



January 2016

Hello and welcome to new and old clients.

2015 summary and 2016 preview

What's the deal with China?

Ugh! Another election year. Should we care?

Introductions, and comings and goings

Changes to Social Security & taxes

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Dear Clients and Friends,

Welcome to the 'new' Colorado Financial Management! We are excited to introduce our new 'brand' to the clients of Sargent Bickham Lagudis, and our newsletter to the clients of the 'old' Colorado Financial Management. But, lest there be any confusion, we are one company and all the resources of the firm are committed to you.

By now you will have received one or two letters or emails from us about why we merged and what to expect. I will say once more, the most important thing you need to know is that nothing changes for you in terms of your Financial Advisor, your Portfolio Manager, or your Client Service Manager. No changes. Nothing. Zip.

Summarizing the announcement one more time... the reason we merged was to build on each company's over 25 year legacy to create a lasting company for the future. Like the Six Million Dollar Man from the 1970's TV show... "We have the technology. We can make him better than he was. Better, stronger, faster."

So just in case you missed it, here are the summary facts of Colorado Financial Management:

- Assets under management ~ \$1.25 billion
- 9 professional financial planners
- 4 Chartered Financial Analyst® (CFA) charterholders
- 27 total employees, including 7 Partners
- 2 former investment bankers
- 1 former KPMG partner
- 3 locations: Boulder, Denver, Loveland

We will introduce our team later in this letter, but first let's begin as we always do with comments on the economy and the markets.

Market Commentary and Review

by Brad Bickham, CFA, CFP®

“The West is now confronted by not just another player but by a powerful new team of nations. And whether win, lose or draw, or whether everybody comes out a winner, will depend on how well we know our competition – and how well we play the game.” – John Naisbitt, Megatrends Asia, 1996

Following are returns for the last one, five, and ten years.

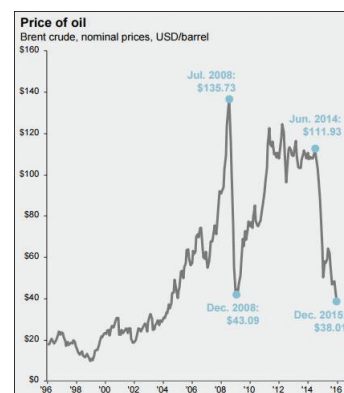
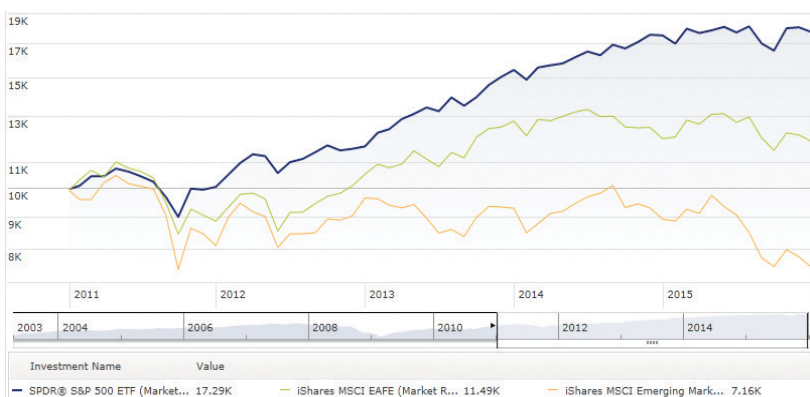
Returns as of December 31, 2015	4 th Qtr	2015	Last 5 Yrs. Annual	Last 10 Yrs. Annual
60/40 Balanced World Index	2.7%	-1.1%	5.0%	4.8%
World Stock Index (ACWI)	4.9%	-2.2%	6.1%	5.0%
Large Cap U.S. Stocks	7.0%	1.4%	12.6%	7.3%
Small Cap U.S. Stocks	3.6%	-4.4%	9.2%	6.8%
Foreign Stocks – ACWI ex U.S.	3.3%	-5.6%	1.1%	2.9%
Foreign Stocks – Emerging	0.7%	-14.9%	-4.8%	3.6%
U.S. Bonds – Taxable	-0.6%	0.6%	3.3%	4.5%
Hedge Fund Index	0.8%	-0.4%	2.1%	2.3%
Gold	-5.1%	-10.7%	-6.1%	7.0%

Overall, 2015 was a flat (to slightly negative) year for most diversified, balanced portfolios as exhibited by the 60/40 Balanced World Index. Bonds and most alternative strategies were flat, and equities on a global basis were down 2%. There really wasn't an asset class that showed positive returns of any significance.

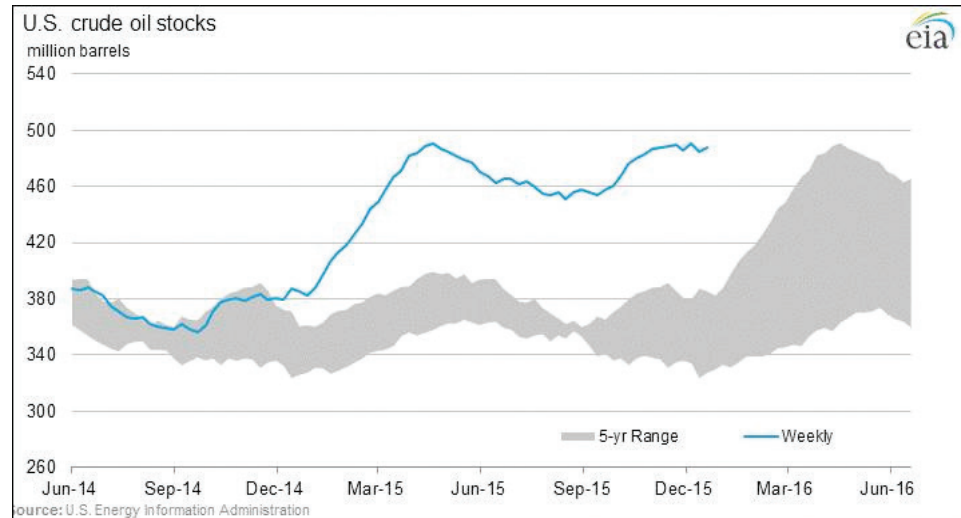
To make matters even more difficult, the S&P return of +1.4% was really driven by four companies. Someone has come up with the acronym for them, “FANG.” They are Facebook, Amazon, Netflix, and Google. If you didn't own these four companies, you likely had a negative year. If you avoided having energy stocks in your portfolio, you also increased your likelihood of having a positive return.

One of the most striking things about 2015 was that it was another year of the U.S. market outperforming the rest of the world. This has become significant. Over the last 5 years the cumulative return of the S&P 500 is 80.7% vs. only 5.5% for the world equity index ACWI-ex U.S. A 75% difference! If you believe at all in the reversion to the mean, you have to consider this in your investment strategy.

As mentioned earlier, energy was a big swing factor in 2015. The price of oil fell over 30% and continues to influence the daily gyrations in the overall market.

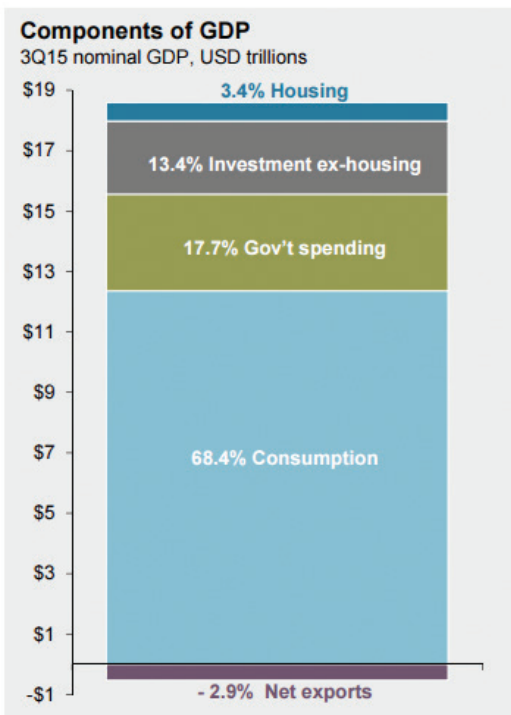
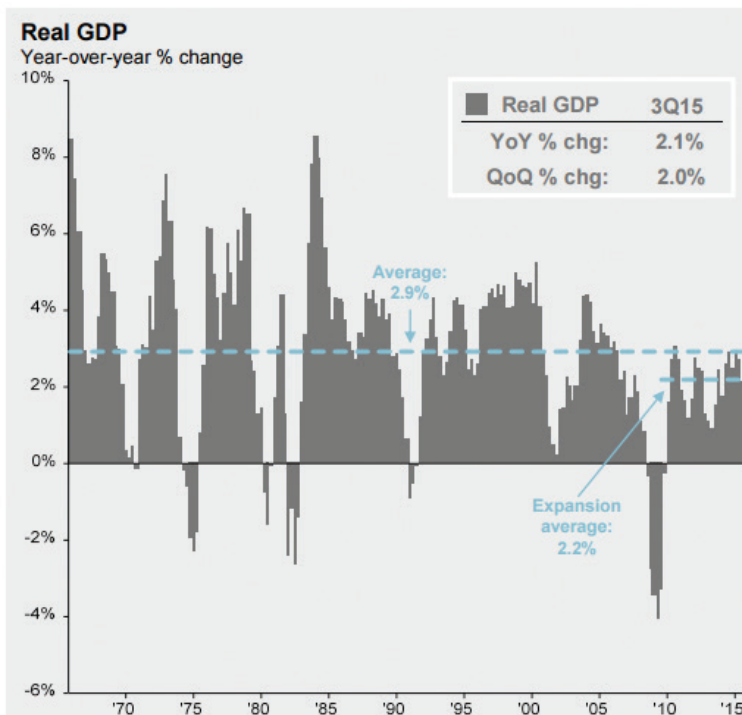


The reason for the drop is easy to understand – it’s simply supply and demand, and is really due to U.S. supply. In this chart, the wide band represents the normal level of supply, and the line shows the current levels.



What is more difficult to understand is why the markets are worried about this. Since when are low oil prices bad? We can only surmise it’s due to the rapidity of the change. It takes a while for people to adjust to a new reality, and it appears low oil prices are going to be with us for quite a while.

Our basic view of the economy is unchanged... continued slow growth. Unemployment trends are still favorable. Housing is growing, and auto sales actually hit a record last year. The slower parts of the economy are energy and exports. However, as shown on the chart below, exports represent only a small fraction of the U.S. economy.

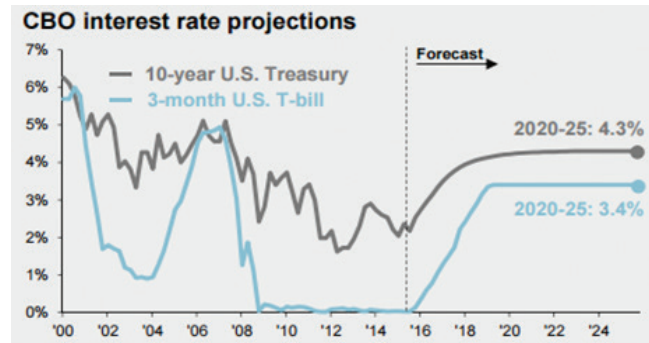


Source: BEA, FactSet, J.P. Morgan Asset Management.
Values may not sum to 100% due to rounding. Quarter-over-quarter percent changes are at an annualized rate. Average represents the annualized growth rate for the full period. Expansion average refers to the period starting in the second quarter of 2009.
Guide to the Markets – U.S. Data are as of December 31, 2015.

The economic slowdown in China is being used as an explanation for the volatility in the stock market, but that really does not make sense. As shown in this chart, the effect on the U.S. from a drop in Chinese demand growth is pretty small. Their effect on U.S. corporate profits is even smaller.



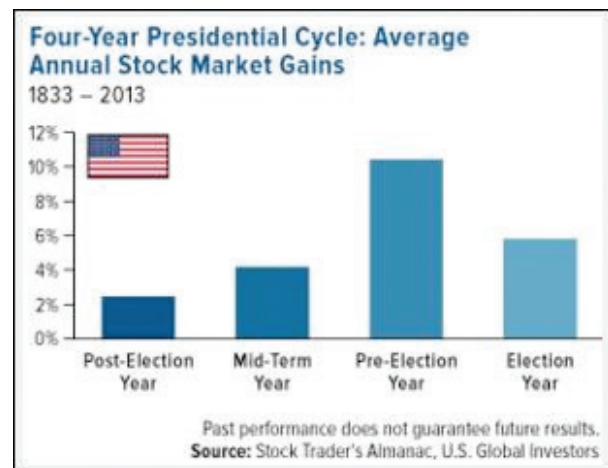
Another concern investors have is rising interest rates. The Fed finally began raising rates in December. Admittedly, rising rates are generally not a good thing for financial assets. However, the Fed has indicated, and we agree, the pace of increases will be very slow and should not interrupt economic growth for quite some time.



Corporate earnings fell last year as represented by the companies in the S&P 500. As we wrote in a prior letter, this is almost entirely due to the energy sector. Excluding energy companies, earnings are expected to be up about 6% for 2015. The preliminary estimates for 2016 show robust growth of 18%. Early estimates are almost always too optimistic, and we expect the reality to be somewhat lower. It is worth noting, however, that the 2016 estimate is only 11% higher than the 2014 earnings figure.

Year End	Operating EPS	% y-y
2007	\$82.54	-5.91%
2008	\$49.51	-40.02%
2009	\$56.86	14.85%
2010	\$83.77	47.33%
2011	\$96.44	15.12%
2012	\$96.82	0.39%
2013	\$107.30	10.82%
2014	\$113.01	5.32%
2015	\$106.39	-5.86%
2016e	\$125.56	18.02%

For valuation purposes, let us assume earnings for 2016 come in at \$115. Using the year end S&P 500 price of 2043, we arrive at a P/E ratio of 17.8. The average since 1988 is 18.7, so we are a little below average, but not screaming cheap.



Finally, 2016 is another election year. Ugh! Clients often ask what to expect during election years – how they affect returns. Following is a chart that shows the average annual gains during the presidential cycles since 1833. What this shows you is that the best year, on average, was last year and the second best year is this year. But, since last year was not good what does that mean for this year? Nothing. These are just averages and returns are really driven by the things we always look at: the economy, earnings, valuation, etc.

The theory around this goes like this... Politicians want to be re-elected, so they increase government spending in the years approaching an election to stimulate the economy. Then after the election, they take the bad medicine in the first couple of years. The difference now is our government is so polarized they do nothing. There is no stimulus, no tax reform, nor anything substantive. The good news is they passed a budget and increased the debt ceiling until 2017, so we should not have to deal with any threats of a government shut down this year.

Performance last year in our portfolios resembled the 60/40 Balanced World Index – depending on particular client allocations and specifics. Our best performance came from our individual stock portfolio, which outperformed the S&P 500 by 3% to 6%. The variance is usually due to different tax situations, but also client preferences, portfolio size, and cash flows. International mutual funds were once again the laggards. And, while the allocation was small, we held positions in MLP funds for most clients that got clobbered along with the energy sector.

As we enter 2016, the markets have begun with the worst first week ever – not an auspicious beginning. However, the December jobs report was just released and shows continued strength – signaling the economy remains on solid footing. We have been warning for some time that volatility was likely to increase; so while this year may be more nerve wracking we believe the fundamentals still favor equities over bonds and cash. We are diligently working to improve the performance of our ‘Alternatives’ strategy where we attempt to outperform bonds with only a fraction of the risk of equities. This sector has been more difficult the last few years evidenced by the closure of more ‘liquid alternative’ mutual funds in 2015 than in any year on record. Our long term record (15 years) has been quite good with an average annual return of about 6% with 40% of the risk of equities, so while it is harder, we believe we can still find a solution.

Financial Planning

By Barbara Lommen

The New Tax Rules for 2016

While you are focused on getting your 2015 taxes done, the IRS recently published the new 2016 tax rules. For planning purposes we thought it timely to share some of these changes here with you.

Income tax rates have not changed for 2016, but the tax brackets have moved up to compensate for inflation. The top tax rate of 39.6% now applies to single taxpayers earning more than \$415,050 (\$466,950 for married taxpayers filing jointly) – up from the 2015 thresholds of \$413,200 and \$464,850, respectively. The bracket for the long-term capital gains rates has also been adjusted upward. For full details on the brackets, please visit the IRS website.

The personal exemption has been increased by \$50 to \$4,050; the standard deduction will remain the same, with the exception of heads of household, up to \$9,300.

Some provisions, like the IRA charitable transfer provision, have been extended permanently. This allows our clients over 70 ½ to make a direct transfer from their IRA to an eligible charity and have it count as (part of) their Required Minimum distribution, without increasing taxable income.

The estate tax exemption has been increased to \$5.45 million, whereas the annual gift exclusion stays at \$14,000 for 2016.

Retirement plan contribution limits to 401(k) and 403(b) plans, as well as IRAs, stay the same as in 2015.

While we are on the topic of important changes, we should mention the elimination of two Social Security benefit filing strategies as of May 1, 2016: the restricted application and the file and suspend strategy. There is a detailed blog post on our website on this subject.

What matters most for now is that only those of you who will be age 66 or older by April 30, 2016 and who have not applied for benefits can still use these strategies, but you must act by April 30. If you are in that situation, we recommend you call us to discuss the best strategy for you.

As always, you can count on your financial planning team at CFM to incorporate these latest changes into your financial plans as they are being developed.

Company News

By Patty Meneley, COO

You may have heard some new voices here at our growing company.

In November we welcomed Shannon Knight to the firm. Shannon is a recent graduate of Virginia Tech and joins us as a Client Service Manager.

Along with Shannon, we welcomed Karina Colvin to our team in December. Some of us knew Karina at the CU Foundation and are delighted that she brings her talents to our company.

Both Karina and Shannon are working with Brad, Meagan, and Jordan and their clients and are very busy getting trained and up to speed with our processes. They're both great and we're happy they've joined the firm.

As several of you may know, Christiana left us in December to pursue her dream of going to culinary school. Christiana was a professional triathlete before we knew her and has a passion for good food that is also good for you. She hopes to be a private chef when she finishes school, but we hope she'll drop by sometimes and practice with us!

We also recently signed a lease for office space in Denver. Previously our Denver office was a shared suite, but sometime in early 2016 when the construction is complete, we'll have our own dedicated office space in the Cherry Creek neighborhood in Denver where we can meet with clients.

The Last Word

By Rick Lawrence, CEO

Welcome – this newsletter is the first communication we have sent out to all of the clients of the new Colorado Financial Management after our merger completed on January 1st.

I would like to share with you a few of my thoughts about why it made sense for our companies to come together.

Geography. With our new locations, we can serve our clients more effectively. Now we have a comfortable place that is convenient for clients whether they are in the metro area or northern Colorado. And in a few months our Denver office – where Barbara, Luke and Chris operate – will move to its permanent location in Cherry Creek.

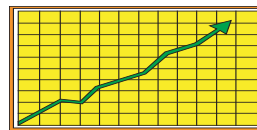
Multiple Portfolio Management Strategies. While our two companies approach client relationships with the same basic values, our investment strategies are different from one another. CFM has tended to use ETFs and mutual funds and follows a highly disciplined model for monthly realignment of portfolios based on tactical indicators and outlook. SBL uses a custom strategy with several different modeled exposures incorporating mutual funds and ETFs, as well as individual stocks and bonds. In the future, we will make all these choices available to clients and we will improve our ability to match an investment approach more directly with the needs and desires of the client.

Staying Power. Plain and simple, having seven partners ranging in age from 32 to 58 sets the stage for the company to thrive. Clients ought to think twice about having a relationship with a firm whose advisors are only their age or older. Who will your kids work with? Our age diversity sets the company on a path to stay in this business for a long time to come.

Talent. Our staff now includes nine financial planning professionals, four Chartered Financial Analysts, and six client service managers. We can create teams of people now, ensuring that there is always someone you know and who is familiar with your account available when you need them.

In short, we entered into this merger because it makes both companies better. Colorado Financial Management is here to stay, and eager to work with you and your families.

Many happy returns,



Colorado Financial Management

www.colofinancial.com

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