MARKET INSIGHTS
BULL BEAR NEWS

DEC 2017

WBI®

S&P 500 AND MSCI WORLD
ARE THESE TWO INDEXES REALLY A WORLD APART?

A couple months ago, I wrote that many passive ETFs are overweight the 20 largest companies of the S&P 500, especially the so-called "FAANG" companies (Facebook, Apple, Amazon, Nvidia – instead of Netflix – and Google), and that it's easy for investors to be overly reliant on these stocks, whether or not they know they are. As 2017 comes to a close, I wanted to pass along words of caution as investors plan to rebalance their portfolios for the new year: Buyer Beware, you may not be as diversified as you think.

FOR MORE ON THIS TOPIC

BREAKING DOWN INDEX CONSTRUCTION: FAANG IS ONLY THE HALF OF IT

wbiinvestments.com/news/news-insights/16-market-commentary/148-breaking-down-index-construction-faang-is-only-the-half-of-it

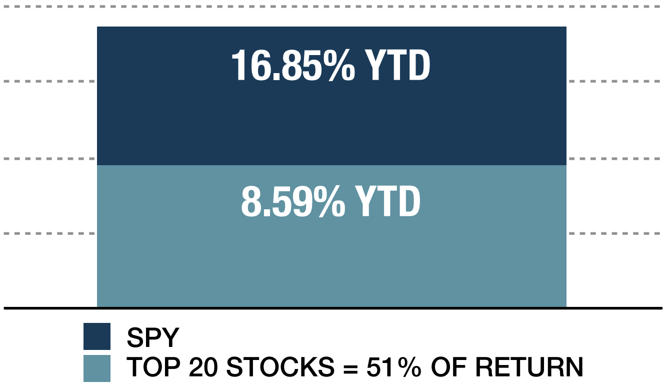
The Dow recently hit the 24,000 milestone, and it's understandable that investors are excited about the all-time highs markets continue to achieve this year. It's also not surprising that investors want to capture the biggest returns possible. However, I'd ask them to consider the where this return is coming from.

MATT SCHREIBER | PRESIDENT & CHIEF INVESTMENT STRATEGIST

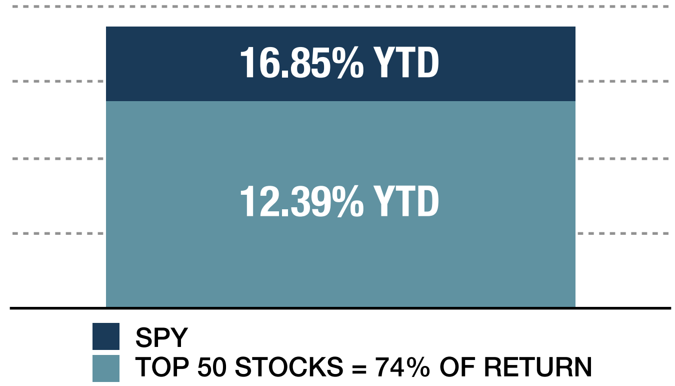
ARE THESE TWO INDEXES REALLY A WORLD APART? CONTINUED

The largest companies in the S&P 500 continue to drive the bus. The investable equivalent of the S&P 500 – the passive ETF SPY – is up 16.85% this year (as of November 20). The top 20 stocks account for 8.59%, or 51% of the year-to-date return. The top 50 stocks are responsible for 74% of the return (12.39%). In other words, just 10% of S&P 500 companies – 50 out of 500 – are driving the vast majority of returns.

TOP 20 S&P 500 STOCKS



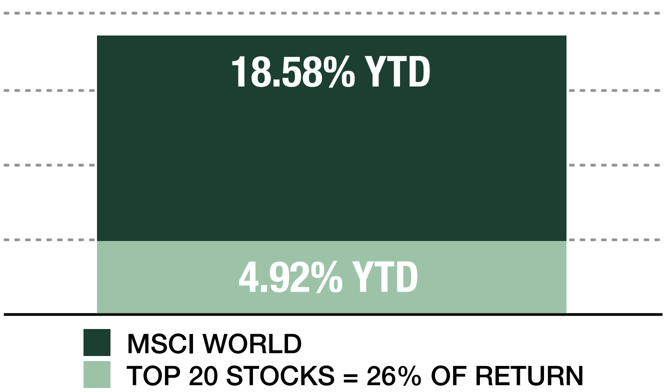
TOP 50 S&P 500 STOCKS



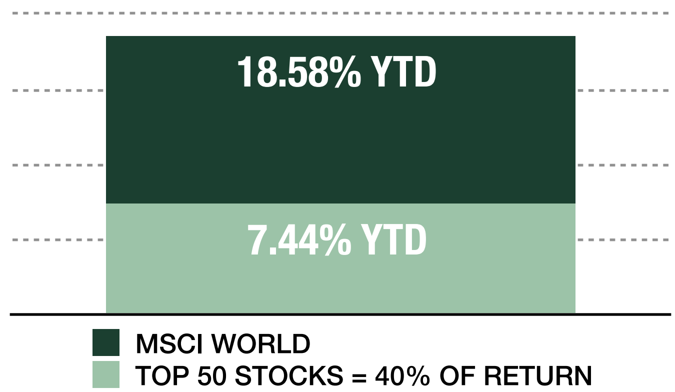
The global version of the S&P 500 has the same concentration issues. Another passive ETF, MSCI World, contains 1,652 stocks from every developed market in the world. However, 18 of MSCI World's top 20 stocks are identical to those in SPY. Honestly, this isn't surprising considering that with few exceptions, the world's largest companies are headquartered in the U.S.

The world's largest companies also disproportionately impact returns. Similar to SPY, MSCI World is up 18.58% this year, with the top 20 stocks responsible for about a quarter of the return (4.29%) and the top 50 accounting for 40% of it (7.44%). Think about that: only 3% of the companies in this global index are providing 40% of the total return.

TOP 20 MSCI WORLD STOCKS



TOP 50 MSCI WORLD STOCKS



Still with me? Good. Here's what all those numbers mean: investing in an ETF like SPY or MSCI World may seem like a simple way to diversify your portfolio, but you may be investing in the same few companies many times over. If those top-20 or top-50 stocks end up performing poorly, the entire index could fall precipitously.

Furthermore, these passive ETFs are capitalization weighted, meaning that the lion's share of money invested in them goes to the top-performing stocks. Should a market downturn or recession cause investors to pull capital from these ETFs, the largest companies would be disproportionately impacted.

Simply put: know what you own. For both investors and advisors, December is the perfect time to assess portfolios and make sure they're broadly diversified. One way to reduce concentration issues is to look at active products and managers who don't all own the same stocks. Passive products have a place in most portfolios, but solely relying on them could be an incredibly costly mistake. Remember that investing, at its simplest form, works best when you buy low and sell high. That means identifying companies with the right fundamentals, not necessarily the largest or best-performing ones. Passive products can't provide the level of precision and research required for this approach.

I think we can all agree that in many ways, 2017 was an unpredictable and tumultuous year. Through both the good (a stock market reaching new record highs) and the bad (cataclysmic weather events), it taught us that we can't take anything for granted. Much as we are a community of financial prognosticators, we don't know what we don't know, in a manner of speaking. Will Congress pass tax reform, infrastructure spending and other growth policies? Will the markets continue to rise? Regardless, the time to plan for 2018 is now.

FOR MORE ON THIS TOPIC

LISTEN TO BULL | BEAR RADIO

Episode 9: Passive Indexed Products Myth Debunked | WBIR: A Global Tactical ETF | Guest Host Gary Stroik

On this episode, Matt and CIO Gary Stroik discuss the risks in today's market environment and what you can do to protect your investments. Plus, Gary explains how WBI Tactical Rotation Shares (WBIR) gives you the world.

https://soundcloud.com/wbiinvestments/ep-9

Each week WBI President Matt Schreiber hosts Bull | Bear Radio with co-host Don Schreiber, Jr., to provide wealth-building insights that keep you on top of the markets.

IMPORTANT INFORMATION

Past performance does not guarantee future results. The views presented are those of Matt Schreiber, and should not be construed as investment advice. Matt Schreiber or clients of WBI may own stock discussed in this article. All economic and performance information is historical and not indicative of future results. This is not an offer to buy or sell any security. No security or strategy, including those referred to directly or indirectly in this document, is suitable for all accounts or profitable all of the time and there is always the possibility of loss. Moreover, you should not assume that any discussion or information provided here serves as the receipt of, or as a substitute for, personalized investment advice from WBI or from any other investment professional. To the extent that you have any questions regarding the applicability of any specific issue discussed to your individual situation, please consult with WBI or the professional advisor of your choosing. This information is compiled from sources believed to be reliable, accuracy cannot be guaranteed. Information pertaining to WBI's advisory operations, services, and fees is set forth in WBI's disclosure statement in Part 2A of Form ADV, a copy of which is available upon request.

Unless otherwise indicated, the source for all price and index data used in charts, tables and commentary is Bloomberg. You cannot invest directly in an index.

S&P 500 TR Index: includes a representative sample of large-cap U.S. companies in leading industries where all cash payouts (dividends) are reinvested automatically. MSCI World TR Gross Index: captures large and mid-cap representation of 23 developed markets with 1,653 constituents, covering approximately 85% of free-float capitalization of each country. MSCI makes no express or implied warranties or representations and shall have no liability whatsoever with respect to any MSCI data contained herein. The MSCI data may not be further redistributed or used as a basis for other indexes or any securities or financial products. This report is not approved, endorsed, reviewed, or produced by MSCI. None of the MSCI data is intended to constitute investment advice or a recommendation to make (or refrain from making) any kind of investment decision and may not be relied on as such.

WBI®