Polaris Greystone
FINANCIAL GROUP, LLC

The Polaris Perspective

For more information or to schedule an introductory consultation contact us at: info@polarisgreystone.com I (800) 268-9046 I www.polarisgreystone.com

Reflections

Think back just one year. The markets were tumbling based upon fear that the United States would fall into a recession in 2019. After all, this was the longest economic expansion since WWII. It was only a matter of time before we had a recession. There were several theories to why this would happen. One theory was the Fed "was on cruise control" and was going to continue to raise rates until our economic growth started to drop (and they wouldn't have enough time to lower rates to combat a recession). A second theory was that the trade war with China would eventually catch up with us and put us into recession. As we argued then, no recession occurred in 2019. The correction in 2018 was all sentiment driven. And while we consider sentiment in how we manage money, we rely far more on fundamental evaluations, technical evaluations, and understanding the macro-economics driving our economy. As we finish up the last few weeks of the year, I think that it is a great time to reiterate how Polaris Greystone tactically manages investments and why we make the decisions we do in your portfolio.

As a reminder, we have discussed that there are four differing ways that firms manage portfolios (as seen below). On the extreme left and extreme right are "buy and hold" and "market timing" managers. Buy and hold is exactly as it sounds. The manager is more worried about taxes than anything else. It is rare to see a change in the portfolio during any given year. Market Timing managers are either "all in" or "all out" of the market. This means they are either completely correct, or completely wrong with their decisions.

The Four Methodologies of Portfolio Management

- Buy & Hold
- Modern Portfolio Theory
- Tactical Investment Management
- Market Timing

In the middle are your Modern Portfolio Theory managers and Tactical Investment Management managers. Modern Portfolio Theory (MPT) managers are by far the largest, in terms of size and assets under management, of all of the methodologies. An MPT manager seeks to create a portfolio that maximizes your return based upon the risk that you are willing to take in order to get that return. Generally, they create this portfolio by looking at the last five years of performance of different investment classes, one year's worth of correlation of these investments, and one year's worth of volatility (risk). They typically rebalance their portfolios quarterly. My biggest issue with MPT mangers is they are looking 100% in their rear-view mirror to make their decisions for their clients. Think about the tech bubble. Would you have wanted money in tech in 2001 or 2002 as it was cratering? MPT had too much exposure. How about investing in oil and MLPs the second half of 2014 through 2019. It was a blood bath, yet MPT managers held them in their portfolios for far too long because they were performing well prior to their collapse.

Polaris Greystone is a Tactical Investment Management company. We believe in understanding history and learning from it, but we try to make our portfolio management decisions based upon "what is going on now, and where we believe things will be in the near-term future."

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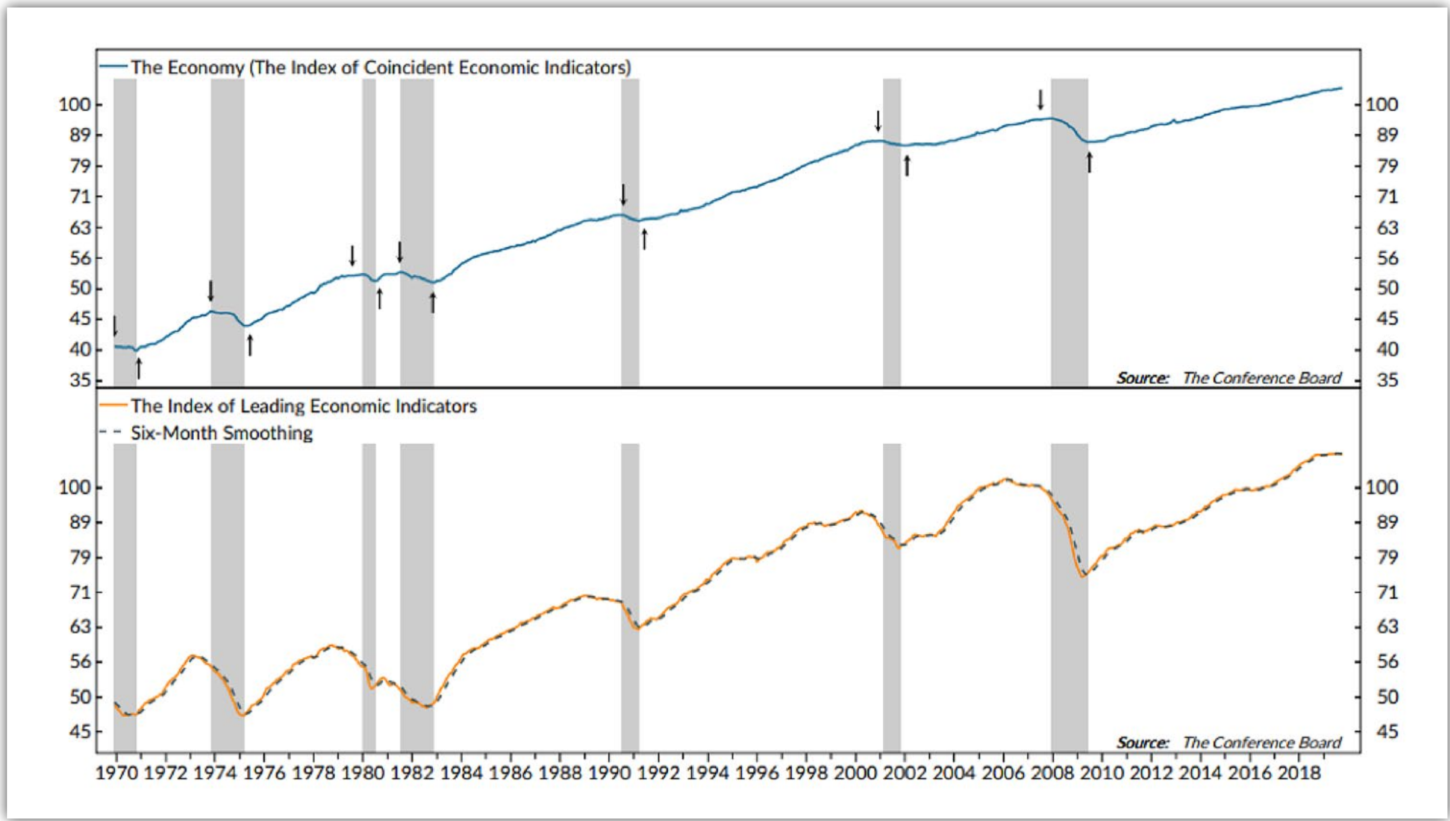
The Four Pillars of Investing

- Macro-Economics
- Technical Research
- Fundamental Research
- Sentiment

Macro-Economics

We use leading and lagging economic indicators to understand not only our economy but the major economies throughout the world. We use research, such as the Chicago Fed National Activity Index, the Index of Coincident Economic Indicators, and the Index of Leading Economic Indicators. As you can see from the chart below, our economic indicators have accurately shown when recessions were to begin. If we were to move close to a recession or enter one, PGFG would get defensive with your portfolio by either going to cash and/or buying defensive stocks.



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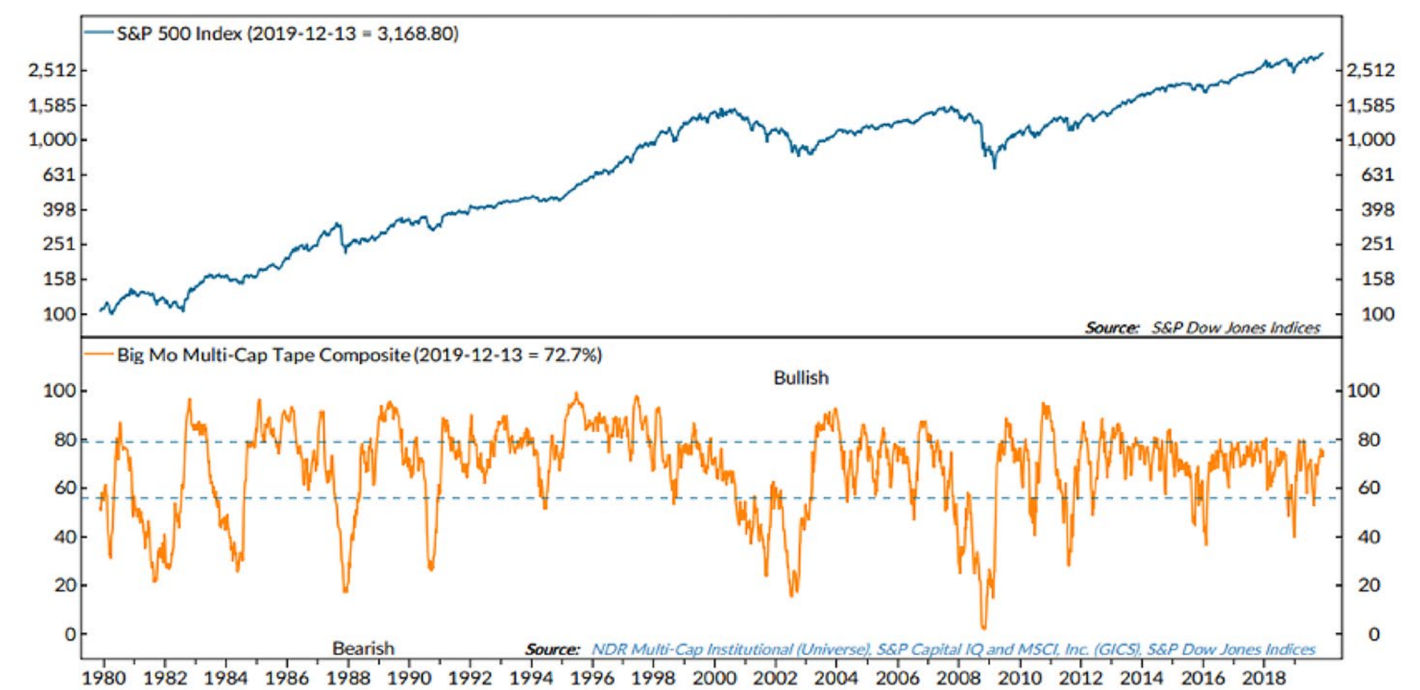
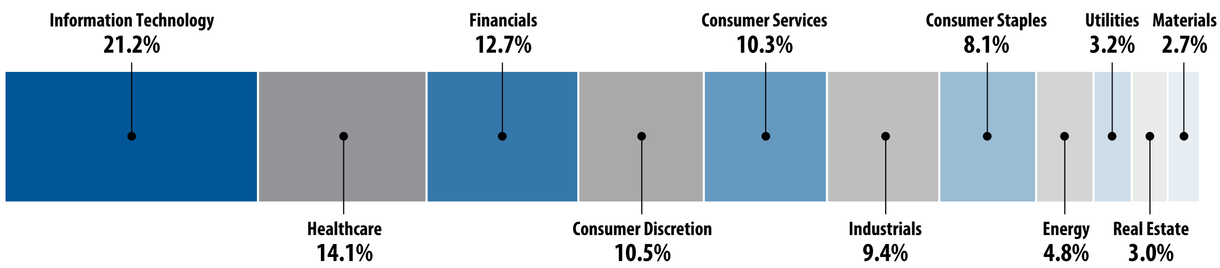
Technical Research

One of the first things that we do is try to understand the overall health of the stock market by looking at the S&P 500 by its parts. We have worked with several independent research providers to help us create a "market barometer" to understand if the markets are bullish, neutral, or bearish. As you can see from the chart below, our "market barometer" has historically shown us when to get defensive and when to try to take advantage of the market conditions.

S&P 500 Index vs. Big Mo Multi-Cap Tape Composite – Directional Mode Basis



Once we've determined the overall health of the markets, we try to understand the health of each of the sectors that make up the markets. As you can see from the graph below, each of the eleven sectors of the S&P 500 have different weightings. We will over or underweight the sectors based upon our research, and in some cases not invest in that sector at all.



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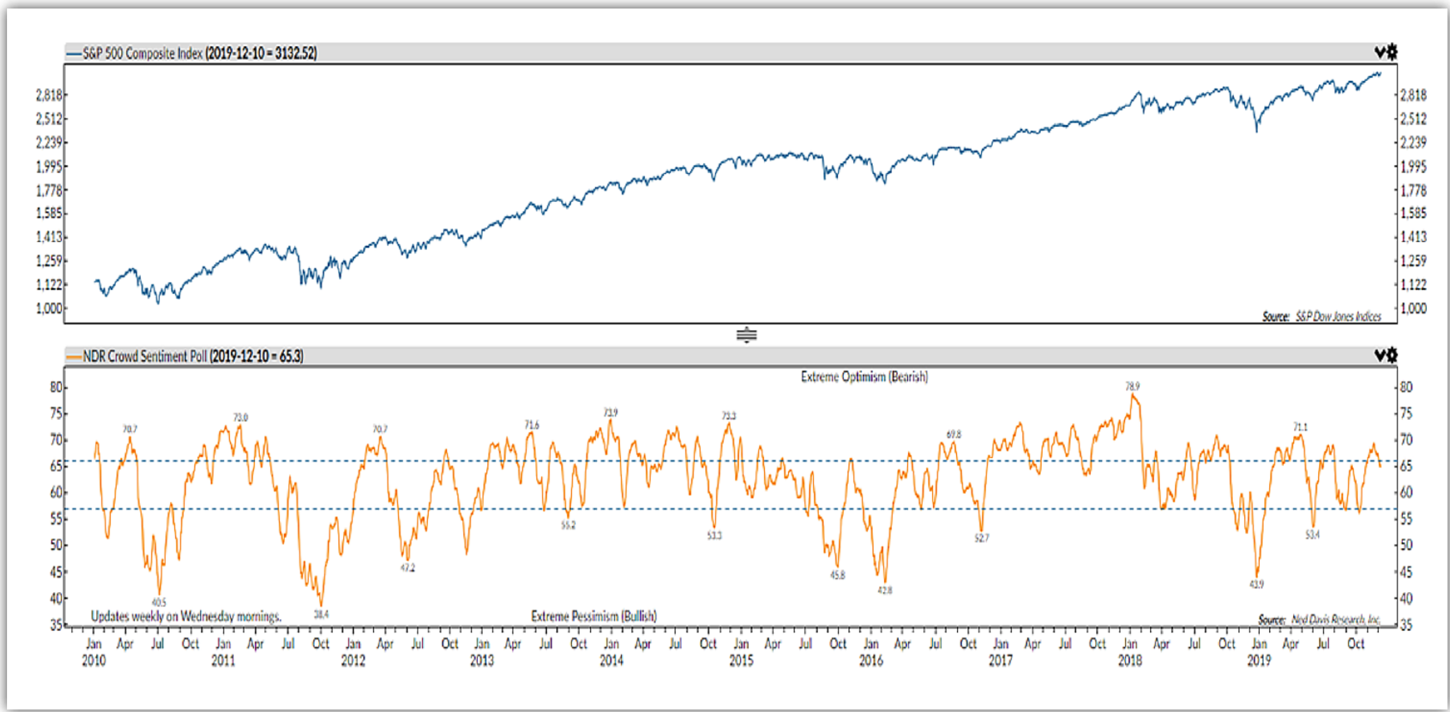
Fundamental Research

Polaris Greystone runs its own proprietary screening models. Each sector of the market has attributes that signal the best companies within that sector. We evaluate hundreds of stocks every week to determine which stocks are the best investment in their particular sector of the market. Once we've determined the portfolio weighting and sector weighting (based upon macro-economics and technical evaluations), we determine which companies would best serve our clients in their portfolios. We chose fundamentally strong companies which are undervalued to where they should be priced given the current market circumstances.

Sentiment

Sentiment is the fourth pillar of our investment strategy. The chart below is a combination of the S&P 500 (above in blue), and our crowd sentiment evaluation (in gold). Sentiment is a contrarian indicator. As you can see from studying the chart below, the more bullish the indicator, the more likely the market is to be at a high and ready to contract. When we get extreme bearish signals, it's typically a good time to invest. We use sentiment, in concert with our other research, to determine your exposure to the stock market.



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Conclusion

This time last year the markets felt like quicksand. The more that you reacted and panicked, the further you sank and the more despair you felt. We chose to look at what was truly going on at the time and not react to the media and supposed pundits who said that we would experience our inevitable recession in 2019. Nothing pointed to what was being said. The macro-economics were well above average. The fundamentals were excellent (24% earnings growth). The thing that sent the markets down last year was sentiment. When sentiment broke down, it dragged down the technicals very quickly.

As dark as things seemed this time last year, we remained disciplined. We didn't sell when we felt uncomfortable. This would have led to us locking in loses at the lows of the market. Instead we remained steadfast, knowing that as bad as it seemed the markets would rebound. Our disciplined approach led to a quick recovery at the beginning of the year and put us into the green during the second half of the year.

Where do things go from here? You'll have to wait until our 2020 Market Outlook webinar on January 15th at 12:00 pm PDT. An invitation will be going out to you in early January with the details. (spoiler alert) We think things will be just fine, but we'll give you our rationale on the Webinar.

As always, I welcome your questions and comments.

Sincerely,

Jeffrey J. Powell
Managing Partner & Chief Investment Officer