TRUST

INVESTMENT PERSPECTIVES

A Publication of TRUST COMPANY OF OKLAHOMA *October 2016*

Finding Meaning in the Noise

When I wrote in this space last October, stock market averages had fallen sharply in August and September and investors were fearful of further declines. My message was to embrace pullbacks in the market as opportunities rather than see them as reasons for anxiety. In other words, investors should try to train themselves to feel happy when the market goes down.

From the end of September 2015 to mid-September this year, the S&P 500 has rallied more than 15%. Bonds have also performed well, which means that pretty much everyone's investment assets are worth more today than they were 12 months ago. Investors who embraced the pain last fall and stayed the course have been rewarded while those who gave in to fear and sold have missed out.

But now that stocks are, on average, 15% more expensive than they were a year ago, how should investors be feeling about the markets? Has the economy really improved so much that stocks deserve a 15% premium to where they were 12 months ago? Or were stock prices unreasonably low last fall and now they have just returned to normal?

The answers to these questions are not easy. In the long run, a company's stock price tends to reflect the underlying economic value of the firm. In the short run, however, stock prices are like a voting mechanism in a popularity contest (or presidential election) subject to the whims and emotions of humans who do not always behave rationally.

For example, on September 9, the S&P 500 fell by nearly 2.5% after going 50 days without a move – up or down – of 1% or greater. Headlines and talking heads in the financial news blamed the move on comments made by a Federal Reserve regional bank president that were more "hawkish" than expected about the possibility of a September rate hike. The very next trading day, the S&P 500 regained 1.5%, and the financial media credited the move to a different Federal Reserve member who made more "dovish" comments. The following day, the market fell again, and this time the move was blamed on a drop in oil prices.

While Federal Reserve interest rate changes and oil prices certainly matter to the economy, there were plenty of other days where a Fed

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Zac Reynolds
Senior Vice President

MARKET RECAP

Equity markets worldwide posted positive returns in the third quarter. It was the first quarter in over a year that international stocks outperformed U.S. stocks.

	Third Quarter	YTD	Past 12 Months
Dow Jones	2.8%	7.2%	15.5%
S&P 500	3.9%	7.8%	15.4%
EAFE (Int'l)	6.4%	1.7%	6.5%

GET TO KNOW US

A closer look at one of our team members

If you've ever visited our Utica office, you know how kind **Lisa Perno** is. Lisa grew up in the San Francisco Bay Area until her family moved to Parkville, Mo., when she was 13. After graduating from high school, Lisa moved back to California, where she lived for seven years before moving to Tulsa to be closer to family. Today, Lisa, a valuable member of our Utica team, performs trust administrative functions. It gives us great pleasure to share a little bit about Lisa's life and passions with you.

Investment Perspectives: What do you like to do when you are not working?
Lisa Perno: I like to read, work jigsaw puzzles, make crafts, and work in the yard.

What is your favorite part of this job?
Getting to know our clients. I have developed precious relationships with some of our clients who are willing to share their life memories with me. That is very fulfilling.

Are you married?
I have been married to Don Perno for 29 years. I have two very special stepdaughters and sons-in-law. And, now I have three grandsons.

How would your friends and family describe you?
I suspect they would say that I am loving, determined, loyal, self-motivated, and considerate. Okay, they would probably say that I am fun with a tendency to be somewhat entertaining.

What might someone be surprised to know about you?
I loved being a part of the Tulsa Dog Training Club's Paw Pals program. My 12-year-old Golden Retriever, Skylar, retired from Paw Pals last year. Taking Skylar to nursing homes and assisted living facilities filled me with joy. I loved the residents' reaction when my big dog put her head on their lap and looked up at them.

If you were not living in Oklahoma, where would you rather be?
I have been very happy in Oklahoma, but if I could not live here, I suppose I would live in Asheville, N.C., or Tampa, Fla., to share my life with my grandsons.

governor gave a speech or oil prices moved up or down where the stock market didn't react in a significant way. It just isn't accurate to assign one overall reason for a market move caused by tens of millions of market participants buying and selling stocks, each with different risk tolerances, time horizons, and motivations for their trades.

Those casting about for reasons for a market move are falling prey to the logical fallacy expressed by the Latin phrase post hoc ergo proctor hoc. In other words, the financial media looks at what the market is doing and then tries to come up with a reason. They are confusing correlation with causation. But you can't blame them – after all, a headline writer can hardly write "Dow Drops 150 But We Don't Know Why."

What you can do is ignore the noise. The trite, but true, reason the market goes up is because there are more buyers than sellers on that particular day (or, more accurately, those buyers are more motivated on average than sellers and willing to take higher prices). Those buyers may have good reason, or it may just be sunny in New York (some studies have shown a meaningful positive correlation between sunny weather in a country's primary financial market city and daily stock market returns; other studies claim the relationship is just… noise).

"I am always skeptical when the argument for the market going higher is 'it's different this time.'"

The Long Term

Rather than worrying about the day-to-day popularity contest the market runs, a more useful approach is to measure the worth of each investment, and the market as a whole, in terms of its long-term potential. Fortunately, we have more tools available, and higher confidence in our predictions, when we switch the focus from weeks or months to years or market cycles.

For example, the S&P 500 is trading at around 20 times its earnings over the last 12 months, higher than historic averages of around 16 times. Over the short run, this information has fairly limited predictive value. Sure, we can say that the market looks a little expensive, but you may recall that the earnings multiple expanded to over 30-times earnings during the tech bubble in the late 1990s. I wouldn't bet on that happening again, but it's certainly possible that today's somewhat expensive market could go up to even richer levels next year.

While one-year returns can't be predicted with much accuracy, stretching out our perspective to look at returns over the next 10 years allows us to use valuation tools to forecast returns much more confidently. Instead of the shorter term one-year P/E ratio, the **chart on page 3** shows price divided by inflation-adjusted earnings over the previous 10 years (this is also known as CAPE or Shiller's P/E). There is a strong relationship between

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Shiller's P/E at any point in time and subsequent real returns over the next 10 years. Unsurprisingly, markets have the highest 10-year returns following periods when price-to-earnings multiples are in the lowest (cheapest) quintile, averaging 10.8% a year above the rate of inflation.

Unfortunately, today's price-to-earnings multiple based on 10-year earnings is nearly 26, putting us squarely in the most expensive quintile. Historically, S&P 500 returns in the decade following valuations at today's levels average just 2.2% per year over the inflation rate.

Other measures are also flashing caution signs. S&P 500 market cap as a percentage of U.S. gross domestic product (GDP) is close to 100%. That measure has only exceeded 100% once since World War II – again, in a stretch leading up to the bust of the tech bubble.

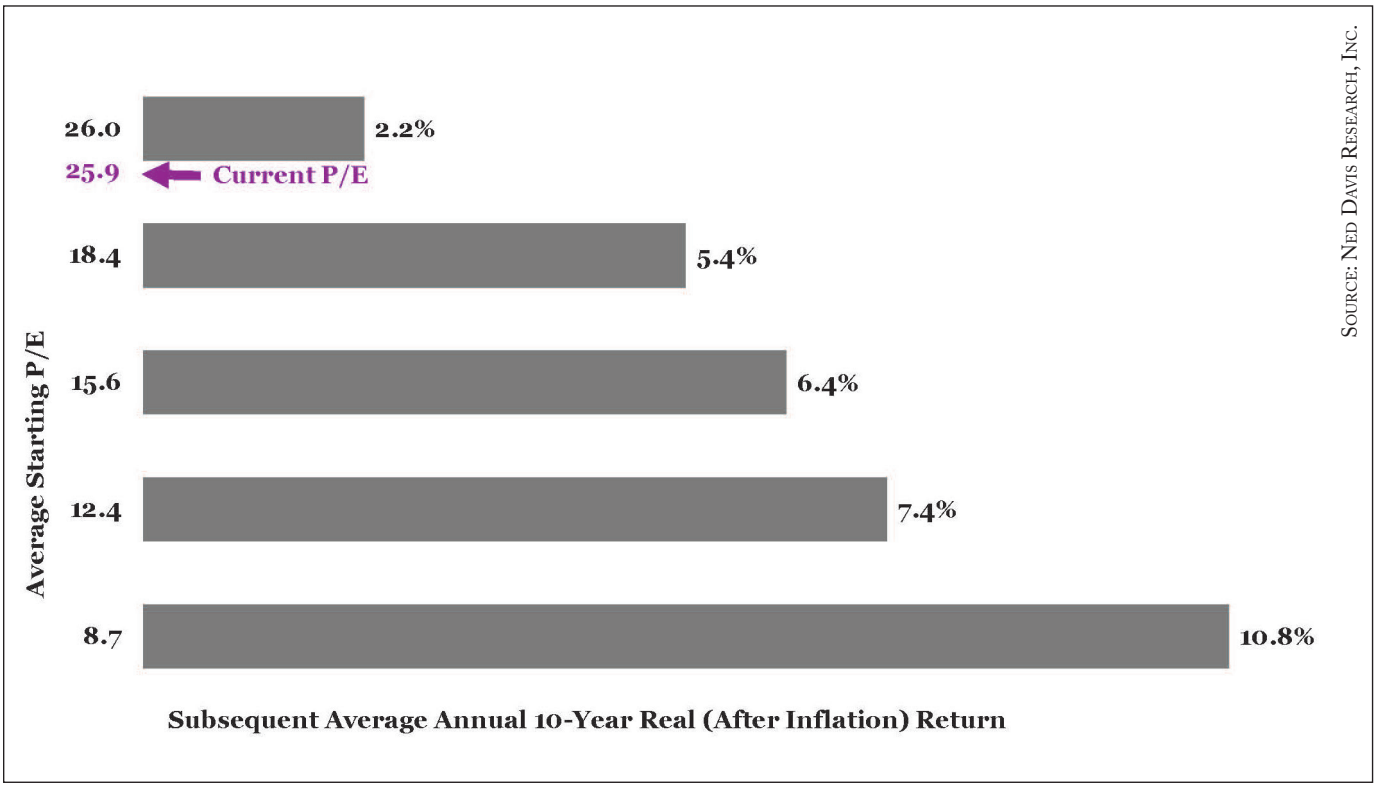
There is, however, a major mitigating factor that must be considered when examining valuation measures today – interest rates. At today's near-record low levels, rates are extremely supportive for the economy and the stock market as consumers and businesses can finance purchases at very low cost. Some strategists argue that traditional valuation methods can't be trusted because low interest rates forced by central bank intervention means there is no alternative to buying stocks.

Perhaps. But I am always skeptical when the argument for the market going higher is "it's different this time." My expectation is that low rates will provide enough of a cushion to boost equity returns significantly higher than the 2.2% implied by the chart, but the market's price-earnings multiple ultimately trends downward toward historic averages. Unless the economy were to significantly accelerate, leading to higher earnings per share, this scenario would still mean below average returns for stocks over the next decade.

Of course, lower average returns have implications for investors planning for the future. Those counting on historically normal returns should consider adjusting their expectations in light of current stock market valuations and interest rate levels. It may be necessary to bump up savings rates or plan to work an extra year or two before retirement. Fortunately, a small course correction made early can help avoid painful decisions later. If you want to talk about what lower returns might mean for your individual situation, please reach out to us.

S&P 500 Average 10-Year Real Return Vs. Beginning Price/Earnings Ratio (10-Year Average Earnings)

January 31, 1881 to June 30, 2016



Retirement Income Planning: Escaping from the Daily Grind

I recently found myself in the market for a new coffee grinder. Having never truly been satisfied with the prior model, I poured myself into researching a replacement. Blade grinder or burr? If burr, conical or flat? Automatic or manual? Altogether, I spent well over six hours determining how best to deliver my caffeine fix each morning.

Although it may not have been a coffee grinder, odds are you too have invested far more time researching some banal household purchase than necessary. But if you are nearing your retirement or are already in the midst of it, how much time have you have considered your income strategy in retirement? Was it more or less than the time spent on your last Amazon.com purchase?

Since the mid 1990's, one of the cornerstones of retirement income advice has been a concept known as the Four Percent Rule. Originally described by William Bengenin, this rule of thumb states that retirees with balanced portfolios consisting of a mix of both stocks and bonds should be able to withdraw four percent of their savings in the first year of retirement, then adjust that amount for inflation each year thereafter. At this withdrawal rate, their retirement portfolios should safely last at least 30 years, i.e. the length of a typical retirement.

Lately, however, the Four Percent Rule has been called into question. The 2008 financial crisis coupled with persistently low interest rates has cast doubt on whether this strategy is sustainable over the lifetime of a retiree. Many criticisms have centered around something known as sequence risk, essentially the risk that a period of extremely poor investment returns (à la 2008) occurs at the beginning of your retirement when it would have the largest impact versus at the end when it would have a smaller one. Other critics have pointed out that assuming a retirement will only last 30 years may be unrealistic considering the increasing life expectancies of most Americans.

Even if there is no such thing as a safe withdrawal rate, the concept was never intended to be a prescription requiring absolute adherence. Most retirees do not spend some predefined number each and every year in retirement; life happens and spending needs wax and wane over time. Not to mention, it should become relatively apparent within the first decade of a retirement as to whether the sequence risk resulting in the worst case scenario has or has not occurred. If you enter retirement with $1 million and 10 years later have $3 million, will you continue to withdraw from your savings based on some inflation-adjusted arbitrary number you set a decade earlier? Nonetheless, establishing a reasonable withdrawal amount is a critical first step for retirement income strategies.

Besides selecting an optimal withdrawal rate, there are other strategies retirees can use to extend the life of their retirement savings. Determining where to locate different types of investments across a retirement portfolio comprised of accounts with varying tax treatment—taxable accounts, tax-deferred accounts like IRA or 401(k) accounts, or tax-exempt Roth accounts—can help make the most out of existing savings. Additionally, the order in which funds are withdrawn from those same types of retirement accounts is important.

Though none of these changes will ever make up for saving too little or spending too much, in aggregate they can significantly impact the longevity of a retirement portfolio.

Unfortunately, when it comes to retirement, there are no easy answers. It is important to have a plan and even more so that you revisit that plan frequently. Working with a financial advisor who is familiar with retirement income planning can also help tremendously.

No matter what you do, avoid placing a greater emphasis on finding your next coffee grinder than you do on providing for your retirement income. Otherwise you may end up with the means to make the perfect cup of coffee yet lack the funds for the beans.

Michael Hopper
Vice President

The Dangers of Senior Isolation

Old age "ain't for sissies." There is some truth to that. Although our Golden Years can be a season to enjoy greater freedom and the fruits of our labor, they may also bring more aches and pains, memory loss, and – hardest of all – the loss of loved ones, resulting in isolation.

No one relishes the idea of aging without a spouse, close family members, or dear friends. However, living alone is a reality for an increasing number of older Americans, especially as Baby Boomers cross the 65+ threshold. According to an AARP 2012 study, about 28% (11.8 million) of non-institutionalized older persons live alone (8.4 million women, 3.5 million men). Also according to the AARP, the number of older adults without children has increased, meaning less family to interact and care for many seniors.

The decrease in social interaction as we get older is significant, and there are many reasons associated with that, including retirement, death of family and friends, loss of hearing and loss of mobility.

Regardless of the causes of senior isolation, the consequences can be harmful. Studies have shown that seniors are twice as likely to die prematurely from loneliness and feeling socially isolated. In fact, loneliness and social isolation are two times more likely to threaten a person's health than obesity, according to a Brigham Young University study.

Tips for Battling Senior Isolation

If you are having feelings of loneliness, what can you do? If you have extra rooms, you might consider having a student live with you in exchange for chores or another senior may move in to offer companionship and shave the costs of utilities. Some roommate matching agencies offer background checks. Another suggestion is getting a pet or going to a local shelter to walk a lonely dog. Pet therapy is medicinal: it can lower blood pressure and anxiety, boost memory and contribute to a sense of well-being.

Volunteering is a great way to connect with people. You could drive elders to appointments and outings or help school-age children learn how to read. If transportation is actually a challenge, consider services such as Uber or Lyft. They make getting around fairly easy and affordable. Social media is a great way to stay connected. Long-term care facilities offer access to GrandCare and ConnectedLiving, and you can always connect with loved ones via Skype, Facebook, and email.

Lynn Bockmeulen
Trust Officer

SPOTLIGHT

Tulsa Habitat for Humanity is dedicated to providing the opportunity of homeownership and building quality, affordable housing in partnership with hardworking, deserving individuals and families in the Tulsa area. Since 1988, the nonprofit has worked with more than 350 families to realize their dream of homeownership.

A common misconception is that Habitat for Humanity simply gives away homes. Instead, the organization provides access to homeownership. Through home sponsorships, individual donations and volunteer time, Tulsa Habitat for Humanity builds affordable and attractive homes that are sold to families through 0% interest loans. In addition to paying for their homes, the home-buyers work side-by-side with sponsors and volunteers to help build their own and other homes. All home-buyers complete the Homeowners College, an intensive program that includes courses on credit management, individualized debt counseling, money management, basic home repair, mortgages and lending process, escrow and taxes, legalities of homeownership and more.

Tulsa's Kendall-Whittier neighborhood is the new strategic focus for the organization. With over 300 vacant lots and 200 boarded up properties, the location offers Tulsa Habitat for Humanity the opportunity to make a measurable impact in a defined geographical area. This redevelopment strategy includes public, private and nonprofit partners focused on education, economic development, sustainability, infrastructure and job creation. It is also important to come up with a home design true to the architecture of the area, remain affordable for homeowners and appreciate in value over time. Through successful partnerships, in 2016 Tulsa Habitat for Humanity has completed three homes in the Kendall-Whittier neighborhood and has acquired more than 20 lots in the area.

All of this is possible only through the support of donors and volunteers. Sponsoring a home, volunteering on a build, donating land, sponsoring a home, donating or contributing monthly through our "Carpenters Club" are just a few ways the community can make a lasting difference in the lives of a family.

To learn more about the organization and how you can help, visit **tulsahabitat.org**.

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COMPANY of OKLAHOMA

P.O. BOX 3627
TULSA, OK 74101-3627

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OPERATIONS DIVISION

Trena Person, Trust Officer; *Dana Davis*, Vice President; *Steve McQuade*, Vice President; & *Jan Sommers*, Vice President.

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