Coherent
Financial Advisers

MANAGER'S LETTERS 2016

Coherent Financial Advisers, LLC

Manager's Letters 2016
by Sargon Y. Zia, CFA

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Article 1: Manager's Letter 2016 Q4

Winds of change have swept across the geopolitical landscape from 2016 and into the new year. How markets will be affected in 2017 and beyond will be the focus of much speculation. At Coherent, we would rather rely on tangible market factors more easily observable than *wind*. Prevailing trends in earnings and financial cycles can be a significant help in gauging the market's tenor. Here are two examples from our fourth quarter analysis.

One trend I've mentioned often in recent articles is the *"silver lining"* effect. I described it in Earnings Insight March 2016, expounding further in several later articles. The silver lining effect states that earning declines in past quarters lower the bar for relative growth in future quarters. Our first chart illustrates this effect.

Operating earnings declined on a dollar-per-share basis throughout 2015. Comparing 2016 quarters beside 2015 shows that growth turned positive in Q3. Our December Coherent Investor article states, *"If earnings continue to rise, mid-2017 will be the apex for the silver-lining-tailwind effect of relatively easy comparable EPS growth."*

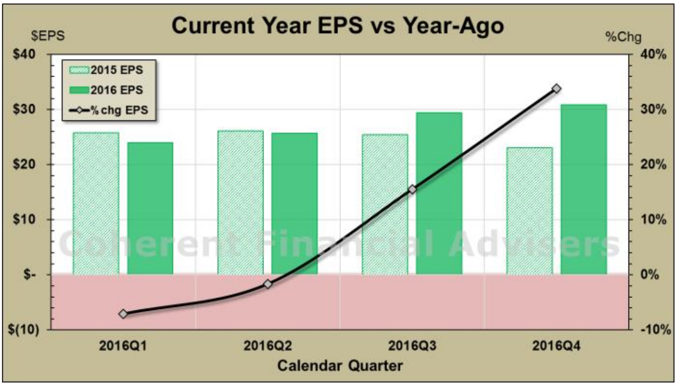

Figure-1 | S&P Dow Jones Indices, us.spindices.com, 31-Oct, 2016

Prevailing financial cycles also impact the market's trend. Our second chart reveals three shorter-term cycles comprising the current 2009 secular bull market. The first cycle doubled over 10-quarters and corrected 20%, bottoming in October 2011. The second doubled over 4-years and corrected 15%, bottoming in February 2016. We are now ten months into the third cycle, which for now is a tailwind while it trends upward.

Figure-2 | Stockcharts.com, 13-Dec, 2016

In my [Q3 Manager's Letter]() I wrote, *"Portfolios remain positioned to fully participate should the uptrend resume."* This has been a profitable decision for Q4. The major support trend line of 2009 (solid green line) will be retested, and eventually broken. Also of note, the 2016 Stock Trader's Almanac cites, *"A takeover of the White House by the opposing party in the past 50-years … has resulted in a bottom within two years, except 1944, a flat year."*

I would like to announce a birthday – Coherent Financial Advisers turns one year old this month! Tom and I extend our deepest gratitude to you for entrusting us with your financial well-being. Our purpose is to take care of your comprehensive financial needs without external impediments. For years, Tom and I worked together diligently and in good faith to make our work environment a place where we could be proud to serve you. To this end, we felt it most beneficial to build our permanent home here, at Coherent.

Tom and I wish you and your family a very happy and prosperous 2017!

Warm regards,
Sargon Zia, CFA
January 3, 2017

Article 2: Manager’s Letter 2016 Q3

Fifty years ago last month, NBC aired the first episode of *Star Trek*. In its preceding pilot, “The Cage”, the captain is held prisoner by aliens who have the power to project incredibly lifelike illusions. Concerning the financial markets, people readily create their own illusions without any assistance from aliens. At Coherent, we prefer sound reason over illusion.

Earnings estimates are a significant driver of the stock market’s trend. I developed the chart in figure-1 to approximate the margins or sales growth needed to produce the market’s estimated operating earnings. As explained in our [August Earnings Insight] article, this chart helps answer the question, “Are current estimates within the realm of reason?”

For many quarters now, the answer has been – *no, not on this planet*. For instance, to produce the $29 and $31 operating earnings per share estimated for Q3 and Q4, the S&P would need to generate 9% and 14% sales growth, respectively, at 9.5% margin. This is like Captain Kirk demanding, “I need warp-factor 12 now!” As Trekkies would agree, that’s an illusion not even Scotty can deliver.

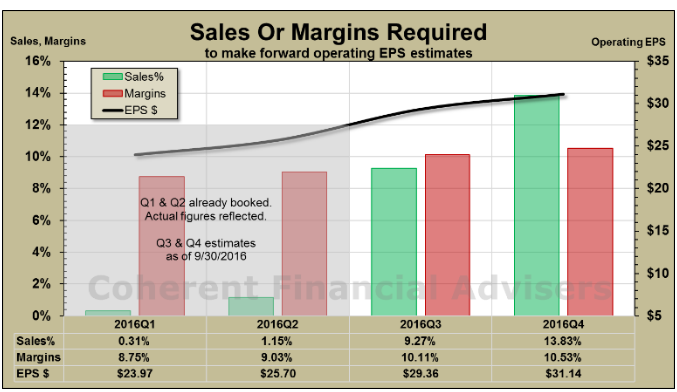

Figure-1 | S&P Dow Jones Indices, 30-Sep, 2016

When the market is priced for the worst, it tends to react well to bad news. But when loftier expectations are already priced-in, it can react negatively even to good news. Operating earnings growth from 2015 through 2016 adds up to being flat at best. Meanwhile, the S&P corrected around its 2014 close (figure-2), albeit at an above-average forward P/E ratio. It appears the market is not priced for the worst.

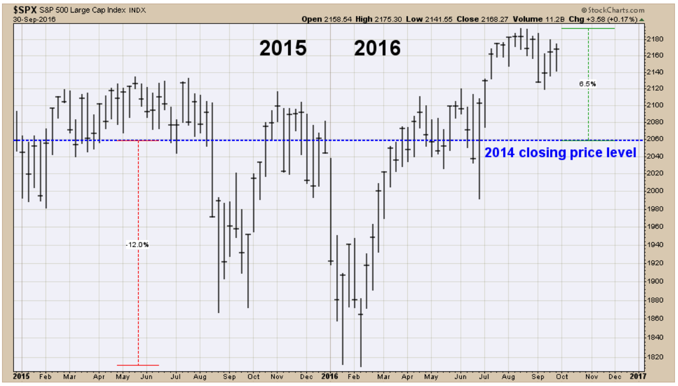

Figure-2 | Stockcharts.com, 30-Sep, 2016

By all accounts, stock market expectations have been excessively optimistic since 2014, as we discussed in our May Earnings Insight article. The wild card is and always will be the P/E ratio. While market fundamentals such as earnings are bounded by the physical laws of nature, what people are willing to pay for them is not.

You and I are paid by market movement, not veracity of opinion. We must therefore consider the market's current uptrend as I shared in our September Coherent Investor article. Given easy monetary policy and favorable earnings and dividend yields relative to the 10-year bond, it is not unreasonable to fathom the market being driven higher. Portfolios remain positioned to fully participate should the uptrend resume. The helm is ready for *evasive maneuvers* when market conditions change.

Live long and prosper,
Sargon Zia, CFA
October 5, 2016

Article 3: Manager’s Letter 2016 Q2

On the flight back from my annual pilgrimage to Charlottesville, Virginia, where I volunteer with the CFA Institute, I thought it appropriate to read Thomas Paine’s *Common Sense*. Published in 1776, his work spoke to the common American reasoning for independence from Great Britain. In an ironic turn, 240 years later, Britons voted for independence from the European Union just days before Americans celebrate their Independence Day.

Paine argued in favor of independence from Great Britain on several points, not the least of which was economic. Peace and prosperity in the long term are inextricably dependent upon a society’s liberty, the ability of people to govern themselves locally. British voters elected independence from the European Union not on a whim, but over mounting grievances tied primarily to British sovereignty.

The pound’s decline subsequent to the vote was heralded by some as an indication of a lack of wisdom. The currency was pounded, declining 8% against the euro in two days (the euro also declined), exacerbating the drop in UK stocks as seen internationally. But the pound has been losing ground for some time. If the two-day decline proves an exit unwise, what does declining over 40% from 2000 to 2008 say about remaining?

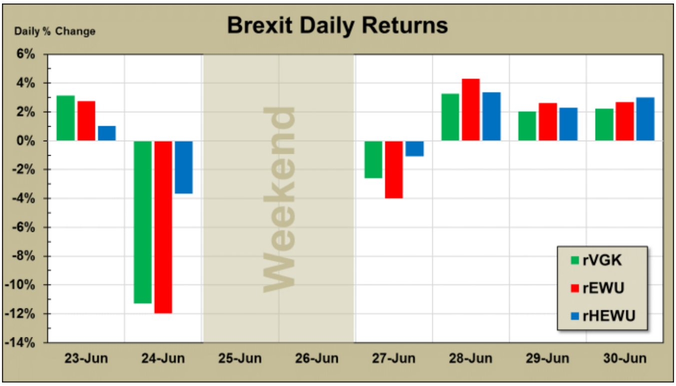

Figure-1 | data from finance.yahoo.com 4-Jul, 2016

Figure-1 shows the daily change in three exchange-traded funds representing Europe (green) of which the UK comprises 30% by market weight, the UK (red), and the UK in local currency as seen by Britons (blue). Thursday’s rally was “on news that” polls were favoring remaining. But on Friday came the vote results to exit and the media barrage of impending doom. European markets regained most of their losses in the week after the vote. What's interesting is that over this entire period the UK markets as seen by Britons *rallied* 5% (figure-2).

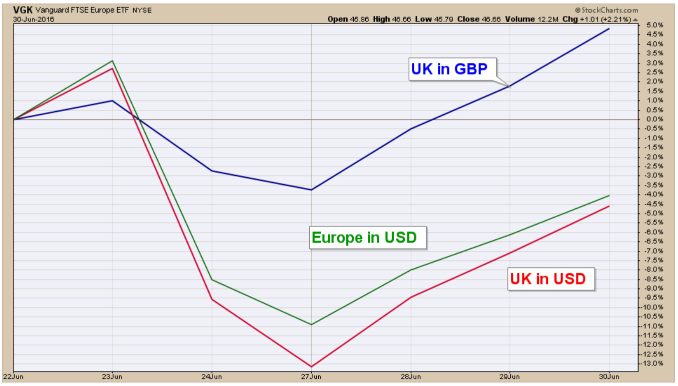

Figure-2 | Stockcharts.com 4-Jul, 2016

Coherent also declared its independence six months ago, with the solemn purpose of taking care of your comprehensive financial needs without external impediments. We are accountable directly and solely to you, not to some distant and impersonal corporate office. It's just … "common sense".

We invite you to visit our website where we post regular articles on the Insights page, commenting on the markets and financial planning topics. There you will also find an online version of the quarterly Manager's Letter. Please always feel free to let us know what you think. We enjoy working with you to achieve *your* financial independence!

Warm regards,
Sargon Zia, CFA
July 4, 2016

Article 4: Manager's Letter 2016 Q1

A long-distance trip on a straight highway can be painfully boring without the occasional curve to provide a better view of what's up ahead. As for markets, I prefer boring. But studying the nature of price swings can yield valuable insight to what might be ahead. The goal is to ascertain whether it's better to ride out the swings, or take a detour.

It has been a tumultuous period since September 2014 when the first crack appeared in the bull market which started in 2011. One year later, the August 2015 tremors would confirm a market that had topped and was correcting. The January aftershocks squelched any remaining euphoria evident in the preceding October rally.

This February's retest of the August lows begged the question, *"Is the September 2014 correction over?"* For answers, we continually study both the market's fundamental health and price behavior. The preponderance of the evidence is seldom beyond a reasonable doubt, compelling us to move cautiously, checking our blind spots.

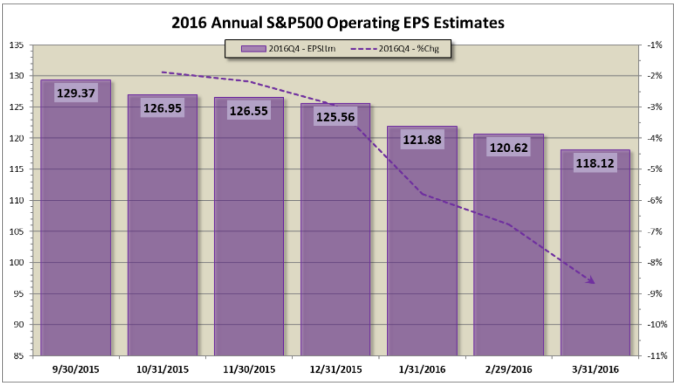

Figure-1 | S&P Dow Jones Indices, us.spindices.com, 31-Mar-2016

In our [Earnings Insight March 2016](#) article we introduced a "silver lining for 2016", namely that 2015 earnings contraction has set a low bar for 2016 growth. However, market valuations are still high by historical standards, even if we accept the more optimistic growth estimates. Meanwhile, hopes for 2016 full year revenue and earnings continue to ebb. First quarter S&P 500 Index revenue is expected to contract, marking five consecutive negative quarters, while earnings estimates call for the worst quarter of consecutive contraction since 2015.

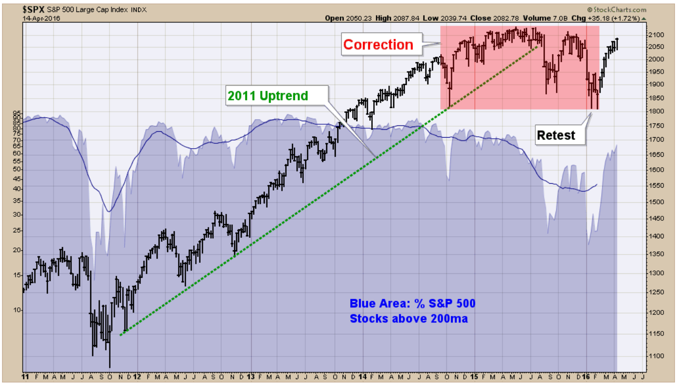

Figure-2 | Stockcharts.com, 14-Apr-2016

When we opted to take a detour last summer by raising cash, our focus turned to determining when and where to get back onto the main road. In our [Market Update February 2016] article we indicated that we had started gradually returning to full equity allocation. As earnings season begins, we remain just shy of full equity allocation, but frankly not without some reservations. Individual stock participation has improved since the February bottom and the S&P 500 has broken initial resistance. The veracity of this upswing will depend on forward looking estimates for a possible return to growth in the second half. This market has been habitually over-optimistic.

We encourage you to visit our website where we regularly share our thoughts in current and relevant articles. Your connection to our website is encrypted at all times using SSL security. We invite you also to connect with us on Facebook, LinkedIn, and Google+.

Warm regards,
Sargon Zia, CFA
April 14, 2016

About Thomas J. Pietrack, CFP®

Tom is a CFP® practitioner and member of the Financial Planning Association's Phoenix Chapter. He is the co-founder of and Director of Financial Planning and Portfolio Manager at Coherent Financial Advisers, LLC.

Tom is a seasoned investment industry professional. His experience includes: Director of Financial Planning and Portfolio Manager at Wealth Management International, Ltd., Portfolio Consultant and Financial Consultant managing a $300MM book of business at Schwab, owner of an American Express Financial Advisors practice. His expertise includes financial planning, portfolio management, advanced tax and estate planning strategies.

Tom's big picture strategic thinking combined with his attention to detail about client's specific goals builds long term relationships with individuals, families, and business owners. Tom believes clients do not merely need more information, but financial wisdom anchored in experience and education tailored to each individual's unique goals, perspective and life ambition.

Tom grew up in Pittsburgh PA, and is an avid football fan. Tom is an advocate for animal welfare and enjoys hiking with his two rescue dogs, Twinkie and Miley. Tom is married and his children are millennials. He is passionate about helping this generation increase their financial knowledge for their long-term financial well-being.

About Sargon Y. Zia, CFA

Sargon is a CFA charterholder and a member of the Phoenix CFA Society. He is the co-founder and Chief Investment Officer (CIO) of Coherent Financial Advisers, LLC

Sargon is a seasoned investment professional. His financial industry experience includes: Chief Investment Officer and Lead Portfolio Manager at Wealth Management International Ltd., High Net Worth Representative with Vanguard's Flagship Services, and Senior High Net Worth Specialist with Schwab's Pinnacle Team. His expertise includes a unique combination of both fundamental and technical analysis.

Sargon also holds a Bachelor's degree in Electronics Engineering Technology. His engineering background includes project design management and supervision serving both the U.S. Military and leading US and foreign commercial clients in Arizona and Milpitas (Silicon Valley), California.

Sargon volunteers with the CFA Institute in Virginia as a final exam grader, and avails himself as a mentor to candidates studying for the CFA charter. Before calling Arizona home, Sargon grew up in Chicago, Illinois, and later moved to California where he worked as an electronics engineer in the heart of San Jose's Silicon Valley. He is the proud father of one son.

Why Coherent?

Coherent Financial Advisers was created from inception with this solemn purpose – *to take care of people's comprehensive financial needs without external impediments.*

At Coherent, we take pride in the care and expertise we deliver to your financial life. We provide comprehensive financial planning, investment management, and employer benefits guidance to select clientele.

For some, financial planning and investment management may be just an occupation. We practice a craft to which we are deeply committed in a lifelong pursuit of excellence.

Why "Coherent"?

Co-her-ent: (adjective) aesthetically ordered, logically connected, harmonious, integrated, consistent, reasoned, rational, as in *"a coherent plan for action."*

- having a natural agreement of the parts
- related in an organized and reasonable way
- having clarity, intelligibility, understandability

Why Coherent?…Because it *defines* us!

Always feel most welcome to contact us for additional information or any questions. We look forward to talking with you about your unique financial goals and personal values!

Visit our website at coherentfa.com today!

Coherent Financial Advisers, LLC, is an independent Registered Investment Adviser (RIA) based in Arizona, offering comprehensive financial planning, investment management, and employer benefits guidance to select clientele. Coherent was founded in January of 2016 by Thomas J. Pietrack, CFP® and Sargon Y. Zia, CFA, consolidating their experience from Charles Schwab, The Vanguard Group, and other smaller boutique firms. Coherent adheres to the higher fiduciary standard of care.

Coherent Financial Advisers, LLC
PO Box 10445, Glendale, AZ 85318-0445
623-432-1157
contact@coherentfa.com
www.coherentfa.com

Available online at coherentfa.com