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About Beacon Financial Advisors Ltd. Beacon is an independent fee-only advisor with a clear mission statement: To provide our clients long-term value-added financial counsel and investment performance with exceptional service. Beacon is a Registered Investment Advisor with the US Securities and Exchange Commission.

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QUESTIONS From Clients
ANSWERS From Beacon



Rates (& Weights) of Investment Return (Part 2)

BEACON'S SERVICE-BRIEF Rates (& Weights) of Investment Return (August 2016) compared/contrasted major asset class historic and projected returns. Summing up, the next several years likely will be less bountiful to investors in stocks and bonds than the long-term past, while volatility won't be meaningfully lower (see p2). **This prompted clients' questions, including why does BEACON use a 3 to 4% lower annual return projection for U.S. and international stocks than long term averages?**

There are but 2 components of a stock's return—income from **dividends**, and capital appreciation from price increases (or decreases as is sometimes the case). The price component has two drivers: the **earnings growth of the company** and the **earnings multiple** investors are willing to pay for that growth—the P/E ratio. As an example consider the “glorious period” from 1980-1998 (just before the Tech crash), the S&P 500 Index grew by 17.7% annually, with the following breakdown:

3.7% Dividend Yield	5.0% Corporate Earnings Growth	8.2% P/E Multiple Expansion	= 17.7% <small>(not additive per compounding)</small>
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The largest component, **P/E multiple expansion**, derived largely from the declining interest rates over 1980 to 1998—P/E's are not infinitely expandable (i.e. trees don't grow to the sky). Corporate earnings growth for the stock market ultimately cannot grow faster than the economy as measured by GDP (gross domestic product). We know the U.S. economy is growing, but at what some call a Plow Horse pace of around 2% annually. Economic growth estimates are not much better in Europe, Japan and the rest of the developed world. In the developing and frontier economies, economic growth is flat due to the crash in commodity prices and US\$ strength, among other things. The consensus about future economic growth is better than today's Plow Horse, but less robust than the past. Finally, today's dividend yield on the S&P 500 Index is but 2% v. the 3.7% above (or 3.5% long-term average). Unlike the “glorious period” of the 1980's and 1990's, today global interest rates are at historic lows and poised to rise over time so there are no brave souls projecting meaningful P/E multiple expansion. Thus, it's projected the next several years (5-10 or so) global stock returns may consist only of **dividends** and **earnings growth**, with slightly faster economic growth from the world's developing and frontier investment markets. Our clients' Financial Goal Plans must factor in

2.0% Dividend Yield	4.0% to 7.0% Corporate Earnings Growth	= 6.0% to 9.0% <small>(excluding compounding)</small>
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this prospect. As always, **BEACON** welcomes your comments and questions.



Rates (& Weights) of Investment Return—MARKET HISTORICAL & PROJECTED RETURNS

Historical Asset Class Returns				Projected Asset Class Returns			
Asset Class Description	1970 - 2015			Asset Class Description	Return	Std Dev	Tax-Free
	Return	Std Dev	Tax-Free				
Cash & Cash Alternatives	4.94%	3.41%	3.25%	Cash & Cash Alternatives	2.50%	2.00%	1.90%
Short Term Bonds	6.39%	4.47%	5.81%	Short Term Bonds	3.30%	2.00%	2.50%
Intermediate Term Bonds	7.37%	6.62%	6.56%	Intermediate Term Bonds	3.50%	6.50%	2.60%
Long Term Bonds	8.68%	10.16%	7.10%	Long Term Bonds	3.30%	12.00%	2.50%
Large Cap Value Stocks	9.97%	16.96%	N/A	Large Cap Value Stocks	7.20%	20.00%	N/A
Large Cap Growth Stocks	10.40%	18.35%	N/A	Large Cap Growth Stocks	6.80%	20.00%	N/A
Mid Cap Stocks	11.23%	18.00%	N/A	Mid Cap Stocks	7.50%	20.00%	N/A
Small Cap Stocks	12.32%	22.94%	N/A	Small Cap Stocks	7.70%	22.00%	N/A
International Developed Stocks	9.45%	22.12%	N/A	International Developed Stocks	8.00%	19.00%	N/A
International Emerging Stocks	8.79%	29.93%	N/A	International Emerging Stocks	9.30%	26.00%	N/A

Historical Portfolio Returns			Projected Portfolio Returns		
Portfolio Name	1970 - 2015		Portfolio Name	Return	Std Dev
	Return	Std Dev			
Capital Preservation I	7.61%	5.90%	Capital Preservation I	4.42%	5.89%
Capital Preservation II	7.98%	7.12%	Capital Preservation II	4.83%	7.64%
Balanced I	8.25%	8.11%	Balanced I	5.10%	8.92%
Balanced II	8.56%	9.43%	Balanced II	5.46%	10.59%
Total Return I	8.79%	10.54%	Total Return I	5.81%	12.09%
Total Return II	9.18%	12.34%	Total Return II	6.27%	14.23%
Capital Growth I	9.63%	14.04%	Capital Growth I	6.70%	16.26%
Capital Growth II	9.92%	15.56%	Capital Growth II	7.10%	18.02%
Equity Growth	10.22%	17.12%	Equity Growth	7.47%	19.80%

Historical Base Inflation Rate		Projected Inflation Rate	
Historical Base Inflation Rate		Projected Base Inflation Rate	
1970 - 2015	4.07%	2.50%	