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INSIGHTS

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# A Look Back at 2016

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Every year brings its share of surprises. But how many of us could have imagined that 2016 would see the Chicago Cubs win the World Series, Bob Dylan receive the Nobel Prize in Literature, Donald Trump elected president, and the Dow Jones Industrial Average close out the year a whisker away from 20,000? The answer is very few—a lesson that investors would be wise to remember.

At year-end 2015, financial optimists seemed in short supply. Not one of the nine investment strategists participating in the January 2016 Barron's Roundtable expected an above-average year for stocks. Six expected US market returns to be flat or negative, while the remaining three predicted returns in single digits at best. Prospects for global markets appeared no better, according to this group, and two panelists were sufficiently gloomy to recommend shorting exchange-traded emerging markets index funds.[1]

Results in early January 2016 appeared to confirm the pessimists' viewpoint as markets fell sharply around the world; the S&P 500 Index fell 8% over the first 10 trading sessions alone. The 8.25% loss for the Dow Jones Industrial Average over this period was the biggest such drop throughout the 120-year history of that index.[2] For fans of the so-called January Indicator, the outlook was grim. Then things seemingly got worse.

Oil prices fell sharply. Worries about an economic debacle in China re-entered the news cycle. Stock markets in France, Japan, and the UK registered losses of more than 20% from their previous peaks, one customary measure of a bear market.[3] Plunging share prices for leading banks had many observers worried that another financial crisis was brewing. As US stock prices fell for a fifth consecutive day on February 11, shares of the five largest US banks slumped nearly 5%, down 23% for 2016.

The *Wall Street Journal* reported the following day that "bank stocks led an intensifying rout in financial markets."[4] A USA Today journalist observed that "The persistent pounding global stock markets are taking seems to be taking on a more sinister tone and more dangerous phase, with emotions and fear taking on a bigger role in the rout, investors questioning the ability of the world's central bankers to calm the market's frayed nerves, and a volatile environment in which selling begets more selling."[5]

February 11 marked the low for the year for the US stock market. While prices eventually recovered, as late as June 28 the S&P 500 was still showing a loss for the year. Meanwhile, a number of well-regarded professional investors argued that the

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## A Personal Note From Global Wealth Advisors

The Federal Reserve's Open Market Committee (FOMC) voted to raise the Federal Funds interest rate a quarter percent to a range of .75 percent to 1 percent during its meeting on March 15th. This is only the third rate increase since the recession of 2007 – 2009. The Committee felt that low unemployment of 4.7%, targeted inflation of 1.9% and forecasted GDP growth of 2.1% for 2017 warranted the increase.

The FOMC also said it would continue with a "gradual" approach to raising interest rates as "The committee expects that economic conditions will evolve in a manner that will warrant gradual increases in the federal funds rate." The Central bankers still have a median projection of two more quarter-point increases for 2017 and three more quarter-point increases in 2018.

The Dow Jones Industrial Average (DJIA), S&P 500 and NASDAQ indexes all responded positively to the formal FOMC announcement. In fact, the DJIA, S&P 500 and NASDAQ are up 6%, 7% and 9% respectively through March 15th of this year. That's why it is so important to ignore politics, conjecture, and short-term volatility when it comes to long-term investing. In the long run, you will be glad you did!

Jim Knaus Mike Krencicki

# Going Global: A Look at Public Company Listings

March 2017
Source: Dimensional Fund Advisors

Trivia time: how many stocks make up the Wilshire 5000 Total Market Index (a widely used benchmark for the US equity market)?

While the logical guess might be 5,000, as of December 31, 2016, the index actually contained around 3,600 names. In fact, the last time this index contained 5,000 or more companies was at the end of 2005.[1] This mirrors the overall trend in the US stock market. In the past two decades there has been a decline in the number of US-listed, publicly traded companies. Should investors in public markets be worried about this change? Does this mean there is a material risk of being unable to achieve an adequate level of diversification for stock investors? We believe the answer to both is no. When viewed through a global lens, a different story begins to emerge—one with important implications for how to structure a well-diversified investment portfolio.

**U.S. AGAINST THE WORLD**

When looked at globally, the number of publicly listed companies has not declined. In fact, the number of firms listed on US, non-US developed, and emerging markets exchanges has increased from about 23,000 in 1995 to 33,000 at the end of 2016. (See Exhibit 1.)

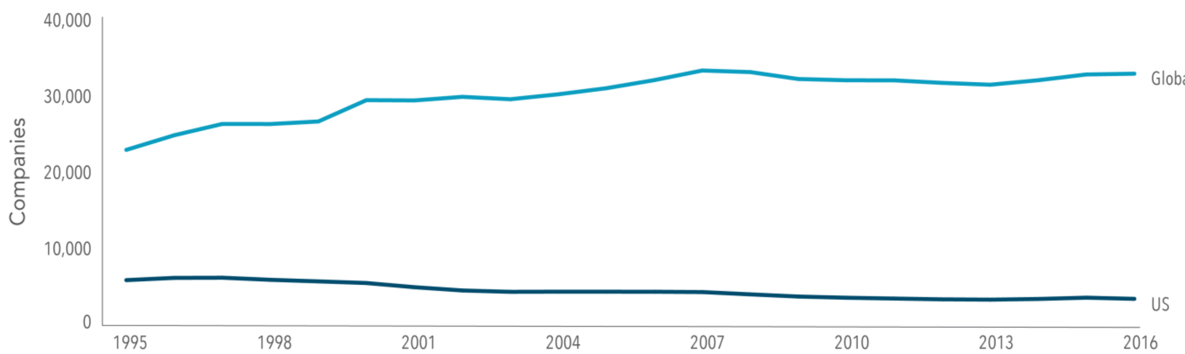
It should be noted, however, that this number is substantially larger than what many investors consider to be an investable universe of stocks. For example, one well-known global benchmark, the MSCI All Country World Index Investable Market Index (MSCI ACWI IMI) contains between 8,000 and 9,000 stocks. This index applies restrictions for inclusion such as minimum market capitalization, volume, and price. For comparison, the Dimensional investable universe, at around 13,000 stocks, is broader than the MSCI ACWI IMI.

While it is true that in the US there are fewer publicly listed firms today than there were in the mid-1990s (a decrease of about 2,500), it is clear that the increase in listings both in developed markets outside the US and in emerging markets has more than offset the decline in US listings. Although there is no consensus about why US listings have decreased over this period of time, a number of academic studies have explored possible reasons for this change. One line of investigation considered if changes in the regulatory environment for listed companies in the US relative to other countries may explain why there are fewer listed firms. Another considered if, since the 2000s, private companies have had a greater propensity to sell themselves to larger companies rather than list themselves. In either case, the implication for investors based on the numbers alone is clear—the number of publicly listed companies around the world has increased, not decreased.

**A GLOBAL APPROACH**

In the US, with thousands of stocks available for investment today, it is unlikely that this change will meaningfully impact an investor's ability to efficiently pursue equity market returns in broadly diversified portfolios. It is also important to note that a significant fraction of the publicly available

**Exhibit 1 Number of Publicly Listed Companies**




**Source: Bloomberg**

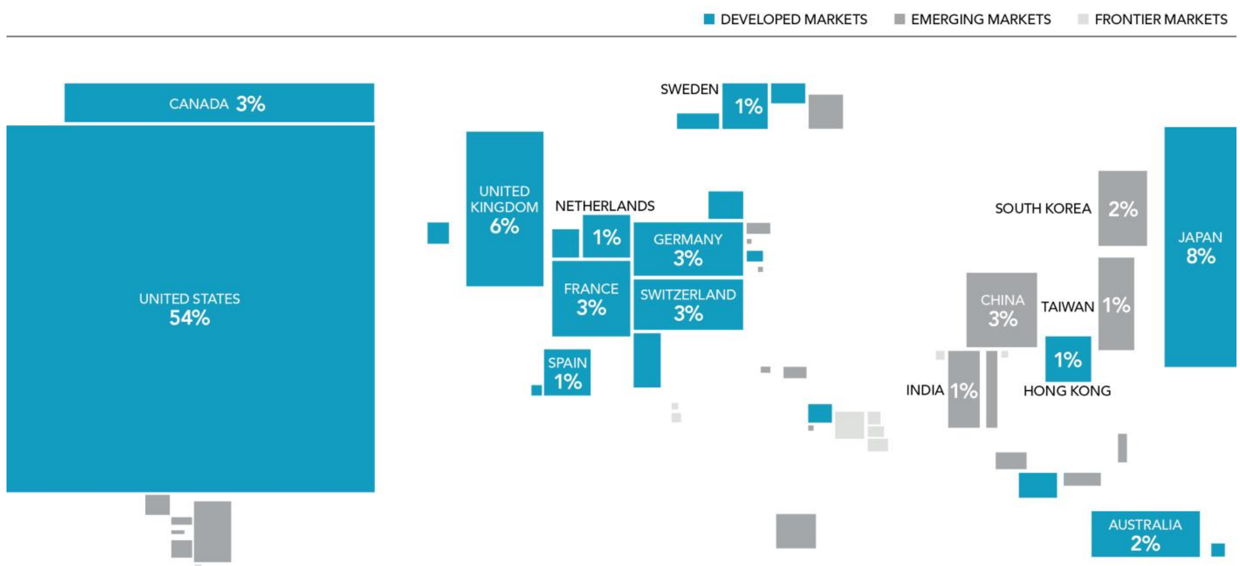
global market cap remains listed on US exchanges. As noted in Exhibit 2, the weight of the US in the global market is approximately 50–55%. For comparison, it was approximately 40% in 1995.

For investors looking to build diversified portfolios, the implications of the trend in listings are also clear. The global equity market is large and represents a world of investment opportunities, nearly half of which are outside of the US. While diversifying globally implies an investor's portfolio is unlikely to be the best performing relative to any one domestic stock market, it also means it is unlikely to be the worst performing. Diversification provides the means to achieve a more consistent outcome and can help reduce the risks associated with overconcentration in any one country. By having a truly global investment approach, investors have the opportunity to capture returns wherever they occur.

## CONCLUSION

While there has been a decline in the number of US-listed, publicly traded companies, this decline has been more than offset by an increase in listings in non-US markets. While the reasons behind this trend are not clear, the implications for investors today are clearer—to build a well-diversified portfolio, an investor has to look beyond any single country's stock market and take a global approach. ●

**Exhibit 2 Percent of World Market Capitalizations as of December 31, 2016**




**Data provided by Bloomberg. Market cap data is free-float adjusted and meets the minimum liquidity and listing requirements. Many nations not displayed. Totals may not equal 100% due to rounding. China market capitalization excludes A-Shares, which are generally only available to mainland China investors.**

[1] Source: Wilshire Associates

*Past performance is no guarantee of future results. There is no guarantee an investing strategy will be successful. Diversification does not eliminate the risk of market loss. Investing risks include loss of principal and fluctuating value. International investing involves special risks such as currency fluctuation and political instability. Investing in emerging markets may accentuate these risks.*

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*Indices, such as the MSCI All Country World Index Investable Market Index (MSCI ACWI IMI) are not available for direct investment.*

## A Look Back at 2016

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next downturn was fast approaching. One prominent activist in May predicted a "day of reckoning" for the US stock market, while another reportedly urged his fellow hedge fund managers at a conference to "get out of the stock market." A third disclosed in August a doubling of his bearish bet on the S&P 500.[6]

Throughout the year, some observers fretted over the pace of the economic recovery. The New York Times reported in July that "Weighed down by anemic business spending, overstocked factories and warehouses, and a surprisingly weak housing sector, the American economy barely improved this spring after its usual winter doldrums."[7]

Despite all of this noise, the S&P 500 returned 11.9% for the year and international stocks[8] returned 4.4% for US dollar investors (6.9% in local currency[9]), helping to illustrate just how difficult it is to outguess market prices. Once again, a simple strategy of embracing sensible asset allocation and broad diversification was likely less frustrating than fretting over portfolio changes in response to news events.

1. Lauren Rublin, "Peering into the Future," *Barron's*, January, 25, 2016.
2. www.djaverages.com, accessed January 6, 2017.
3. Michael Mackenzie, Robin Wigglesworth, and Leo Lewis, "Stock Exchanges across the World Plunge into Bear Market Territory," *Financial Times*, January 21, 2016.
4. Tommy Stubbington and Margot Patrick, "Banks Drop as Global Rout Deepens," *Wall Street Journal*, February 12, 2016.
5. Adam Shell, "Market Tumult Charts New Waters," USA Today, February 12, 2016.
6. Dan McCrum and Nicole Bullock, "Growling Bears Provide Soundtrack for Investors," *Financial Times*, May 21, 2016.
7. Nelson D. Schwartz, "US Economy Stays Stuck in Low Gear," *New York Times*, July 29, 2016.
8. Source: MSCI. International stocks represented by the MSCI All Country World ex US IMI (net div.).
9. Local currency return calculation represents the price appreciation or depreciation of index constituents and does not account for the performance of currencies relative to a base currency such as the US Dollar. Local currency return is theoretical and cannot be replicated in the real world.

*Past performance is no guarantee of future investment results. Indices are not available for direct investment; therefore, their performance does not reflect the expenses associated with the management of an actual portfolio. Diversification does not eliminate the risk of market loss. There is no guarantee an investment strategy will be successful.*