KWAG May Update

Good Afternoon. We want to begin this update with a heartfelt thank you for the positive feedback we received regarding the first-quarter newsletter and our recent monthly updates. We appreciate all manner of constructive feedback, whether positive or negative, since it lets us know what our readers find valuable and what they don't. So thank you!

We also want to thank a number of clients for their recent referrals. We understand the gravity of recommending an investment advisor to a close friend or relative, and we appreciate that you believe enough in us and in our services to make these kinds of recommendations. We also want to assure you that we won't let you down and will take extremely good care of those you have referred to us, just as we do with all our clients.

Finally, we want to thank everyone for the kudos sent to our operational staff during the recent tax season. Tax season is a little crazy with all the last minute requests we get, and we can assure you that our staff does their very best to take care of your needs in a timely fashion and is 100% committed to your financial well-being. Over the last few years, we have implemented a number of new processes designed to better serve everyone, so all of the positive comments are encouraging. Of course, we're not perfect, so we also appreciate anyone who reaches out to us to provide constructive criticism. That type of feedback is equally important, as it will make us an even stronger team in the long run!

So, thanks again, from the bottom of our hearts. We at KWAG feel blessed to have such a great group of clients and friends.

Recent Updates

At this point, we hope everyone has had an opportunity to read the recent first-quarter newsletter, which discussed probabilistic reasoning and forecasting. The main point of the newsletter was to offer some insight into the way we view financial markets and explain why a long-term perspective is such a critical determinant of investing success. Using probabilistic reasoning to make long-term investing decisions has been shown to significantly increase the likelihood of success for investors over the long run. A number of readers mentioned how this discussion helped them better understand what we do as investment advisors and why.

We also received positive feedback on our summarization of the five "disconnects" that we included in the newsletter. We appreciate these comments and will point out other disconnects as we see them developing over the next few years. One of the more interesting "disconnects" that we have not covered in great depth is the energy "disconnect." Over the next decade, our country is going to become energy independent, and this will have huge ramifications domestically and around the globe.

A number of you also liked the summary of the stock and bond markets. Specifically, a number of people liked how we reinforced the critical aspect of a long-term perspective and the use of probabilistic reasoning in portfolio construction by embracing the use of small and mid-cap stocks. We also received a number of comments regarding the coverage of our bond strategies that seek to avoid "interest rate

risk” while still providing an inflation-beating return. This feedback is incredibly important, as we always strive to provide a fresh perspective on our approach to wealth management and we want to make sure that our investment process is as transparent as possible. Again many thanks.

The Stock Market

In the first-quarter newsletter we discussed the significant rally we’ve witnessed in the stock market over both the short and long-term. Specifically, we stressed the folly of trying to “time the market” and we encouraged everyone to avoid the temptation of significantly tilting their target asset allocation towards stocks in the midst of this huge rally. Remember, as the stocks continue to rise relative to fixed income investments, the weight of stocks in your portfolio also increases over time. If you chose to increase your target allocation to stocks at this point, you would effectively be doubling-down on something that has been very hot for a long time, which is rarely a good idea.

Of course, the market has continued the rally we saw in the first-quarter and has breached a number of new all-time highs in April and early May. At the time of this writing, the S&P 500 and the Russell 2000 indexes are both up more than 13% year to date. Please note that the longer the rally goes, the higher the likelihood of seeing a typical magnitude (10%-15%) pullback. Frankly, a pullback would probably be healthy at this point because the longer a rally lasts, the larger the pullback generally is once it finally occurs. We don’t have a crystal ball and don’t pretend that we can reliably forecast short-term stock market moves. No one can.

What's Driving the Rally?

The recent run up in stock prices has continued for a number of reasons. First, the European Central bank cut key interest rates for the first time in quite a while, which is viewed as a shot in the arm for the European economy. This came on the heels of the Federal Reserve announcement that they will continue to maintain their accommodative stance for the foreseeable future. This means the Fed will continue growing the money supply while keeping interest rates low. Both moves have (and will continue to) act as stimulus for the stock market.

In addition, home prices have begun to rise and inventories of homes for sale continue to fall, which has the trickle-down effect of creating jobs in a number of different industries. All of these developments act as an economic stimulant, and when you add increasing corporate earnings to the mix, it's not difficult to see why the financial markets have continued to rally. Of course, this rally cannot continue unabated and at some point we will see a correction. Over the longer term, we are still convinced that the stock market will continue to reward patient long-term investors, mostly because the key drivers of growth (low interest rates, relatively cheap labor, improving technology, growing global trade and a growing middle class) remain intact.

The Bond Market

Although it's always nice to see a stock market rally, it's even more impressive to see a bond market rally, especially against far steeper odds. Nonetheless, this is exactly what's happened over the past six weeks. In the month of April, every single one of our bond funds generated positive total returns. While in May, our largest bond holding overall, NEFZX, continued its ascent and is now up 7.25% for the year. Over the last six months, or so, we have been making

changes to our fixed income portfolios in order to reduce exposure to "interest rate risk." So far, these changes appear to be paying off.

In Closing

As usual, if you have any questions about this update, our newsletters, your accounts or our managers, please feel free to call or email us anytime. We hope that you enjoy the remainder of your spring. Again, we thank you for your continued confidence in our firm. And, as you know, we remain 100% committed to your financial well-being.

As a reminder, Joe will be out of the country from May 17th through May 31st. Should you have any needs or questions concerning your account, Joe will be checking emails while away at jkiely@thekielygroup.com. If you need immediate assistance during that time, please email Katie at katie@thekielygroup.com or call our Headquarters office at 877-366-5623.

Enjoy your Spring!

- **Joe and The Gang at KWAG**

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