

# CLS's WEEKLY 3

What You Need To Know About the Markets

MAY 28, 2019



1. With more than 2,300 ETFs from more than 160 issuers, the players in this saturated industry need continuous innovation to compete and survive.
2. Staying invested and diversifying across multiple asset classes in a globally diversified and balanced portfolio may provide a greater chance of reaching long-term goals.
3. Avoiding performance chasing, staying diversified, and putting aside bias opens up a larger world of opportunities.

## Market Performance (as of 5/24/2019)

| Fixed Income                                | 10-YEAR | 5-YEAR  | 3-YEAR  | 1-YEAR  | YTD     | QTD    | LAST WEEK |
|---|---------|---------|---------|---------|---------|--------|-----------|
| Cash Equivalent <sup>1</sup>                | +0.43%  | +0.80%  | +1.29%  | +2.23%  | +0.97%  | +0.38% | +0.06%    |
| U.S. Investment Grade Bonds <sup>2</sup>    | +3.75%  | +2.59%  | +2.26%  | +6.22%  | +3.84%  | +0.87% | +0.27%    |
| Equities                                    | 10-YEAR | 5-YEAR  | 3-YEAR  | 1-YEAR  | YTD     | QTD    | LAST WEEK |
| Global Equity Market <sup>3</sup>           | +10.15% | +5.86%  | +10.26% | -0.59%  | +11.15% | -0.84% | -0.87%    |
| Total U.S. Market <sup>4</sup>              | +14.74% | +10.21% | +13.05% | +5.03%  | +14.02% | -0.06% | -1.17%    |
| Domestic Large-Cap Equity <sup>5</sup>      | +14.49% | +10.76% | +13.59% | +6.19%  | +13.40% | +0.19% | -1.17%    |
| Domestic Small-Cap Equity <sup>6</sup>      | +14.36% | +7.08%  | +10.20% | -4.30%  | +13.41% | -1.81% | -1.52%    |
| International Equity <sup>7</sup>           | +6.56%  | +1.88%  | +7.76%  | -6.47%  | +8.27%  | -1.76% | -0.55%    |
| Developed International Equity <sup>8</sup> | +6.76%  | +1.88%  | +7.03%  | -5.60%  | +10.10% | -0.33% | -0.55%    |
| Emerging Market Equity <sup>9</sup>         | +5.98%  | +1.92%  | +10.65% | -8.99%  | +2.89%  | -5.97% | -0.55%    |
| Diversifiers                                | 10-YEAR | 5-YEAR  | 3-YEAR  | 1-YEAR  | YTD     | QTD    | LAST WEEK |
| Diversified Alternatives <sup>10</sup>      | +3.86%  | +0.36%  | +1.45%  | +0.23%  | +3.07%  | +0.11% | -0.16%    |
| Commodity <sup>11</sup>                     | -3.73%  | -9.55%  | -0.87%  | -12.02% | +3.58%  | -2.58% | -1.21%    |

<sup>1</sup>Morningstar Cash Index <sup>2</sup>Bloomberg Barclays Capital U.S. Aggregate Bond Index <sup>3</sup>Morningstar GblMkt Large-Mid Index <sup>4</sup>Morningstar U.S. Market Index <sup>5</sup>Morningstar U.S. Large Cap Index <sup>6</sup>Morningstar U.S. Small Cap Index <sup>7</sup>Morningstar Gbl xU.S. Large-Mid Index <sup>8</sup>Morningstar DM xUS Large-Mid Index <sup>9</sup>Morningstar EM Large-Mid Index <sup>10</sup>Morningstar Diversd Alt Index <sup>11</sup>Bloomberg Commodity Index

## Week in Review

Global equity markets were generally lower last week. Small-cap domestic companies were the worst performers within equities, down more than 1%. Additionally, value companies outperformed growth. International companies beat domestic companies by losing less, both within developed international and emerging markets.

Fixed income did its job as a diversifier as aggregate bonds squeezed out a positive return with the 10-year Treasury yield falling all the way to 2.32%, the lowest level since late 2017. Commodities had a negative week, down over 1% due to a tumble in oil prices amid trade tensions. Diversified alternatives were just slightly negative, helping to dampen market losses.

In economic news, ongoing tariff disputes between the U.S. and China had a particularly negative effect on technology and energy companies over the week. In addition, the U.S. manufacturing PMI (Purchasing Managers Index) for May hit the lowest level since September 2009, highlighting a slowdown in business activity. Elsewhere, Brexit worries continue as Prime Minister Theresa May announced she would step down from her role on June 7 – the market reaction was surprisingly tame.

# Thematic ETFs: The Current Stage in ETF Evolution

*"If there's one thing the history of evolution has taught us, it's that life will not be contained. Life breaks free, it expands to new territories and crashes through barriers painfully, maybe even dangerously, but, uh, well, there it is."*

—Ian Malcolm, *Jurassic Park* (1993)

ETFs were once the baby of the investing world, the newest financial innovation. But it seems they have achieved at least teenager status, as there are now more than 2,300 ETFs available to purchase in the U.S. What may surprise you is that there are 161 unique ETF issuers, according to Morningstar data. Bet you can't name more than 30!

With this saturated ETF landscape, it is getting tougher to compete on price alone, and there are only so many traditional asset classes to re-create.

So, what are all these issuers doing to be different, to compete, and to survive?

They are coming up with new and innovative ways to invest. While mature companies have huge think tanks devoted to product development, which certainly create some revolutionary ideas, it is often the kid sitting in their parents' basement that develops the next great ETF idea.

Currently, some of the best ETF ideas are in the realm of thematic investing. This style of investing

is called thematic because ETFs are being launched with a specific "theme" or idea that may not have existed in the past but could be a meaningful part of the future. Here are the top themes in the marketplace, along with a few ETF ideas on how to play each (we think a great ETF starts with a great ticker!):

## 1. Disruptive Technologies

What are the technologies and innovations that are driving change in our world? These include companies working on artificial intelligence, virtual reality, automated transportation, cybersecurity, space exploration, robotics, and next-generation networking, such as 5G, to name a few.

*SPDR Kensho New Economy Composite ETF (KOMP): Kensho Technologies has partnered with State Street to provide a suite of ETFs revolving around disruptive technologies, headlined by this composite, which includes 16 innovative technology sub-themes.*

*Procure Space ETF (UFO): This recently launched fund gives investors a way to participate in the space race.*

## 2. Demographic Shifts

We have an aging population that needs support and enhancements within the medical field. At the same time, we have tech-savvy millennials eager to make an impact on the

world. And last, but certainly not least, we have a strong movement for women's empowerment.

*Global X Millennials Thematic ETF (MILN): This ETF invests in companies that derive revenue from spending categories associated with millennials.*

*The Long-Term Care ETF (OLD): This fund focuses on long-term care services and products required by an aging population.*

*SPDR SSGA Gender Diversity Index ETF (SHE): SHE tracks companies that employ women in high-level leadership roles.*

## 3. Government Policy

A day doesn't go by without breaking political news, and people are getting more involved and attentive as to what the government is doing. Of course, governmental policies can have a meaningful impact on various companies and industries.

*EventShares U.S. Policy Alpha ETF (PLCY): This ETF invests in companies that may be positively impacted by current and proposed government policies and regulations.*

## 4. Clean Energy

While considered a subset of ESG (environmental, social, and governance), the world's search for clean and renewable energy is truly heating up. With global warming top of mind, there has

## Thematic ETFs: The Current Stage in ETF Evolution (Cont.)

been more focus on reducing carbon emissions across all industries.

*Invesco Solar ETF (TAN) and First Trust Global Wind Energy ETF (FAN): These funds provide exposure to solar and wind energy companies, respectively.*

### 5. Crypto & Cannabis

Everyone's two favorite words over the last couple of years! Growth in both industries has sparked a lot of interest from investors and ETF issuers.

*Amplify Transformational Data Sharing ETF (BLOK): This ETF*

*invests in global companies focusing on blockchain technologies.*

*AdvisorShares Pure Cannabis ETF (YOLO): YOLO provides actively managed exposure to cannabis companies, both in the U.S. and abroad.*



### **Kostya Etus, CFA** *Senior Portfolio manager*

*Konstantin "Kostya" Etus specializes in international investments. He is a co-manager on two mutual funds (aggressive allocation and international) and manager on various separate account strategies, including Core Plus ETF and ESG. In addition, he manages 529 plans.*

*Mr. Etus began his career at CLS in 2011 as a Trading Specialist and became a Research/Portfolio Analyst in early 2013. In 2016, he was promoted to Portfolio Manager. Prior to working at CLS, Mr. Etus worked as an Associate Financial Analyst at ConAgra Foods, Inc., managing the company's global cash network.*

*He graduated from the University of Nebraska at Omaha with a Bachelor of Science degree in Business Administration and obtained Master of Investment Management and Financial Analysis and Master of Business Administration degrees from Creighton University. He holds the FINRA Series 65 securities registration and the Chartered Financial Analyst (CFA) designation.*

*Did you know? [Kostya grew up in Soviet Russia.](#)*



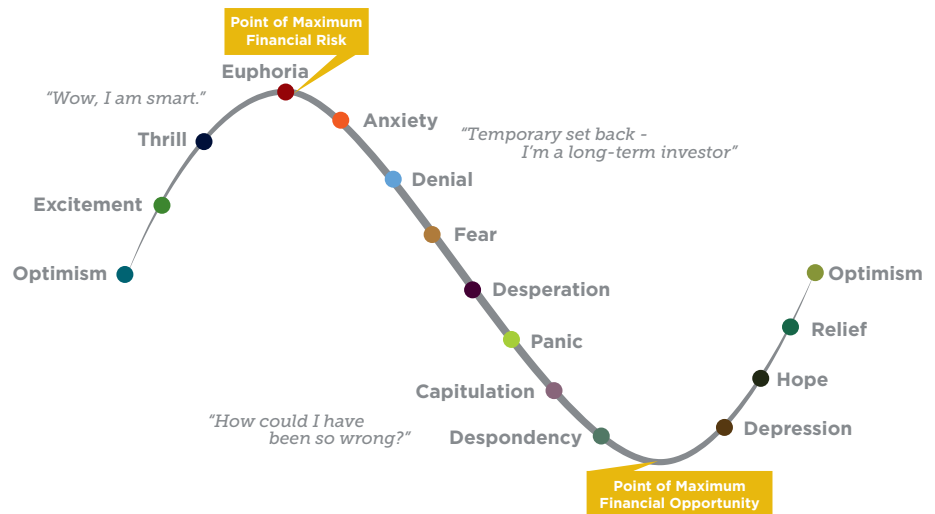
## GLOBAL AND BALANCED: Helping Investors Succeed (Cont.)

exposure to a variety of asset classes limits the negative impact of underperforming allocations. It also provides more stable returns, thereby helping to keep you invested for the long term.

### Saving Us From Ourselves

Most investors understand the negative effects of buying high and selling low. But in times of market uncertainty, emotions can make irrational decisions seem rational. A natural human tendency is to buy at market peaks when things are good and sell during market troughs when fear is high.

To quantify the human nature effect, let's evaluate the difference between investor-driven returns and the actual returns of an investment. The difference



between these two performance figures is known as the "behavior gap" (the cost associated with human behavior). A recent study by Dalbar, an independent research firm, showed that investors lost about 3.6% in average annual returns between 2007 and 2017 because of their

behavioral biases and emotion-based investment mistakes.

**It seems that no matter what people are investing in, they need to be saved from themselves. This is where globally diversified, balanced portfolios come to the rescue.**

## Country Ranks: A 10-Year View

*"Yesterday we were an army  
with no country, tomorrow, we  
have to decide which country  
we want to buy!"*

*–Simon, Die Hard (1995)*

The U.S. is often thought of as having the strongest returns post-2008 (post financial crisis). That is actually not true. Between 2009 and 2018, Thailand, the Philippines, and Indonesia had stronger returns. But what is even more interesting is that the U.S. was not the top performing country in any year within that period – yet another reminder of the benefits of global diversification.

The chart on the following page ranks 47 countries (which are investable through ETFs) by performance each year since 2009. The horizontal black line in the

middle marks the halfway point. There are a few key observations:

**1. Diversification typically works.** Not only was the U.S. never number one, it was in the top half for only six of the 10 years recorded. The MSCI All Country World Index (ACWI) and an equal-weighted average of all the countries were also in the top half for six years, but their rankings were more consistent and stable across time.

**2. Performance chasing can be dangerous.** Typically, the countries at the extremes tend to have a reversal the following year. Notice the downward arrows. The country that was the top performer in a given year tends to be toward the bottom

of the list the following year. This relationship generally holds true on the other end; last year's dogs tend to be this year's winners.

**3. It's a large world out there.**

There are a lot of countries in the world, and through the power of ETFs we can now invest in almost 50 of them. But home and familiarity biases tend to drive U.S. investors to U.S. investments because they are more comfortable with what they know and understand. But an investment manager who can sift through the media noise and evaluate the economic, fundamental, and valuation situations of various countries can have the upper hand due to the vast opportunity set available to them.



## Country Ranks: A 10-Year View (Cont.)

| 2009            | 2010            | 2011            | 2012            | 2013            | 2014            | 2015            | 2016            | 2017            | 2018            |
|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|
| Brazil          | Argentina       | Ireland         | Turkey          | UAE             | Egypt           | Denmark         | Brazil          | Argentina       | Qatar           |
| Indonesia       | Thailand        | Qatar           | Nigeria         | Argentina       | Indonesia       | Ireland         | Peru            | Vietnam         | Peru            |
| Russia          | Peru            | Indonesia       | Egypt           | Greece          | Philippines     | Belgium         | Russia          | Austria         | Brazil          |
| India           | Chile           | New Zealand     | Philippines     | Finland         | India           | Israel          | Thailand        | Poland          | Russia          |
| Turkey          | Colombia        | USA             | Belgium         | Ireland         | Israel          | Japan           | Colombia        | China           | Finland         |
| Norway          | Malaysia        | Malaysia        | Poland          | USA             | Argentina       | Russia          | Canada          | Korea           | New Zealand     |
| Chile           | South Africa    | Philippines     | Colombia        | Germany         | Turkey          | Austria         | Taiwan          | Chile           | USA             |
| Colombia        | Indonesia       | United Kingdom  | Thailand        | Spain           | Qatar           | Italy           | New Zealand     | India           | Israel          |
| Taiwan          | Philippines     | Thailand        | Denmark         | Netherlands     | Thailand        | Finland         | South Africa    | Peru            | Thailand        |
| Thailand        | Sweden          | Colombia        | Singapore       | Qatar           | USA             | Netherlands     | Indonesia       | Turkey          | Malaysia        |
| Australia       | Qatar           | Switzerland     | Germany         | Nigeria         | Peru            | Portugal        | Chile           | Nigeria         | India           |
| Singapore       | Denmark         | ACWI            | UAE             | Belgium         | Taiwan          | USA             | Norway          | Hong Kong       | Hong Kong       |
| Peru            | Mexico          | Norway          | New Zealand     | Japan           | China           | Switzerland     | UAE             | South Africa    | Norway          |
| Korea           | Korea           | Belgium         | Mexico          | Switzerland     | New Zealand     | France          | Australia       | Singapore       | Taiwan          |
| Philippines     | Nigeria         | Australia       | Hong Kong       | France          | UAE             | Argentina       | Austria         | Denmark         | Switzerland     |
| Sweden          | Hong Kong       | Korea           | India           | Denmark         | Denmark         | Hong Kong       | USA             | Thailand        | Indonesia       |
| Argentina       | Singapore       | Mexico          | Austria         | Sweden          | Vietnam         | Germany         | Korea           | Netherlands     | Singapore       |
| China           | Taiwan          | Netherlands     | China           | ACWI            | South Africa    | ACWI            | ACWI            | France          | ACWI            |
| Hong Kong       | India           | Spain           | Australia       | United Kingdom  | Hong Kong       | Sweden          | Qatar           | Greece          | Portugal        |
| South Africa    | Turkey          | Canada          | Sweden          | Italy           | ACWI            | Vietnam         | All Country Ave | Italy           | Colombia        |
| Belgium         | Canada          | ACWI Ex USA     | France          | ACWI Ex USA     | Belgium         | ACWI Ex USA     | Argentina       | All Country Ave | Australia       |
| Mexico          | Russia          | Japan           | Korea           | All Country Ave | Singapore       | India           | France          | Norway          | UAE             |
| Canada          | All Country Ave | South Africa    | Netherlands     | Austria         | Ireland         | New Zealand     | Netherlands     | Germany         | Vietnam         |
| All Country Ave | Japan           | Nigeria         | All Country Ave | New Zealand     | Canada          | Korea           | ACWI Ex USA     | Taiwan          | France          |
| Israel          | Poland          | Sweden          | Switzerland     | Hong Kong       | Switzerland     | Philippines     | Portugal        | ACWI Ex USA     | Poland          |
| Malaysia        | USA             | Denmark         | Peru            | Portugal        | Finland         | United Kingdom  | Germany         | Spain           | Japan           |
| New Zealand     | Australia       | Hong Kong       | Vietnam         | Israel          | All Country Ave | China           | Japan           | Malaysia        | Netherlands     |
| Spain           | ACWI            | France          | South Africa    | Norway          | Australia       | Australia       | Hong Kong       | Philippines     | All Country Ave |
| United Kingdom  | Egypt           | All Country Ave | Norway          | Taiwan          | Netherlands     | All Country Ave | Singapore       | Indonesia       | Sweden          |
| Austria         | Switzerland     | Singapore       | ACWI Ex USA     | Egypt           | ACWI Ex USA     | Taiwan          | China           | Brazil          | Egypt           |
| Netherlands     | ACWI Ex USA     | Germany         | Taiwan          | Malaysia        | Japan           | Mexico          | Sweden          | Japan           | United Kingdom  |
| Poland          | Norway          | China           | ACWI            | Vietnam         | Spain           | UAE             | Poland          | ACWI            | ACWI Ex USA     |
| ACWI Ex USA     | Vietnam         | UAE             | USA             | Canada          | United Kingdom  | Norway          | United Kingdom  | Portugal        | Nigeria         |
| Portugal        | Finland         | Russia          | United Kingdom  | Australia       | Sweden          | Spain           | Spain           | Switzerland     | Denmark         |
| Egypt           | Austria         | Chile           | Finland         | Korea           | Mexico          | Chile           | India           | Finland         | Mexico          |
| Denmark         | United Kingdom  | Taiwan          | Malaysia        | China           | Italy           | Singapore       | Malaysia        | United Kingdom  | Spain           |
| ACWI            | Germany         | Peru            | Russia          | Poland          | France          | Indonesia       | Finland         | USA             | Philippines     |
| France          | New Zealand     | Brazil          | Italy           | Singapore       | Germany         | Qatar           | Switzerland     | Sweden          | Canada          |
| Vietnam         | Brazil          | Portugal        | Canada          | Russia          | Malaysia        | Malaysia        | Philippines     | Australia       | Italy           |
| UAE             | China           | Italy           | Japan           | Mexico          | Korea           | Nigeria         | Ireland         | Belgium         | China           |
| Italy           | Israel          | Israel          | Chile           | Philippines     | Chile           | Thailand        | Belgium         | Ireland         | Chile           |
| USA             | Netherlands     | Poland          | Ireland         | India           | Brazil          | Egypt           | Vietnam         | Colombia        | Korea           |
| Switzerland     | Belgium         | Finland         | Indonesia       | South Africa    | Poland          | Canada          | Turkey          | Canada          | Germany         |
| Germany         | France          | Turkey          | Greece          | Thailand        | Colombia        | Poland          | Mexico          | Mexico          | South Africa    |
| Greece          | UAE             | Austria         | Portugal        | Brazil          | Norway          | South Africa    | Italy           | New Zealand     | Ireland         |
| Ireland         | Portugal        | India           | Spain           | Colombia        | Nigeria         | Peru            | Egypt           | Russia          | Belgium         |
| Finland         | Italy           | Vietnam         | Brazil          | Chile           | Austria         | Turkey          | Greece          | Egypt           | Austria         |
| Qatar           | Ireland         | Argentina       | Qatar           | Indonesia       | Portugal        | Brazil          | Denmark         | UAE             | Greece          |
| Japan           | Spain           | Egypt           | Israel          | Turkey          | Greece          | Colombia        | Israel          | Israel          | Turkey          |
| Nigeria         | Greece          | Greece          | Argentina       | Peru            | Russia          | Greece          | Nigeria         | Qatar           | Argentina       |

Source: Morningstar using MSCI indices, 1/1/2009 - 12/31/2018

This information is prepared for general information only. Past performance is not a guide to future performance.

The Morningstar Global Market Large-Mid Index is an index that measures the performance of the global market's equity markets targeting the top 90% of stocks by market capitalization. The Morningstar U.S. Market Index is an index that measures the performance of U.S. securities and targets 97% market capitalization coverage of the investable universe. It is a diversified broad market index. The Morningstar U.S. Large Cap Index is an index that measures the performance of U.S. large-cap stocks. These stocks represent the largest 70% capitalization of the investable universe. The Morningstar U.S. Small Cap Index is an index that measures the performance of U.S. small-cap stocks. These stocks fall between the 90th and 97th percentile in market capitalization of the investable universe. In aggregate, the Small Cap Index represents 7% of the investable universe. Morningstar Global ex U.S. Large-Mid Index is an index that measures the performance of Global Markets (ex-U.S.) equity markets targeting the top 90% of stocks by market capitalization. The Morningstar DM ex U.S. Large-Mid Index is an index that measures the performance of developed markets ex-U.S. equity markets targeting the top 90% of stocks by market capitalization. The Morningstar EM Large-Mid Index is an index that measures the performance of emerging markets targeting the top 90% of stocks by market capitalization. The Barclay's Capital U.S. Aggregate Bond® Index measures the performance of the total United States investment-grade bond market. The Morningstar Cash Index is an index that measures the performance of a Treasury Bill with six to eight weeks until maturity in the U.S. market. The Bloomberg Commodity Index is made up of exchange-traded futures on physical commodities and represents commodities that are weighted to account for economic significant and market liquidity. This index provides investors with a means of understanding the performance of commodity futures markets and serves as a benchmark for investment performance of commodities as an asset class. The volatility of the indexes may be materially different from the individual performance attained by a specific investor. In addition, portfolio holdings of investors may differ significantly from the securities that comprise the indexes. You cannot invest directly in an index.

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