Inside Views From an Investment Management Leader

UPDATE

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About our Company

Company Profile:

Concord Investment Counsel is a private, boutique investment firm who has helped our clients grow and protect their wealth since 1991.

Key Offerings:

- *Personal wealth management*
- *Proactive investment strategies*
- *Proprietary research*
- *A professional team*
- *Fee-only services*

Distinguishing Values:

- *Passion for excellence*
- *Strategic focus*
- *A disciplined process*
- *Prudent risk management*
- *Comprehensive client care*
- *Superior long-term performance*
- *Sound judgment*
- *Objective Analysis*

CONCORD Investment Counsel

9811 Irvine Center Drive
Suite 200
Irvine, CA 92618
Phone: 949-852-4100 or 800-497-9400
Fax: 949-852-4106
www.cichome.com

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Economic Review & Outlook

China's Growth Problems Weigh on Global Outlook

The Chinese economy is now the second largest in the globe and all that is good there and all that is bad there economically has significant impact on the rest of the globe. For the last five years the strong consumption from the Chinese economy helped the globe recover from one of the worst recessions in history. Now this consumption engine is slowing considerably and causing fear throughout global economies (Fig 1). China has not had a recession in 40 years but likewise has never had debt fueled consumption to the extent seen over the last decade. While the US economy does not trade significantly with the Chinese we are highly dependent upon other economies that do trade with China.

Very few economists have been willing to speculate on the extent of China's economic woes. However, the Federal Reserve and global investors are clearly bracing for a potential storm. The Fed has deferred planned increases in rates almost entirely based upon the unknowns from Chinese economic weakness. Financial markets around the globe sold off considerably in the third quarter of 2015, seemingly only because of the potential problems brewing in China. The S&P 500 fell 6.4% in Q315, and the Shanghai composite fell 27.9%. The US bond market, which has been in unprecedented territory for several years, went back in rally mode in the third quarter as China's economic weakness made headlines. Commodities had their worst quarter in years as demand for raw materials waned. Crude oil had a 30-handle for a few days as demand weakened and total global storage capacity was nearly breached.

In August, China acted to protect their exports by devaluing their currency (Yuan) approximately 5% relative to the dollar (Fig 2). This protective action, however, has been difficult to maintain and the Yuan has since regained almost half of the devaluation. Growth in retail sales in China remains high but has slowed from 22% in 2008 to 10% currently (Fig 3). Likewise growth and industrial production has slowed from a high of 15% in 2011 to 6% currently (Fig 4). China has used vast amounts of debt to finance the construction of public works projects and office and commercial buildings. Despite the slowdown in China's economy, reported unemployment remains at near 4% (Fig 5). There has been lots of talk of China having too much debt similar to the rest of the world. While China's debt has increased, they maintain only a modest annual deficit and their debt to GDP ratio is still less than 20% (Fig 6). This is a fraction of what the other economic superpowers maintain.

Mitch Pletcher
President
Chief Investment Officer

The ripple effect of Chinese economic weakness for the most part has yet to be felt in America. Thus far we have seen significant impact on the energy and basic materials sectors. However, consumer goods, consumer services, industrial products, and financial services in America continue to grow and prosper.

It's hard to imagine this economic cycle ending anytime soon when the Fed has yet to raise rates and any form of inflation has not emerged. Historically, almost every economic cycle has ended just after a period of high interest rates, high inflation, unfriendly central bank policy, and excess capacity in multiple sectors of the economy. Currently, none of this is visible with the exception of some excess capacity in energy.

Healthcare in America has taken a beating in the market despite strong growth and rising expectations for earnings growth for the next few years. Hillary Clinton's prospects for election are the backbone of this weakness. Biotech's innovation continues to drive double-digit earnings growth in that industry group. Investors are struggling to adequately discount the risk to slower growth from the likely pressure on pricing that will result from a Hillary Clinton victory.

The problems in the globe and the impacts here in America are real but the markets have likely discounted these into prices already. The ripple effect in America, as well as the continued news out of China, will set the course for the financial market performance for the rest of the year and into 2016.

We remain optimistic.

Financial Market Review & Outlook

Markets Correct on Economic and Growth Worries

Mitch Pletcher
President
Chief Investment Officer

Risk assets had a terrible quarter as concerns about growth and earnings mounted in the third quarter. The growth in earnings concerns mostly came from the perception that China's problems will become the world's problems, as well as evidence that earnings growth here in America has paused a bit.

Equities of all sizes, shapes and forms declined in the third quarter of 2015. The S&P 500 fell 6.4% and is now down 5.4% year to date. Concord's Dynamic Growth portfolio fell 7.1% and is down 1.4% YTD. Small-cap growth stocks (IWO) fell 13.0% in the quarter and are down 5.4% year-to-date. European stocks (EZU) fell 8.5% and are down 3.8% year-to-date. China (Shanghai composite) fell 27.9% and is down 5.6% year-to-date. China is obviously where the problems are and hence their markets fell the most in the quarter. The economies closely tied to China like Western and Eastern Europe saw their markets decline more severely than the American markets.

With expectations for global growth falling, commodity prices continued the decline that began in the previous quarter. The Goldman Sachs commodity basket (GSG) fell 19.1% in the quarter and is down 21% year-to-date. The money that left stocks and commodities seemed to find itself going back into defensive areas it had just exited. Treasury notes and bonds performed well as did utility stocks as yet another flight to quality played out. Dividend paying apartment REITs (REZ) also had a good quarter raising 6.8% and still up 3.3% year-to-date. The percent of our population living in apartments is at a two decade high as Generation X and the Millennials continue to favor mobility over homeownership.

The outlook for the equity market hinges on the ability of the globe to hold its footing and not fall backward into recession. This seems likely with central banks united in an effort to keep stimulation on until sustainable growth in the globe is obvious. The excess capacity in energy and materials is being mopped up without much damage to the economy overall.

As worries about recession fade, the leadership in the market will return to the companies with the best expectations for earnings. This would include technology, select consumer discretionary areas, financials, and select areas of healthcare.

Table 1: Stock & Bond Market Returns — *9/30/15*

	Quarterly Change	Trailing 12 Mos		Quarterly Change	Trailing 12 Mos
Large Cap Growth (IWF)	-5.4%	2.9%	Small Cap Value (IWN)	-10.7%	-1.7%
Large Cap Value (IWD)	-8.4%	-4.5%	Small Cap Growth (IWO)	-13.0%	4.2%
Europe Asia Far East (EFA)	-9.7%	-8.2%	Emerging Markets (EEM)	-17.3%	-19.4%
Invest Grade Bonds (LQD)	1.2%	1.5%	High Yield Bonds (HYG)	-4.9%	-4.4%
Interm Treasurys (IEF)	3.2%	6.1%	Mortgage Bonds (MBB)	1.5%	3.3%

Source: Bloomberg, Barclay's Global Investors ETFs. Actual performance including dividends.

Table 2: Real Estate & Commodity Returns — *9/30/15*

	Quarterly Change	Trailing 12 Mos		Quarterly Change	Trailing 12 Mos
DJ US Real Estate (IYR)	0.4%	6.4%	DJ Commodity Index (DJP)	-15.9%	-28.9%
Int'l Real Estate (IFGL)	-5.2%	-3.3%	Goldman Commodity (GSG)	-19.1%	-42.3%
NAREIT Residential (REZ)	6.8%	20.0%	Gold (GLD)	-4.9%	-8.0%

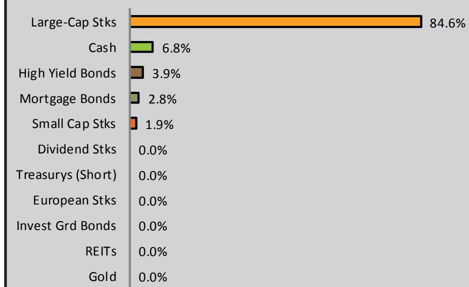
Source: Bloomberg, Barclay's Global Investors ETFs. Actual performance including dividends.

CIC Managed Accounts

Growth Portfolios

Dynamic Growth

A dynamic blend of stocks, bonds, commodities, REITs, and cash for growth investors with a bias toward timely asset classes.



Growth

A portfolio of large- and mid-cap US stocks that are industry leaders with strong brands and timely products.

Diversified Equity

A global, all-cap equity portfolio following economic trends across capitalization and geographic ranges.

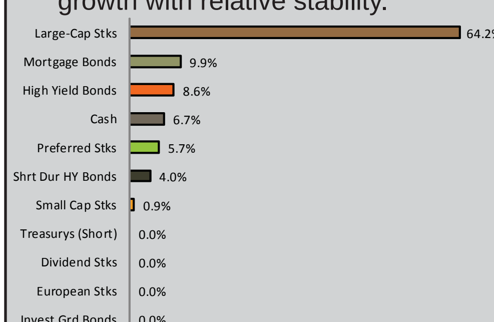
Focused REIT

A portfolio of companies whose primary business is owning and leasing real properties.

Balanced Portfolios

Asset Allocation for Income

A portfolio of stocks, bonds, and cash for moderately-conservative investors seeking income and growth with relative stability.



Equity Markets: Consumption Drives Growth

Earnings growth drives leadership in the stock market, while consumption generally drives earnings. Every market cycle has consumption themes which are either secular or cyclical in nature. Here's what is active in this market cycle.

Secular Consumption Themes:

- **Theme:** Global demand for wireless devices, digital media and cloud computing power. Demand growth is a product of industry's ability to innovate. Sector: Technology
- **Theme:** Global demand from wealthier and growing emerging market populations for meat and poultry to support more "western-like" eating habits, as well as growing demand for technologies that provide greater agricultural yields.

  Sector: Materials
- **Theme:** Global demand for energy as population grows as well as increasing demand for the technologies that make it viable to extract natural resources from the farthest reaches of the earth. Sector: Energy
- **Theme:** Increasing demand for healthcare as population ages, as well as growing demand for new and better products provided by innovation in the development of life-saving drugs, devices, and services. Sector: Healthcare

Cyclical Consumption Themes:

- **Theme:** The return of mild consumer discretionary spending balanced against purchasing decisions based on need instead of want. Sector: Consumer Discretionary/Staples
- **Theme:** Pent-up demand within the enterprise upgrade cycle. Sector: Technology
- **Theme:** The re-surfacing of emerging market infrastructure spending. Sector: Industrials
- **Theme:** Credit market stabilization and a return of demand for investment banking products and services. Sector: Financials
- **Theme:** The return of demand for manufactured products.

  Sector: Industrials, Energy

Commentary: Volatility Rocks Equity Markets

Global market turmoil left few places to hide in the third quarter, with only the safe-haven Utilities sector showing positive performance. Earnings expectations for the S&P 500 are now essentially flat for the year, dragged down significantly by energy and materials sectors. As global growth concerns have come into sharp focus alongside a significant decline in Chinese equity markets, investors are left to seek out the areas of the market where earnings growth hasn't evaporated. Technology and Consumer Cyclical sectors offer modest growth expectations, along with some healthcare segments that are now more reasonably priced after a their recent sell-off of almost twice the market in aggregate.

Sector Performance Review *9/30/15*

	Quarterly Change	Trailing 12-Months
Utilities	4.7%	4.9%
Consumer Staples	-0.9%	5.8%
Consumer Discretionary	-3.4%	11.5%
Technology	-6.1%	1.8%
Financials	-6.1%	1.1%
Telecom	-6.8%	-7.5%
Industrials	-7.4%	-3.7%
Healthcare	-11.2%	4.9%
Materials	-16.8%	-17.7%
Energy	-18.4%	-31.4%

Data based upon Russell 1000 Index and GICS sectors. Source: Bloomberg Financial

Fixed Income Review

By Kyle Aron

Holding Pattern

Kyle Aron
Senior Analyst

Unsurprising in light of recent market volatility, the Federal Reserve declined to begin raising its target interest rate during its meeting in September. While unemployment may be near the Fed's target, a persistent downtrend in labor force participation and negligible inflation helped keep any Fed action on pause. With global financial market and economic weakness coming into stronger focus during the third quarter, timing of the Fed's first move with interest rates remains uncertain. In fact, Fed Funds futures place the likelihood of an increase in rates during the October meeting at 8.0%, with December still low at only 37.0%.

Global financial markets were roiled by volatility in Chinese equities during the third quarter of 2015. The Shanghai Composite Index fell nearly 28.0% in the quarter, leading the way for tumbling equity performance across developed economies. The S&P 500 dropped 6.4%, while European equities lost 8.5% (EZU). Commodities were likewise under pressure as global growth concerns mounted, which was only exacerbated by a continued glut in oil and negligible inflation (DJP, -15.9%). REITs outperformed similar to their fixed income peers, ending up marginally for the quarter (IYR +0.4%).

As expected alongside the Fed's inaction and market tumult, fixed income saw largely positive performance in the third quarter. High-quality issues saw the best performance, with long-dated Treasurys (TLT) up nearly 6.0%. Mid-range Treasurys (IEF) were likewise up over 3.0%. Investment-grade corporate bonds (LQD) fared modestly well, up 1.2% for the quarter. Mortgage-backed securities performed similarly, posting a gain of 1.5% (MBB).

High-yield securities were again under pressure, as overall risk-aversion and the persistent headwind of overexposure to the energy sector lead investors to continue exiting the space (HYG, -4.9%). While many energy companies may have been limping along since the tumble in oil prices began last year, price hedges and other temporary means of support are likely coming to an end. As the price of oil has failed to sustain any lasting rebound, investors are likely concerned that defaults may begin to accelerate.

Despite the risk-aversion that flared up during the third quarter, it's notable that the strong gains across much of fixed income were not enough to bring performance into the green for the year. Long-dated Treasurys (TLT) remain down 0.2% for the year, while investment-grade corporate bonds (LQD) are still 0.6% in the red. Getting ever-closer to the eventual liftoff in interest rates, the duration risk present in many segments of fixed income remains evident. As equity markets move past the fears that gripped them during the third quarter, investors may be well-suited to seek out the areas of stronger growth that remain in stocks. The fixed income landscape will remain treacherous at least until the Fed's timing more fully reveals itself.

Economic & Financial Market Charts

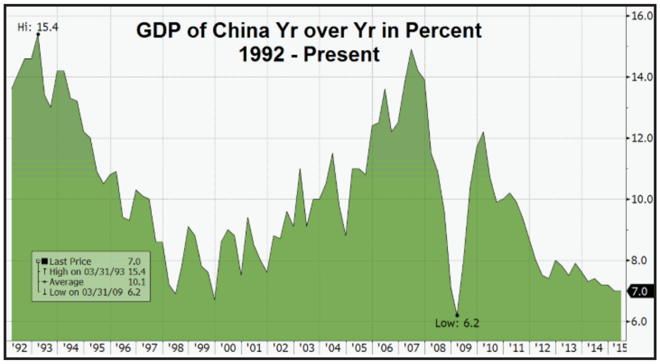


Figure 1 - Source: Bloomberg Financial

Graph of China GDP showing a steady decline from previous years of double digit growth

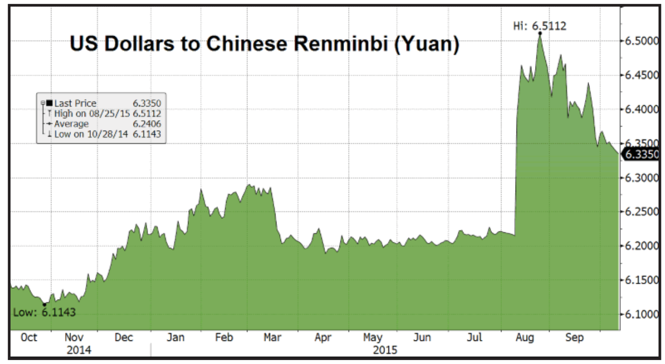


Figure 2 - Source: Bloomberg Financial

Graph of the relative value of the US Dollar to the Chinese Yuan, showing China's abrupt currency devaluation

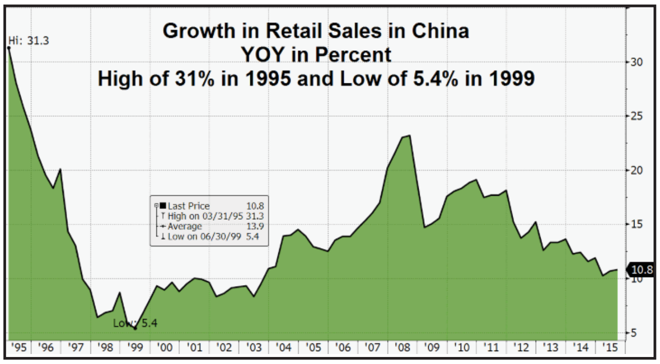


Figure 3 - Source: Bloomberg Financial

Graph of Chinese retail sales growth data, showing a steady downward trend in recent years

Figure 4 - Source: Bloomberg Financial

Graph of Chinese industrial production data, exhibiting a downward trend similar to that of retail sales

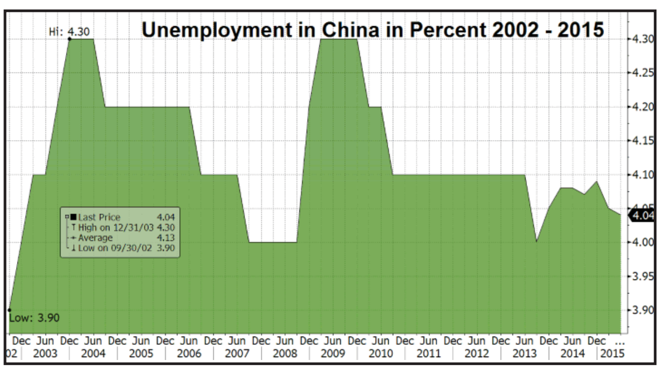


Figure 5 - Source: Bloomberg Financial

Graph of China's unemployment, reported as modestly lower than US levels at approximately 4.0%

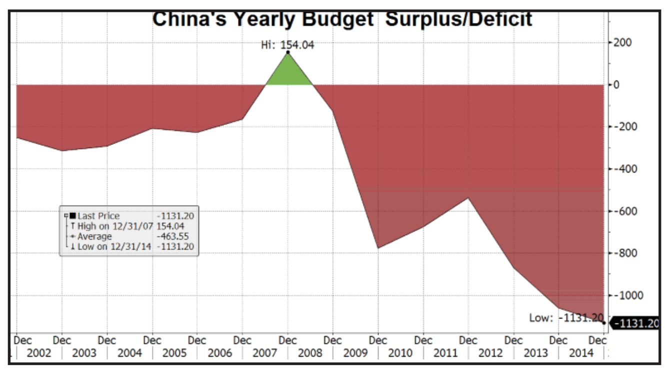


Figure 6 - Source: Bloomberg Financial

Graph of China's annual budget, showing only a modest annual deficit relative to many developed nations

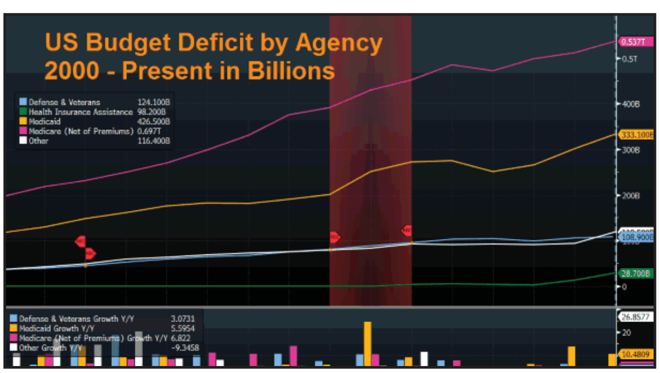


Figure 7 - Source: Bloomberg Financial

Graph of US budget deficit by agency, with Medicare spending exhibiting an outsize lead

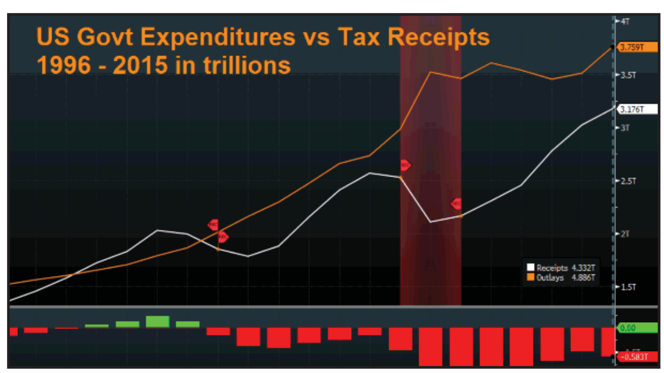


Figure 8 - Source: Bloomberg Financial

Graph of US annual budget, showing a fairly wide but gradually contracting annual deficit