CAPSTONE PACIFIC
INVESTMENT STRATEGIES INC

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The Capstone Quarterly

As we head into the new year we are grateful for all the client relationships we have formed over the years. We look forward to another year of working with some of the best clients ever. The financial industry is one of constant change, but one thing that has remained consistent for us here at Capstone Pacific is that we remain committed to putting our clients' best interests first.

Bryce's Point of View

-By Bryce Pease, CFP®, Chief Investment Officer

The investment markets were anything but uneventful in 2016. Perhaps most noticeable of the events of 2016 was the US presidential election on November 8. Investors around the world waited on the edge of their seats to see the outcome of the US election. As the election results were being tallied the night of the election, and it was becoming clearer that Donald Trump would be the next president of the United States, the stock markets started to crash. However, by the time the market closed on November 9, the US stock markets had staged a stunning recovery, and have been jumping up since. Instead of the stock markets taking a beating with a Trump win, it was the bond market that got hammered. See the chart below:

S&P 500 vs. AGG Nov. 2016-Dec. 2016 © 2016 Worden Brothers, Inc.

This is a picture of how stocks and bonds have performed since November 2016. Stocks are the top line, bonds are the bottom line, the red arrow points to the Election Day.

The above chart is comparing the US stock market as measured by the S&P 500 Index to the exchange traded fund AGG which tracks the Barclays Capital U.S. Aggregate Bond Index. The stock market (the line on top) has been jumping dramatically since the election and the bond markets (the line on the bottom) have been falling since the election. In other words, while US stocks have been doing just fine all of a sudden, now it's bonds that have been holding investors back.

The recent drop in the bond markets just adds to the frustration of diversified investors. While the stock markets have been going up since the election, this hasn't been the case for the last year and a half. See the chart below for the S&P 500 Index going back to June of 2015:

S&P 500 June 2015—December 2016 2016 Worden Brothers, Inc.

The green arrow is approximately June 2015 and the red arrow is around the time of the election. What you can see here is that the US stock market went nowhere for 18 months, with some gut-wrenching losses along the way. All the current gains in in the S&P 500 Index over the last year and a half have come in the last couple months.

The bottom line is that diversified investors who have had money in stocks and bonds have felt like they have been going in circles and were held back by their bonds when the US stock markets took off in November 2016. We have a couple thoughts on this.

The first thought is that we think the US stock market may finally be entering a sustainable trend to the upside. Research we follow that tracks supply and demand in the financial markets shows that demand is increasing for US stocks. If demand continues to increase, our plan is to participate in this uptrend in the stock market as long the demand persists.

The second thought regarding recent market action is that bond values may have dropped too fast too quickly. What can hurt quality bond values are rising interest rates. Interest rates jumped up after the Trump election, which caused many bond markets to fall. Our research suggests that bonds are oversold and that interest rates may be levelling off for now. We are watching our bond funds very closely and may be moving some of them to cash if things continue to fall. However, it appears that bond rates may have stabilized for the time being and we could see some recovery in the bond market.

In addition, we think there are some sectors with potential to grow in the new political environment. This is not a political comment and we are not saying whether we agree or not with this approach to economic growth, but Trump has said he is going to be spending some serious money on infrastructure. One possible approach we are currently evaluating is to look to position toward sectors that could benefit from infrastructure spending such as industrials, defense and materials.

To wrap up, the good news is we think the stock markets may have finally entered a sustainable trend while the bond markets may be stabilizing after a sharp sell-off. In addition, we think there are some sectors with some potential to grow in the new economic and political environment

Thank you for your patience in a difficult and challenging market. While there is no less uncertainty in the world, we see brighter things on the horizon for diversified investors. We continue to fine tune our strategies and hone our approach to adjust to the changing times and market conditions. We will see what 2017 has in store.

Casey's Corner

-By Casey Morris, CFP®

In my work at Capstone there is a question that seems to come up often and it has to do with IRA withdrawals and rollovers. The rules have changed on this not all that long ago, so we feel it's worth reviewing some of the aspects of IRA rollover rules here.

Currently you can transfer your IRAs between IRAs as many times as you want without taxes or penalties, as long as it's a direct transfer and goes directly to the custodian and not you. However, if you are issued a check in the rollover process, the rules are different. You can only do one of these rollovers once per 12-month period. Part of this rule has not changed because it's always been the case that you can only do one rollover per year (where you take actual possession of the funds). What's changed is that you used to be able to do this once per IRA per 12-month period, but now you can only do it once per year for only one of your IRAs.

How this could hurt an investor is let's say you took money out of an IRA and put it back in another IRA as a rollover (currently you have 60 days to do this) and then later on in the same 12-month period you take money out of another IRA you own and attempted to put it back into an IRA as a rollover—that second transaction would be considered a distribution and not a rollover and would be subject to taxes and penalties.

The point we want to emphasize is be very, very careful when doing an IRA rollover. If you go wrong on this, you could really hurt yourself in taxes and penalties as well as future tax deferred growth. Please don't hesitate to contact us if you have any questions about how IRA rollovers work. See www.irs.gov for more information.

The Planning Perspective

-By Jon Teran, CFP®

I had the chance to participate in one of the Financial Planning Days offered by Certified Financial Planner Board of Standards, Inc.®, Finanial Planning Association®, the Foundation for Financial Planning and the US Conference of Mayors. Financial Planning Days offer free no strings attached one-on-one counseling for attendees who might otherwise not be able to afford financial plannig services. While the meetings were generally brief due to time constraints, a common question kept coming up—"What should I prioritize?" Many of the folks I met with asked me about which financial planning matters they should focus on first. Saving money for a house? Putting money away for college? Start saving for retirement?

While there are some general rules of thumb in financial planning (like it's a good idea to build up emergency savings or pay off debt before buying that fancy sports car), financial planning really comes down to very specific priorities for very specfic situations. There is no one size fits all list of priorities. So instead of relying on some pre-determined list of financial priorities put together by the latest self help guru, we think it makes more sense to engage a process when it comes to determining priorities that are right for you.

This isn't based on any fancy research or analysis, what we suggest just seems common sense after many, many conversations with clients. The steps of the process look something like this:

Gather Info → Identify Steps → Set Priorities

Rather than starting with priorities, we would suggest collecting and gathering as much information as possibe about what you are trying to accomplish. Given what's important to you, what are all the things you would like to accomplish and what are all the resources you have to accomplish those goals? Then identify all the steps you need to achieve your goals. Start by figuring out everything you hope to accomplish and all the resources you have to use to accomplish your goals, then start planning your next steps and determining your priorities.

Whether it's paying off some debt, helping your child or grandchild through school, saving for retirement, balancing your insurance needs or saving for that second home, a full-scale collection of information and resources can go a long way toward helping you determine your next steps.

Did You Know?

Did you know we have clients in other states than California? Video conferencing has made it even easier for us to share computer screens and go over reports and analyses remotely with clients. While we always prefer a face to face meeting, especially for our local clients, we still have the capability to work with clients after they move from the area or even when we are referred to someone out of state. In addition, one of the custodians we use, TD Ameritrade, can now provide secure electronic access to signatures making opening and servicing accounts remotely even easier than before.

Finally…

We are proud supporters of the Covina Rotary Fun Run; a competitive 5k run as well as one of the largest 1mile kids runs in Southern California. Last year there were over 700 runners at the event. All funds raised from the event go to benefit teachers of the Covina-Valley and Charter Oak Unified School Districts as well as other community needs. The next run is going to be held on April 29, 2017 at Covina-Valley Unified School District Field. There are all sorts of ways to get involved, from sponsorship or participating in the event itself. Please visit www.covinarotary.com for more information. Come join us on April 29 for breakfast, a run and some fun—all for a good cause.

Wishing you and your family a happy new year.

Sincerely,

The Team at Capstone Pacific

P.S. If you ever run across anyone who could use our services, we always appreciate it when you pass on our name.

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