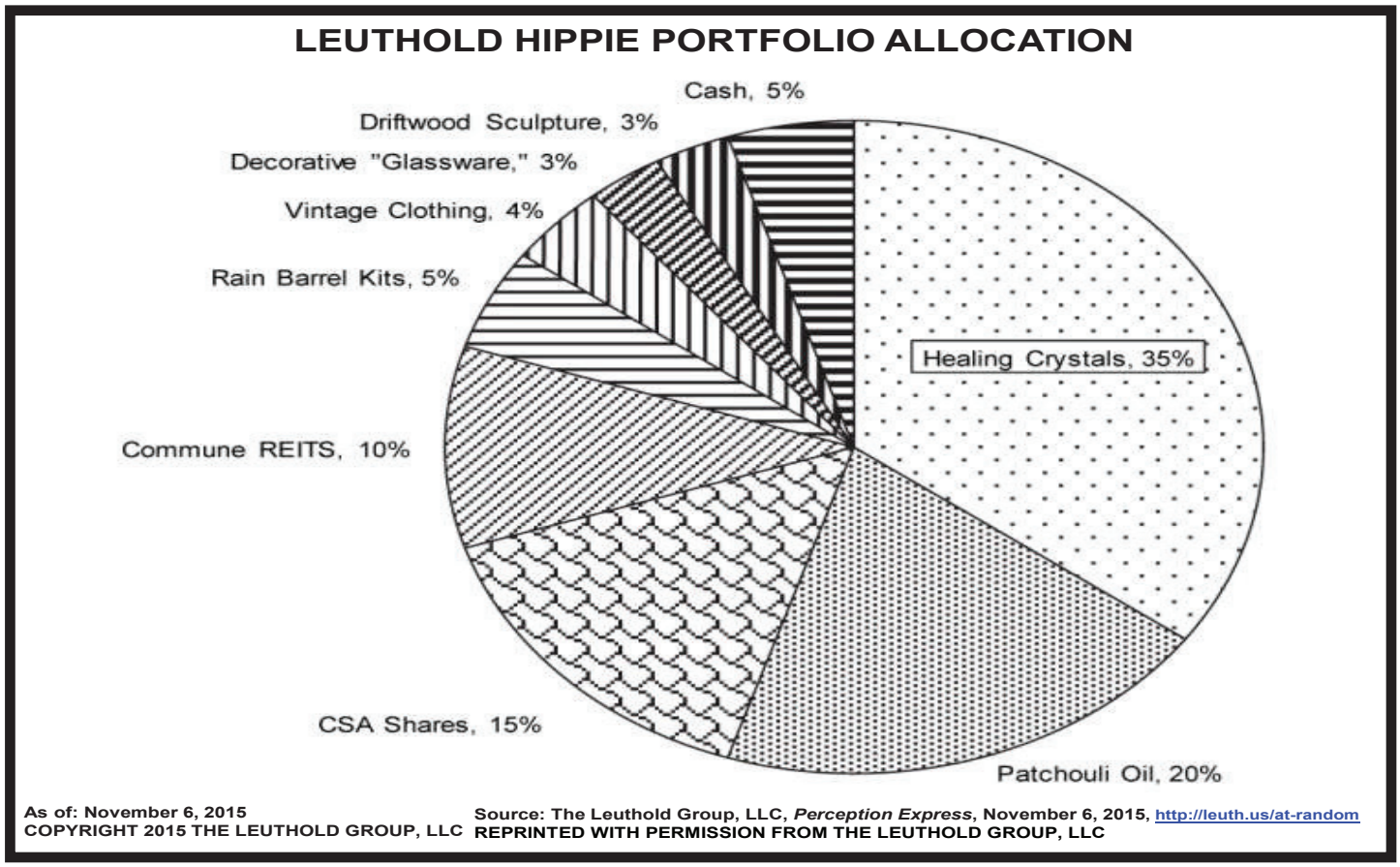
There are many reasons why a stock's P/E might fall below its industry average. Wary investors may expect the company to hit a bumpy patch soon, from a seasonal downturn in sales to an unfavorable outcome to pending litigation. Also, some stocks simply can't shake off a bad perception, especially if the company has restated earnings in recent years or institutional investors lack confidence in its management.

Above all, it's best to avoid viewing a P/E in isolation. It is important to consider a stock's earnings multiple in the context of the company's historical growth rate, its industry's prospects and the role of macroeconomic factors such as inflation and interest rates.



PULSE

# JUST FOR FUN



# LEGEND FINANCIAL ADVISORS, INC.® & EMERGINGWEALTH INVESTMENT MANAGEMENT, INC.'S

## INVESTMENT MANAGEMENT SERVICES

Legend Financial Advisors, Inc.® (Legend) and EmergingWealth Investment Management, Inc. (EmergingWealth) offer Personalized Investment Management Services to individuals and institutions. Investment portfolios are developed to match the client's return and risk requirements, which are determined by the clients' completion of a Risk Comfort Zone Questionnaire, with the guidance of a Legend Wealth Advisor or EmergingWealth Advisor, respectively. Each type of investment portfolio is managed to achieve the short, intermediate and long-term investment objectives of the client, as may be applicable.

## INVESTMENT PROCESS

**Investment Portfolios:**

Unlike most financial advisory firms that offer one style of investment or portfolio type, we offer a wide array of investment portfolios that usually fit with the large majority of client needs. If necessary, we will create customized solutions as well. For the types of investment portfolios, please see our Investment Portfolios, Potential Return and Risk Spectrum Chart on the next page. For a detailed description of our portfolios, please contact Louis P. Stanasolovich, CFP®, founder, CCO, CEO and President of both firms for a confidential discussion at (412) 635-9210 or e-mail us at legend@legend-financial.com.

**Investment Research:**

Our Investment Committee performs extensive research to identify opportunities, mitigate risks and structure investment portfolios. Emphasis is placed on developing portfolios that maximize the potential return relative to the amount of risk taken.

In-depth due diligence including face-to-face interviews in many instances with portfolio managers for open-end mutual funds is performed on each investment we select for a portfolio. Factors (both from a qualitative and quantitative standpoint) that we conduct a thorough analysis of each investment include, but is not limited to, liquidity (including the primary investment and/or the underlying investments, if utilizing pass through vehicles such as open-end mutual funds or exchange-traded products), income taxation, all related costs, return potential, drawdown potential (historical declines from peak-to-trough), volatility and management issues (Anything having to do with the management team of a stock, open-end mutual fund or an exchange-traded product.).

All portfolios for EmergingWealth are subadvised by Legend.

**Client Education:**

Education is very important to us. We are dedicated to educating each client about the different investment portfolio types and how they relate to market volatility, time horizons, and investment returns. It is our goal to ensure that the client understands and agrees with our investment philosophy. Furthermore, we assist each client in selecting a risk tolerance level with which they are comfortable. Ultimately, an investment portfolio is designed to meet the client's objectives.

## PERFORMANCE REPORTING

Many investment firms only offer monthly brokerage statements, which provide minimal information; typically only account and investment balances. We, on the other hand, provide detailed quarterly reports that outline performance, income and management fees (among other items) in a simple, easy-to-read report. In addition, each performance report is sent with an extensive index page that illustrates the investment environment during the reporting period.

## FEES

To find out more about the fees for either Legend or EmergingWealth's Investment Management services, please contact Louis P. Stanasolovich, CFP®, founder, CCO, CEO and President of both firms for a confidential discussion at (412) 635-9210 or e-mail us at legend@legend-financial.com.

# LEGEND FINANCIAL ADVISORS, INC.®, AND EMERGINGWEALTH INVESTMENT MANAGEMENT'S INVESTMENT PORTFOLIOS, POTENTIAL RETURN AND RISK SPECTRUM