ATR Advisors

ABSOLUTE TOTAL RETURN
SECOND QUARTER 2016 COMMENTARY

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Climbing a Wall of Worry

Last quarter we predicted that the US stock market would "climb a wall of worry." This turned out to be the case.

As many of the previous macro-economic uncertainties eventually resolved themselves, more and more buyers were drawn into the market. As a result, the S&P 500 Index (SPX) returned almost 2-1/2% for the quarter.

Some Contrarian Calls

This was a profitable quarter for the ATR portfolio, as some of our contrarian investments out-performed.

For example, late in 2015 we started buying Equity REIT's (these are Real Estate Investment Trusts that own tangible real estate). These returned over 6.75% in the 2nd quarter, as represented by the IYR real-estate sector ETF.

Our investment in discounted closed-end funds, which invest in tax-exempt municipal bonds, also paid off. The bonds themselves were up almost 2.6% in the quarter (as represented by the MUB muni sector ETF), and many of the closed-end funds were up much more than that.

Our investment in Taxable Muni's did even better. The Taxable Muni sector, as represented by the BAB sector ETF, was up almost 5.4% in the quarter.

The Paradox of Expensive Thrift

In 1714, the Dutchman Bernard Mandeville, wrote about the paradox of thrift in England:

"As this prudent economy, which some people call Saving, is in private families the most certain method to increase an estate, so some imagine that, whether a country be barren or fruitful, the same method if generally pursued (which they think practicable) will have the same effect upon a whole nation, and that, for example, the English might be much richer than they are, if they would be as frugal as some of their neighbours. This, I think, is an error."

What this meant was that if the entire population saved too much, then total revenues for companies would decline. This would decrease demand and cause a contraction of output, giving employers and employees lower incomes. Eventually the population's total saving would decline because of lower incomes and a weaker economy.

Now, three centuries later, the paradox has come back to haunt us with even greater force. Many central banks in the developed world, have brought their interest rates *below zero*. This means that lenders actually have to *pay money* to borrowers! This has had a profound effect on the US bond market, keeping US interest rates down – because even at low rates the US bonds are still a better investment than the "negative interest rate" bonds in other developed countries.

This truly has made thrift a very expensive virtue around the developed world! We predict that this trend will continue and that long-term interest rates in the US will remain low.

This means that high-income stocks, such as those in the ATR portfolio, will continue to be sought after. We intend to be alert to these opportunities, and to take advantage of them for our clients.