

October 30<sup>th</sup>, 2015

## **A Look Back**

For investors around the world, 2015 is turning into a year to forget. Stocks, commodities and currency funds were all in the red, and even the measly gains in bonds were wiped out by the little inflation that occurred. Various factors (listed below) contributed to the widespread decline in asset prices:

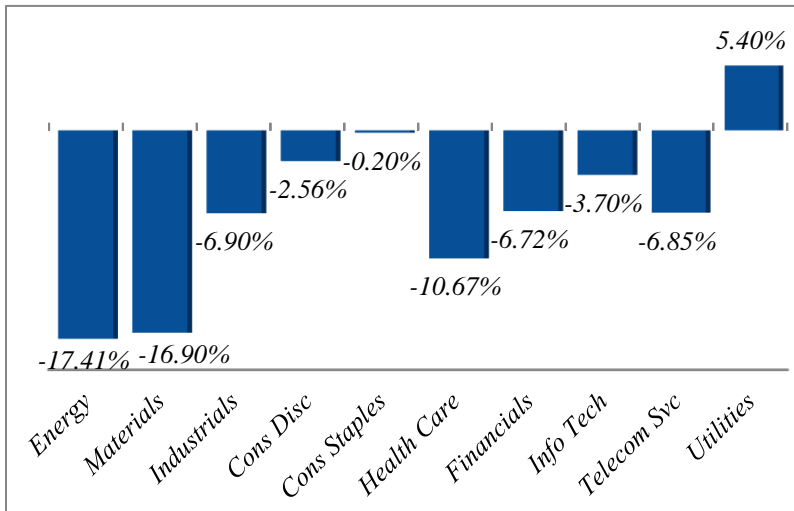
- Geopolitical instability in various parts of the world;
- A strong dollar which could negatively impact sales and profits for U.S. multinationals;
- Weak petroleum prices which negatively impacted both capital expenditures and hiring in that sector;
- Spreads in the high yield debt market widened dramatically as investors began to fret about a pick up in the default rate (particularly in petroleum related businesses);
- The slowdown in China.



Wall Street is clearly on a losing streak. Stocks just posted their third straight quarter of losses - this is the longest string of down quarters since the last financial crisis. Blue chip stocks (as measured by the Dow Jones Industrial Average) at one time were down over 2,100 points for the year, with most of these losses coming since China devalued its currency on August 10<sup>th</sup> (a surprise move that led investors and economists to question whether the world's number two economy is in worse shape than originally thought).

### 3rd Quarter Performance

Nothing worked in the 3<sup>rd</sup> quarter. Commodities tanked, the high yield bond market cratered (particularly energy issues), and the stock market experienced its worst quarterly performance since 2012. ***There was almost no place to hide. Nine out of the ten sectors that comprise the S&P 500 were in the red with utilities being the sole positive performer advancing 5.4%.*** Energy and Materials were the clear losers declining 17.41% and 16.90% respectively.



The worst performing index was the Russell 2000, a basket of small capitalization stocks which declined by 11.92%. The S&P 500 declined by 6.44%, but that doesn't tell the real story, as a significant number of the 500 stocks that comprise that index tumbled by more than 10%. A good many stocks within the S&P 500 have fallen by 20% or more during the nine months of calendar year 2015.

Although the stock market is not nearly as inexpensive as it was in 2008 and the first half of 2009, there are still many stocks that are

quite cheap and could significantly increase in value over the next five to ten years. ***Our work indicates that there is no asset class on a relative basis that is as inexpensive as stocks.***

### Some Thoughts About Investing

As we have mentioned many times in the past, on an emotional level nobody likes stock market corrections. However they are an integral part of the investing process, and without them one could never experience outside future gains. How deep and long the current slide will be is anybody's guess, but we have learned the prudent approach is to stay the course, have ample cash reserves, and the courage to use them when stocks go on sale.

***Furthermore, an investor should remember it is time in the market and not market timing that counts.*** Emotionally, particularly during steep market declines staying the course can become intolerable, but missing just a handful of days can be injurious to your long term financial well-being.

*For example, by missing just the market's five top-performing days over the 20- year period from January 1, 1994 to December 31, 2013, an individual who started with \$100,000 and remained invested for the entire period would have accumulated \$582,287, while an investor who missed just five of the top-performing days during that period would have accumulated only \$386,550.*



### Some Thoughts About The Stock Market

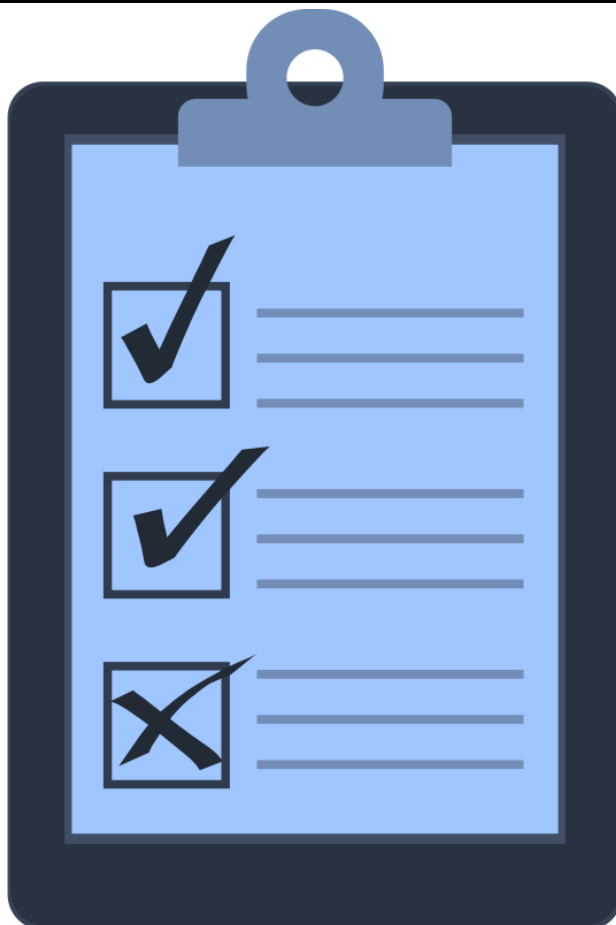
We have been lamenting that the stock market was void of volatility for years, which is highly unusual. Well it finally arrived with a vengeance. There was a five-day stretch in August during which the S&P 500 dropped 11%- the first "correction" of over 10% since 2011. Furthermore, a significant number of stocks fell 20% or more during that time-frame. Several trading days during the quarter saw sharp moves (in both directions), and the financial press did its best to create anxiety among investors. While we certainly do not celebrate declines

in the value of stocks held in our portfolios, cheaper prices often present opportunities to deploy our cash reserves to make investments that we anticipate will reap rewards in future years.

The big questions though are how long and deep will the correction be, and how aggressively should we buy as stocks fall? Given the uncertainty of the health of the global economy as illustrated on page one of this letter, one might conclude it is a time to be cautious and maintain a higher than normal cash reserve. However, we have learned from years of experience, global economic and political problems in the majority of instances appear more dire than they are, and the stock market tends to overreact more than is warranted.

So our method of dealing with these factors is to focus on the business values of individual companies. At times the market becomes irrational, and allows you to buy businesses at fire sale prices. Remember, that the price of a stock on any given day is merely what someone is willing to pay for it. It has nothing to do with the true value of the company. So you buy regardless of what is happening in the world. In most instances you will never buy at the low, but if you are valuing the business accurately, and buy it at a steep enough discount to its private market value, overtime you will compound at a very satisfactory rate. Investors eventually recognize business value, and if not a buyer of the entire enterprise will emerge.

### What is the Ideal Environment to Purchase Stocks?



*Source: The Boyar Value Group and Bill Miller*

You can always find numerous reasons not to invest in the stock market. However, it is our opinion that as a result of the recent stock market decline and the reasons enumerated above; if you are a patient long-term investor the environment to own equities could not get much better.

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*We have been warning for years about the possible dangers of ETF investing. The article below discusses some recent problems that have occurred with this increasingly popular investment vehicle. Unfortunately we think these problems could just be the beginning. Caveat Emptor.*

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## **The Problem with ETFs**

One of Wall Street's most popular products faces questions after wild swings in stocks.

The extreme stock-market gyrations in August exposed cracks that many critics had warned about in the booming business of exchange-traded funds—cracks that fund managers such as BlackRock Inc. are now acknowledging as they work to figure out what went wrong.

At issue is one of Wall Street's most popular products ever. Investors have poured hundreds of billions of dollars into ETFs over the past decade, drawn by low fees and the prospect of being able to buy or sell a mutual-fund-like product whenever they want like a stock. But trading records and conversations with investors show ETFs couldn't keep that promise when the Dow Jones Industrial Average dropped more than 1,000 points in the first minutes of trading on Aug. 24<sup>th</sup>. Steep share-price declines that Monday triggered a slew of trading halts that started in individual stocks and cascaded into ETFs.



Dozens of ETFs traded at sharp discounts to the sum of their holdings, worsening losses for many fund holders who sold during the panic. The strange moves highlighted concerns raised by academics and others over the years that ETFs might not be as easy to move in and out of as advertised in times of stress.

One fund hit by the dislocations was BlackRock's iShares Select Dividend ETF, which trades under the ticker DVY and holds shares of U.S. companies that consistently pay dividends. Its largest holdings include Lockheed Martin Corp., Kimberly-Clark Corp. and McDonald's Corp.

At 9:42 a.m. in New York on Aug. 24, the ETF tumbled 35% to \$48, its lowest level of the day. At the time, the combined weighted values of the stocks the ETF held was \$72.42, down just 2.7% for the day, accord FactSet....

The disruptions could also slow the growth of what has been one of Wall Street's greatest success stories in recent years. A spokeswoman for BlackRock, one of the world's largest ETF providers through its iShares business, said the firm generated \$3.26 billion in ETF-related revenue last year, 29% of the company's total. Other major ETF providers include State Street Global Advisors and Vanguard Group.

Assets in ETFs in the U.S. have grown to roughly \$2 trillion from \$305 billion a decade ago, according to research and consultancy firm ETFGI LLP. In July, U.S. exchange-traded products, a group that includes ETFs, represented just over one-quarter of total stock-trading volume, according to NYSE Group. That compares with 14.9% a decade ago...

This isn't the first time trading issues have plagued exchange-traded products. In 2012, the Velocity Shares 2x Long VIX Short Term Exchange note, a more complex product that not only tracks stock-market volatility but also operates with leverage, plunged even though actual volatility in the market was little changed.

There is also growing concern about how bond ETFs, a popular niche, will perform if investors rush to the exits, as some predict might happen when U.S. interest rates rise.

The trading turmoil of Aug. 24 disrupted the arbitrage activity in which traders buy and sell ETFs and their components to take advantage of price discrepancies. Those market mechanics are the key to keeping fund values in line with their underlying assets and make all-day trading possible. “I don’t think we are happy with what we saw coming from ETF trading on the early morning of the 24th,” said Jim Ross, who heads State Street Global Advisors’ line of SPDR ETFs...

Still, the breakdowns highlighted the risk of promising instantaneous pricing of products that are assembled from dozens of individual stocks. Some observers have warned for years that this was a recipe for a breakdown.

—Excerpt from *The Wall Street Journal* in an article written by Corrie Driebusch, Saumya Vaishampayan and Leslie Josephs on September 14, 2015.

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*The expression the “early bird gets the worm,” does not seem to hold true for equity investors according to the article below. For what it is worth, Boyar Asset Management rarely if ever trades securities at the stock market open.*

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### **Early Birds Suffer in Market**

Rising stock-market volatility is proving especially costly for retail investors who typically buy and sell stocks soon after the market opens—often the most perilous time of the trading day.



Buying and selling by individual investors is especially heavy in the minutes immediately after the market opens in the U.S. at 9:30 a.m. Eastern time, when the chances of getting the best price for a stock are lower and swings tend to be bigger, traders and other market observers said.

But within minutes, the gap between the price sellers want for a stock, known as the “ask” price, and what buyers are offering, the “bid,” shrinks sharply and continues to narrow up until the end of the trading session. This quirk in the market has been amplified in recent weeks amid the big market swings.

The smaller gap, or spread, is better for investors because they are less likely to overpay for a stock or sell below the prevailing price in the market. The wider the spread, the more exposed investors are to high costs, which can erode returns at a time when major stock indexes are down for the year.

In the first half of the year, the difference between the bid and ask prices of shares in the S&P 500 was 0.84 percentage point in the first minute of trading, according to data from ITG, a brokerage. That gap shrinks to 0.08 percentage point after 15 minutes and to less than 0.03 percentage point in the final minutes of the trading

day. This difference often amounts to only pennies a share. But it can add up for the many individual investors who pile into the market early in the trading day...

“The overall cost to trade is lower, and the risk of getting a bad trade is lower, if you wait 30 minutes after the market opens,” said Scott Kubie, chief strategist at CLS Investments LLC, an asset manager that invests mostly through exchange traded funds. After a half-hour passes, the gap between the bid and ask prices narrows and big swings abate, Mr. Kubie said. “At that point, whatever orders had been pushed in from people the night before are done, and you can avoid the swings,” he said.

To be sure, volatility can be beneficial if it allows an investor to buy or sell stocks at a more favorable price. Trades for individual investors tend to be executed in the morning, because they put in orders the previous evening through their online brokerage accounts or their financial advisers, often after they have been able to catch up on the news after work. About 15% of average daily trading volume is driven by individual investors, according to TABB Group, a research and consulting firm focused on financial markets.

Stock-trading volumes in general tend to be clustered near the market open and close, but large institutional investors tend to congregate toward the end of the day, The Wall Street Journal has reported. In 2014, more than 13% of all trading volumes took place between 9:30 a.m. and 10 a.m., a figure that has held steady for the past five years, according to trading data compiled by Credit Suisse. The opening 10 minutes accounted for nearly 5% of volumes, according to the bank...

—Excerpt from *The Wall Street Journal* in an article written by Dan Strumpf and Corrie Driebusch on September 15, 2015.

### **Jihadis Generate \$500m from Oil as US-Led Air Strikes Miss Target**

A year of bombing, more than 10,600 strikes and a coalition of more than 60 countries have failed to make a significant dent in ISIS’s war chest, with revenues from oil, its main source of income, generating as much as \$500m a year. Production figures from workers at oilfields, checked against western intelligence estimates, indicates as much as 34,000-40,000 barrels a day are being produced in ISIS-controlled territory, generating up to \$1.53m a day.

In a striking admission of failure in the US-led fight against ISIS, senior western diplomats and intelligence officials say a recent reassessment of the jihadis’ financial strength suggests it has yet to be depleted in a way that hampers their operations. It is a finding corroborated in dozens of interviews with people in Syria and Iraq involved with the ISIS moneymaking machine, as part of an investigation by the Financial Times. ISIS income from oil exceeds revenue from other sources such as taxation, extortion and the trade in stolen antiquities.

Senior figures in the US-led coalition battling ISIS, in Europe, the Middle East and Washington, say it has adapted its operations to air strikes and runs its trade network with impunity, siphoning millions from oil wells as if it were a national oil company. “This year, we calculated they made \$40m [from oil] in just one month,” said a US official. “That is even after the air strikes....”

It is a contrast to the success the US and its allies enjoyed in degrading the financial clout of al-Qaeda in the wake of the 9/11 attacks. Unlike its rival, ISIS can generate most of the money it needs from within its borders and does not depend on covert foreign fundraising...

Many of the dozens of remaining facilities are operated by local people unaffiliated to the terrorist group. The truckers who move crude oil and refined products around ISIS territory — whose convoys are often visible

from the air — are also not necessarily ISIS members, is a dilemma for military planners. “The transport system [for oil] is indistinguishable from other regular trucks,” said one senior western diplomat. “So we can’t bomb them.”

“You kill the driver, you get a family of jihadis,” he said. “You run the risk of radicalizing the population.” Interrupting the flow of oil across ISIS borders has had limited effect. There is still a huge domestic market over which ISIS holds a monopoly. “They are generating an awful lot of money internally,” said the US official. Among options considered by the coalition are supplying oil at cheaper prices to non-ISIS groups in Syria or flooding the northern Iraqi market with cheap crude to undercut the jihadis.

Western diplomats and intelligence officials are confident ISIS’s finances will reach a “pinch point” — though when is still unclear...

—Excerpt From an article written in *The Financial Times* by Sam Jones and Guy Chazan on October 15, 2015.

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*Below is an excerpt from a story about a reporter who was jailed in China for literally reporting bad news. This one striking example (there are many others) of heavy-handed government intervention in the financial system is one of the many reasons why we do not invest in Chinese equities.*

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### **China Reporter Confesses To Stoking Market ‘Panic And Disorder’**

A leading journalist at one of China’s top financial publications has admitted to causing “panic and disorder” in the stock market, in a public confession carried on state television.

The detention of Wang Xiaolu, a reporter for *Caijing* magazine, comes amid a broad crackdown on the role of the media in the slump in China’s stock market, which is down about 40 percent from its June 12 peak. Nearly 200 people have been punished for online rumor-mongering, state news agency Xinhua reported at the weekend.

*“I acquired the news from private conversations, which is an abnormal way, and added my personal judgment and subjective views to finish this story,” said Mr Wang in a confession aired on China Central Television. “I shouldn’t have released a report with a major negative impact on the market at such a sensitive time. I shouldn’t do that just to catch attention which has caused the country and its investors such a big loss. I regret . . . [it and am] willing to confess my crime...”*

The wider clampdown has also targeted those spreading online rumors about the recent fatal explosions in Tianjin and “other key events.” According to Xinhua’s report, crimes punished include claiming a man had jumped to his death in Beijing because of the stock market slump... David Bandurski of the China Media Project at the University of Hong Kong said he was deeply concerned by the detention.

“This isn’t about the factual nature of his reporting, it’s about the political impact. This looks like a vendetta,” Mr Bandurski said, noting that it was much more worrying than previous cases of journalist detentions that have involved allegations of revealing state secrets or media corruption.

China’s leaders reckon they erred on the side of being too transparent in handling the slide in Chinese equities. When the market turmoil began in June, Beijing imposed restrictions on media reporting of the stock market.

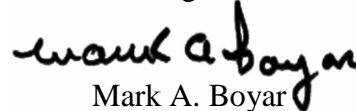
The independent China Digital Times, which monitors internet censorship in the country, said in June media were told to avoid stoking panic.

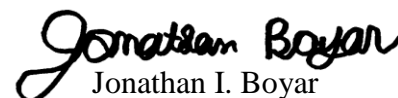
“Do not conduct in-depth analysis, and do not speculate on or assess the direction of the market,” it reported an official directive as saying. “Do not exaggerate panic or sadness. Do not use emotionally charged words such as ‘slump’, ‘spike’ or ‘collapse’.”

—Excerpt from the *Financial Times* from August 31, 2015

If you have any questions or comments, please do not hesitate to call.

Best regards,

  
Mark A. Boyar

  
Jonathan I. Boyar

IMPORTANT DISCLAIMER

*Past performance is no guarantee of future results. Investing in equities and fixed income involves risk, including the possible loss of principal. The S&P 500 Index is included to allow you to compare your returns against an unmanaged capitalization weighted index of 500 stocks designed to measure performance of the broad domestic economy through changes in the aggregate market value of the 500 stocks representing all major industries. The Russell 2000 is an index measuring the performance of approximately 2,000 small-cap companies in the Russell 3000 Index, which is made up of 3,000 of the biggest U.S. stocks. The NASDAQ Composite is a market-capitalization weighted index of the more than 3,000 common equities listed on the NASDAQ stock exchange. The Dow Jones Industrial Average is a price-weighted average of 30 significant stocks traded on the New York Stock Exchange and the NASDAQ. The volatility of the above-referenced indices may be materially different from that of your account(s), and the holdings in your account(s) may differ significantly from the securities that comprise the above-referenced indices. Your results are reported gross of fees. The collection of fees produces a compounding effect on the total rate of return net of management fees. As an example, the effect of investment management fees on the total value of a client's portfolio assuming (a) quarterly fee assessment, (b) \$1,000,000 investment, (c) portfolio return of 8% a year, and (d) 1.50% annual investment advisory fee would be \$15,566 in the first year, and cumulative effects of \$88,488 over five years and \$209,051 over ten years. This material is intended as a broad overview of Boyar Asset Management's, philosophy and process and is subject to change without notice. Account holdings and characteristics may vary since investment objectives, tax considerations and other factors differ from account to account.*