Cypress Financial Planning, LLC

FOURTH QUARTER 2015

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Q3 Market Update

(values as of 9/30/2015; % changes for Q3, not YTD)

U.S. Stock Indices

S&P 500	1,920 (-6.94%)
Dow Jones	16,285 (-7.58%)
Nasdaq	4,620 (-7.35%)
Russell 2000	1,101 (-12.39%)

Global Stock Indices

FTSE (London)	6,062 (-7.04%)
DAX (Germany)	9,660 (-11.74%)
CAC (France)	4,455 (-6.99%)
Nikkei (Japan)	17,388 (-14.07%)
Emerging Mkts	144.64 (-8.29%)

Bond Indices (Bloomberg)

U.S. Gov't.	124.07 (+2.07%)
U.S. Corporate	136.39 (+0.64%)
U.S. High-Yld	146.83 (-5.14%)
Eurozone	135.43 (+2.78%)
Emerging Mkts	143.52 (-1.44%)

Commodities

Gold (per oz)	1,115 (-4.89%)
Silver (per oz)	14.48 (-7.69%)
Oil (WTI, barrel)	44.40 (-23.89%)

Fixed Income Yields

U.S. 2-Year Treasury	0.64%
U.S. 10-Year Treasury	2.06%
U.S. 30-Year Treasury	2.87%
U.S. High-Yield Index	8.09%

Currency Exchange Rates

Euro/Dollar	1.12
Pound/Dollar	1.51
Dollar/Yen	119.86

Knowing Your Fiduciary

In our Q1 newsletter published this January, we noted a recently-settled class-action lawsuit brought by the employees of Lockheed Martin against the company, alleging breaches of fiduciary duty within the firm's 401(k) plan. That settlement was followed by a similar one this August, this one involving 190,000 employees and retirees of Boeing, the world's second-largest defense contractor.

While the details of the cases vary slightly, both involve the use of investment advisors and funds that did not align with the best interests of plan participants, including poorly-chosen or overly expensive investment options.

The logical question for retirees everywhere is, if these issues exist at some of the largest 401(k) plans in the country (Boeing boasts roughly $48 billion in plan assets, Lockheed about $27 billion), do the participants of smaller plans have any chance of getting a fair shake? After all, across the 401(k) landscape, nearly 60% of active plans have total assets of less than $2.5 million, a far cry from the tens of billions at Boeing and Lockheed. Accordingly, the average plan can be expected to have much lower bargaining power with financial firms than the Fortune 100 companies, and theoretically much more vulnerability to breaches of duty.

Not surprisingly, the Department of Labor (DOL) has taken notice, recently issuing a proposed new fiduciary rule, which could redefine the types of investment advice that would qualify an advisor (or custodian) as owing a fiduciary duty to participants.

So, just what is a fiduciary? And how does it affect you as a 401(k) plan participant, or as an investor more generally? We've put together a quick primer, so that you can understand just who qualifies as a fiduciary, and why it matters to you.

What is the fiduciary standard?

In the investment industry, the fiduciary standard is the highest standard of care that an advisor can owe a client—whether that client is a 401(k) plan participant, an individual client, or otherwise. Generally speaking, there are two standards to which advisers can be held, roughly corresponding to two different compensation structures.

The *suitability standard* applies to investment brokers, who typically work for large investment companies (broker-dealers) and earn their compensation based on commissions from the sale of investment products. Essentially, the suitability standard requires only that the broker recommend securities that are consistent with the investing objectives and time horizon of the client. The suitability standard *does not* require that the broker put the clients' interests ahead of his or her own, and conflicts of interest often follow.

A broker may, for example, be incentivized to steer a client toward a higher-fee product instead of a lower-fee product with similar investment characteristics, simply because the broker stands to earn a higher commission from the sale of the higher-fee product. While the broker may still choose to recommend the lower-fee product, he is under no legal obligation to do so.

The *fiduciary standard*, meanwhile, typically applies to Registered Investment Advisors (RIAs), as registered with either the SEC or the state securities regulators (a distinction that depends on the size of the firm). These advisors are normally compensated via fees paid directly by the client—they are thus often referred to as “fee-only” advisors, and they generally do not earn money from product sales commissions. As mentioned earlier, the fiduciary standard also frequently applies to 401(k) plan administrators, who may or may not otherwise be in the business of giving investment advice.

Getting To Know Your Advisor

Key Questions

- ☐ How are you compensated?
- ☐ Are you a fiduciary?
- ☐ Are you a registered investment adviser (RIA)?
- ☐ What, if any, are your conflicts of interest?
- ☐ Who is your typical client?

Unlike brokers subject to the suitability standard, an advisor operating under the fiduciary standard *must* place the clients’ interests above his or her own. Any sources of compensation and potential conflicts of interest must be disclosed (often in writing), and breaches of this fiduciary duty can carry stiff penalties, including loss of professional licenses. In the investment world, the fiduciary standard is the most protective for clients, and it creates a special relationship that is rare in the business world.

That said, there is room for both approaches within the financial industry. For a given client, there are various situations where one type of advisor may be preferable over the other. The problem comes when a client *thinks* he or she is talking to an advisor who owes a fiduciary duty, when in fact there is none. In that circumstance, misunderstandings and suboptimal outcomes are likely to occur.

But, it’s complicated…

While the distinction between the two standards might seem fairly straightforward, such simplicity is of course rarely the case—if it were, then the DOL wouldn’t feel the need to issue new rules clarifying the fiduciary standard.

Most confusingly, it is possible for the same advisor to be subject to *both* the suitability standard *and* the fiduciary standard, even while working with the same client. This is most often the case with “dually registered” advisors, who operate as both RIAs *and* investment brokers. In this case, advisors will often serve in a fiduciary role when giving general advice or engaging in financial planning, but shift over to the suitability standard when it comes time to recommend investments. This “two hats” approach might seem crazy, but it’s fairly common, and it breeds significant confusion. Remember: just because someone refers to himself as an “advisor” doesn’t mean that he’ll operate as a fiduciary.

Is my financial advisor a fiduciary?

It’s hard to know unless you ask. The only way to know for sure is to thoroughly interview your advisor *before* engaging his or her services, and to have an open dialogue with them. First and foremost, it’s important to understand how your advisor is being compensated. If your prospective advisor earns commissions from product sales, ask how that might affect the advice they give. If their answer seems unsatisfactory, then you may want to consider interviewing another advisor.

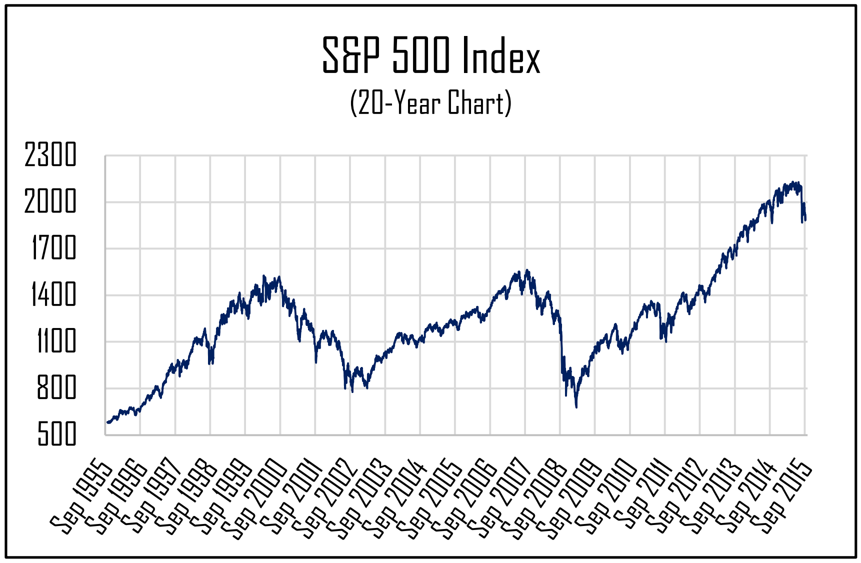
At Cypress, we take great pride in serving as a fiduciary to all of our individual clients, including providing advice on their workplace 401(k) options. We also offer fiduciary services to 401(k) plans and their participants, in order to help prevent lawsuits like those at Lockheed and Boeing. If you need help navigating your personal or 401(k) investment options, either as a participant or administrator, we can help.

The S&P 500 Lost 6.9% in Q3, Its Worst Quarterly Return Since 2011

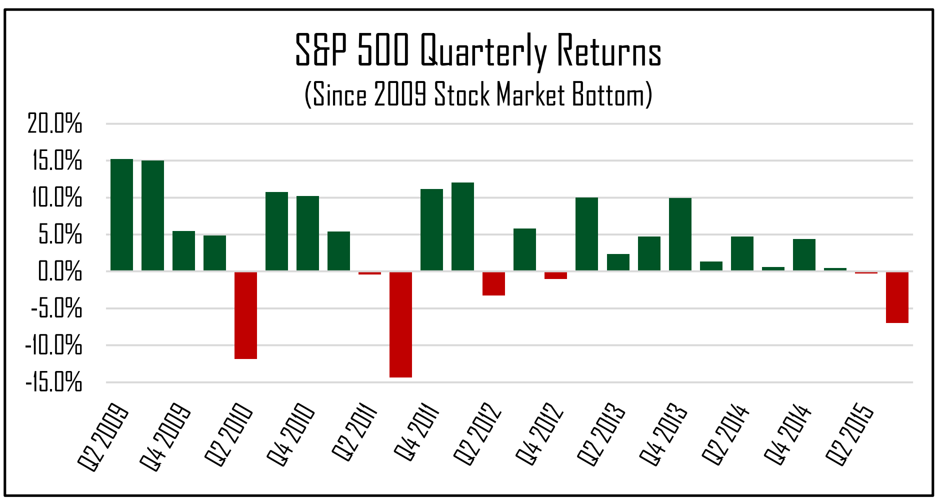
Equity Overview – U.S. Equity Markets

After a largely indifferent first half of 2015, domestic stock markets staged a dramatic breakout during the third quarter. Unfortunately for investors, the breakout move was not in the direction that has typically prevailed over the last few years, instead turning swiftly lower.

After rallying more than 2% in July to briefly mark another new all-time high of 2,130, the S&P 500 index took a hard turn downward in August, punctuated by a one-week, 11% plunge from 2,097 to 1,868. Concerns about a slowing global economy and a free-falling Chinese stock market helped fuel the selloff, resulting in the worst quarterly return for the market in four years.



And yet, despite a litany of ugly statistics regarding the quarterly performance, it bears reminding that the market remains at historically high levels. While no investor likes to endure a loss, the S&P 500 closed Q3 at a level still 3% above its lowest levels from last fall (during a brief pullback in October 2014), and a full 23% above the index's previous bull-market highs (the 2007 bull market topped out around 1,565, before the chaos of the Great Recession). So, for long-term investors, this quarterly dip should be examined with a historical context in mind. The market recently concluded its third-longest period in history without experiencing a pullback of 10% or greater. Those types of stretches can have a tendency to warp investor perception, as individuals (and some advisors) lose sight of the market's longer-term path.



Since 1900, there have been 35 declines of 10% or more in the S&P 500—in those previous instances, the index fully recovered its value after an average of 10 months. Most recently, the S&P index fell nearly 20% during the summer of 2011, in response to the European debt crisis and a Standard & Poor's downgrade of U.S. Treasury debt. Of course, the market proceeded to nearly double over the subsequent four years, bringing us to our current lofty levels.

Yes, there is some concern that the slowing global economy could spark a wider recession, which would likely cause a deeper correction in the markets. However, the recent downturn should not distract an investor from adopting a long-term view of the markets. For the disciplined investor, these sorts of moves provide opportunities to reassess and rebalance portfolio allocations, in order to become better positioned for the market's next move, whatever it may be.

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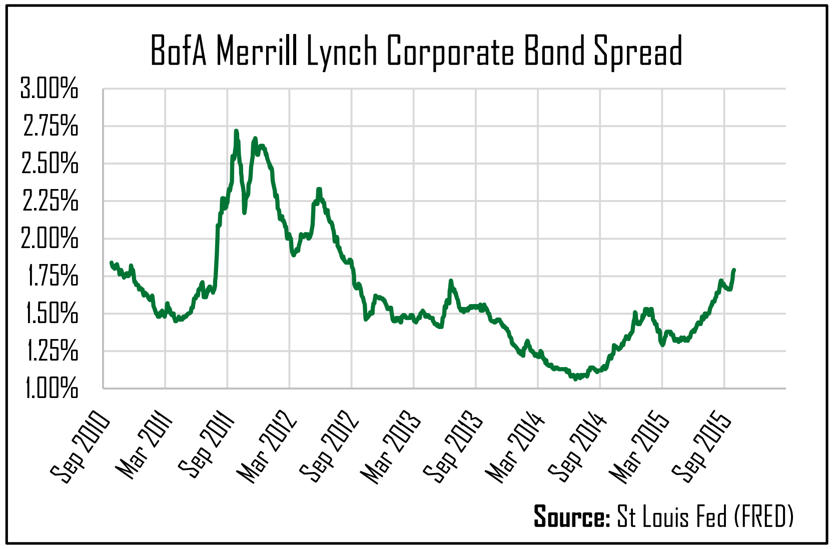
Widening Corporate Bond Spreads Often Predict Impending Recessions

Corporate Bond Spreads Continue to Widen – Fixed Income

During periods of stock market turbulence, it is often instructive to study the behavior of the bond market for indications of broader investor sentiment. Specifically, examining trends in corporate bond spreads (the difference between the average percent yield on investment-grade corporate bonds and the yield on "risk-free" government bonds) can provide insight into investor expectations of near-term economic growth.

When these spreads are flat or narrowing, investors are typically expecting continued economic growth, leading to robust corporate earnings. But when they are widening, the outperformance of the government bonds is an indication of a "flight to quality", and a decline in investor trust of the creditworthiness of corporate lenders. Perhaps unsurprisingly—given data that suggests a slowing global economy—the third quarter saw a steadily widening corporate spread, as spreads (measured by BofA-Merrill Lynch) reached levels last seen in 2012.

As a result, Bloomberg's US Corporate Bond Index was essentially flat for Q3, even as its US Treasury

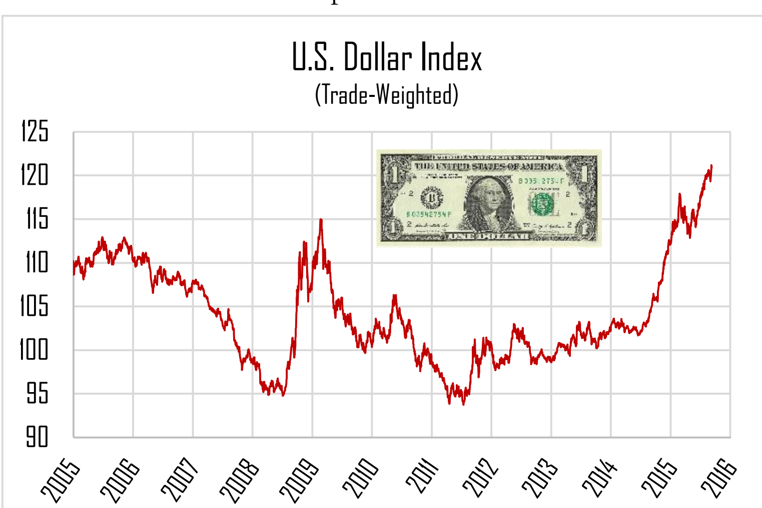


Bond Index gained 2.07%. While bonds of all types can typically be expected to outperform stocks during recessionary periods, corporate bonds will rarely keep pace with their government counterparts.

Source: Federal Reserve Bank of St. Louis

Strong Dollar Impacts U.S. Corporations – Foreign Currencies

One of the downstream impacts of the Fed's recent



monetary policy tightening is a steadily appreciating dollar, as it gains ground against the currencies of nations whose banks continue to ease policy.

While a strengthening dollar is not without its benefits, it typically harms multinational corporations who have significant international sales. As a result, U.S. companies like McDonald's, Nike, and Amazon have seen their earnings come under pressure in recent quarters.

This dynamic complicates the decision-making of the Federal Reserve, which remains wary of further harming corporate profits by tightening too aggressively. While most pundits still project that the Fed will raise short-term rates by mid-2016 at the latest, we continue to expect that the Fed will be patient and deliberate with any policy tightening, lest they disrupt our nation's still-tepid economic growth.

Source: Federal Reserve Board of Governors