Dear Client

It's been a lazy, sleepy kind of summer — for both the U.S. and the global financial markets.

In fact, it's been that way for most of 2017, with the markets hitting one new high after another amid almost nonexistent volatility.

Until now. The escalation of tension between the United States and North Korea has dominated recent headlines, causing investors to wonder about the impact on the stock market and what financial moves they should be making — if any.

My Edelman Financial colleagues and I decided this would be a good time to write to you, offering our collective thoughts about the current landscape and giving you our recommendations.

Before we do that, let's briefly examine the stock market's unusual behavior so far this year.

Through the first week of August, stock prices have risen slowly and consistently amid rather low volatility. It's been a lazy stream of mostly modest gains — 30 points one day, 50 points another, etc. — that pushed the Dow Jones Industrial Average[1] first past the 20,000 mark, then 21,000 and finally past 22,000 on Aug. 2. The Dow set nine consecutive records through Aug. 7, bringing the year's number of record closes to a whopping 35.

(That sounds like a lot, but 35 is nowhere near a record. The Dow posted 52 record closes in 2014 and 38 of them in 2013. The all-time high was 69 in 1995. But then, 2017 still has four months to go.)

Meanwhile, the S&P 500 stock index[1] registered 30 record highs through the week ending Aug. 11 — its biggest number since 2014. And the Nasdaq composite posted 44 records — the most for it since 1999, according to Dow Jones data.

But was anyone taking notice? When record closes come that often — a little at a time — investors tend to become numb to them. The records begin to feel passé. We might even say it's been a Rodney Dangerfield kind of market this year — getting no respect!

Documenting the market's tortoise-like pace, the Dow's average daily move in either direction in 2017 was only 0.31 percent through Aug. 8 — the smallest swing in 53 years, according to *The Wall Street Journal*. A decade ago, as conditions that would lead to the financial crisis were developing, the average daily move was more than twice that.

What positive economic factors drove the market's rise this year? These four, in combination, have had the greatest impact:

- Inflation remains relatively low, averaging 2.15 percent so far in 2017. It averaged 1.26 percent in 2016 and only 0.12 percent in 2015, according to InflationData.com. Therefore, the Federal Reserve has had little incentive to raise interest rates significantly.

- The U.S. unemployment rate, which was at 4.8 percent (considered full employment) in January, has remained low, even dropping to 4.3 percent in July.
- Corporate profits for the most part have been strong. Of S&P 500 firms that reported theirs by July 31, most exceeded analysts' expectations, according to MarketWatch.
- The VIX (volatility index)[1] fell to a record low of 8.84 — its lowest since its 1993 inception — around the end of July.

But history has shown that — in any year — even though the market may be relatively quiet for several months, news events can sometimes spur more volatility.

As we noted, that happened during the week of Aug. 7, after North Korea's Kim Jong Un threatened to fire missiles near the U.S. territory of Guam.

On Aug. 10, the S&P 500 dropped 1.45 percent, its biggest one-day drop since May 17, and the Dow fell 0.93 percent. The VIX closed above 16 — its highest level of the year. The Dow returned to positive territory again for a few days, but then took a 274-point drop on Aug. 17 — following the reaction to the recent events in Charlottesville, VA.

Since 1928, on average, the S&P 500 has fallen 5 percent or more every 10 weeks and 10 percent or more every eight months, according to AllianceBernstein. It has been more than a year since the last 5 percent decline in the index and 18 months since it incurred a 10 percent loss, says Bloomberg.

Can we expect a 5 percent or greater drop in market prices anytime soon? Well, if there is one constant we can count on regarding market behavior, it's *change*. So you can be sure that, sooner or later, we will see prices decline. What might be the trigger?

Here are several distinct possibilities based on what we've seen in the past:

- So far this year, we've seen major terrorist attacks in France, Belgium, the United Kingdom and, most recently, Spain. There have been many others throughout the world, especially in war-torn Iraq and Afghanistan. Additional terrorist attacks could happen anytime and spark a negative reaction in the markets.
- An uncertain outlook for U.S. fiscal policies if Congress remains deadlocked. The House and Senate need to pass 12 spending bills to keep the government running beyond Sept. 30, and at last check, Washington seems more dysfunctional than ever.
- Further escalation of foreign political tensions — not only with North Korea, but also potentially with Russia, China, Iran and based on what we've seen lately, even Venezuela.

Or there could be a negative event no one sees right now.

Whatever the reason, a downturn in the markets will occur sooner or later.

When that happens, what should you do?

Sadly, more than three-quarters (77 percent) of respondents to a recent survey conducted for the American Institute of CPAs said they believe it's important to make financial decisions *quickly* when new financial news becomes available.

Actually, if you've been a client for a while, you know that we ordinarily recommend that you do just the opposite: *Do not act quickly*.

Remember Brexit? That's when the United Kingdom voted to leave the European Union. It rattled the markets — but only temporarily and not nearly to the degree the pundits predicted. The year before, China shook up foreign-exchange and equity traders with a surprise devaluation of its currency. But that impact, too, failed to last. Before that, there were media-hyped fears that Greece's economy would collapse. Today that too is a distant memory.

Obviously, it would have been a mistake to sell based on any of those events — even though they each seemed pretty scary at the time.

Remember, we continuously monitor events for you. The Edelman Managed Asset Program® also engages in strategic rebalancing, designed to take advantage of occasional market downturns. Thus, you don't need to take any action on your own and we'll inform you if market conditions warrant any further changes.

Thank you for your continued confidence. Be assured we will always do everything in our power to fulfill our fiduciary obligation to serve your best interests.

Regards!

Ric Edelman
Founder and Executive Chairman

P.S. If you have a friend or family member who could use our guidance, please invite them to contact us. We're happy to help!

[1]An index is a portfolio of specific securities (common examples are the S&P, DJIA, NASDAQ, VIX), the performance of which is often used as a benchmark in judging the relative performance of certain asset classes. Indexes are unmanaged portfolios and investors cannot invest directly in an index. Past performance does not guarantee future results.

Investing strategies, such as asset allocation, diversification, or rebalancing, do not assure or guarantee better performance and cannot eliminate the risk of investment losses. All investments have inherent risks, including loss of principal. There are no guarantees that a portfolio employing these or any other strategy will outperform a portfolio that does not engage in such strategies. Past performance does not guarantee future results.

Ric Edelman is an Investment Advisor Representative who offers advisory services through Edelman Financial Services, LLC, a Registered Investment Advisor. He is also a Registered Representative and Registered Principal of, and offers securities through, EF Legacy Securities, LLC, an affiliated broker/dealer, member FINRA/SIPC.

Life, long-term disability, long-term care or other nonvariable insurance products offered through EFS and Edelman Insurance Services LLC in California, license no. 0G00750. Variable insurance products offered through EFLS and EF Legacy Insurance Agency LLC in California, license no. 0L01472.