"You have to love a nation that celebrates its independence every July 4, not with a parade of guns, tanks, and soldiers who file by the White House in a show of strength and muscle, but with family picnics where kids throw Frisbees, the potato salad gets iffy, and the flies die from happiness. You may think you have overeaten, but it is patriotism." ~ Erma Bombeck

Global Diversification

Dear Valued Clients and Friends:

Some people believe diversification stops at our country's borders. They believe US companies provide enough diversification. However, the data below shows that portfolios invested only in the US are increasingly missing out on many global investment opportunities. Making a prediction about a single country may bear more risk than taking a more globally diversified approach.

"In God we trust; all others bring data." ~W. Edwards Deming

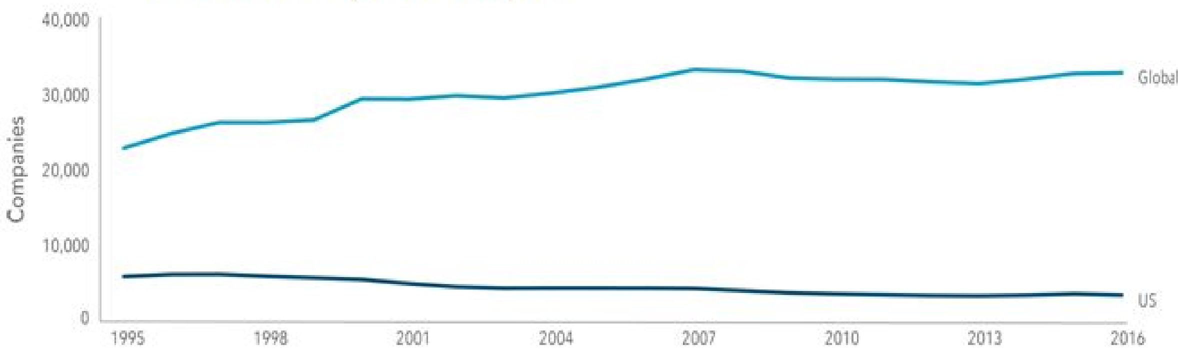
As of December 31, 2016, the Wilshire 5000 Total Market Index (a widely used benchmark for the US equity market), actually contains only around 3,600 names. In fact, the last time this index contained 5,000 or more companies was at the end of 2005 [1].

This mirrors the overall trend in the US stock market. In the past two decades there has been a decline in the number of US-listed, publicly traded companies. Should investors in public markets be worried about this change? Does this mean there is a material risk of being unable to achieve an adequate level of diversification for stock investors? We believe the answer to both is no. When viewed through a global lens, a different story begins to emerge-one with important implications for how to structure a well-diversified investment portfolio.

When looked at globally, the number of publicly listed companies has not declined. In fact, the number of firms listed on US, non-US developed, and emerging markets exchanges has increased from about 23,000 in 1995 to 33,000 at the end of 2016. (See **Exhibit 1**.)

It should be noted, however, that this number is substantially larger than what many investors consider to be an investable universe of stocks. For example, one well-known global benchmark, the MSCI All Country World Index Investable Market Index (MSCI ACWI IMI) contains between 8,000 and 9,000 stocks. This index applies restrictions for inclusion such as minimum market capitalization, volume, and price.

Exhibit 1. **Number of Publicly Listed Companies**



Source: Bloomberg.

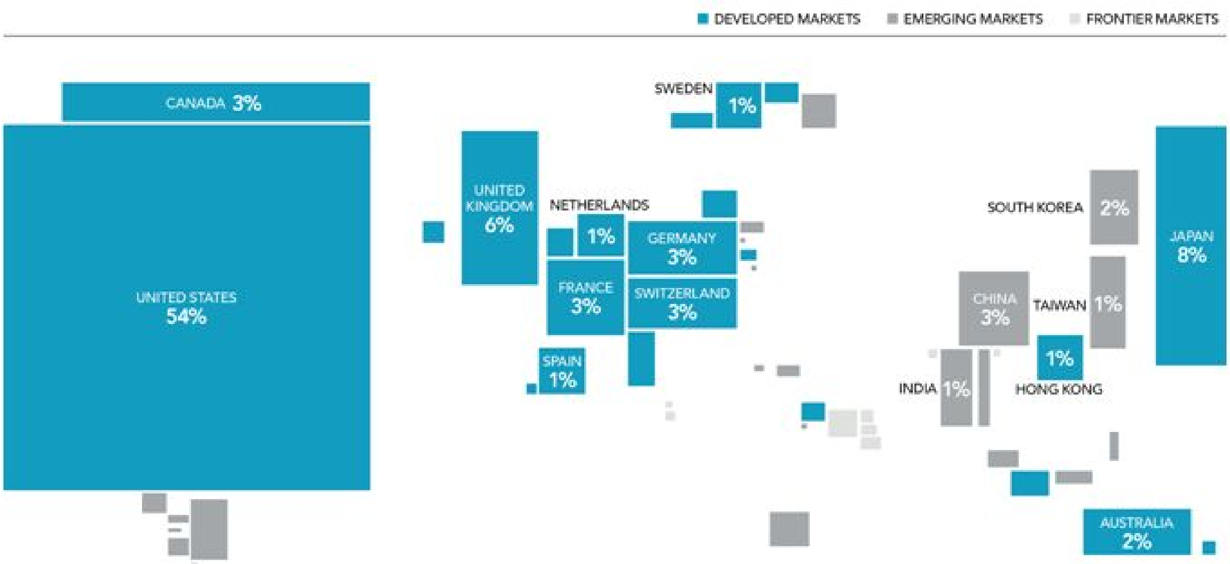
While it is true that in the US there are fewer publicly listed firms today than there were in the mid-1990s (a decrease of about 2,500), it is clear that the increase in listings both in developed markets outside the US and in emerging markets has more than offset the decline in US listings. Although there is no consensus about why US listings have decreased over this period of time, a number of academic studies have explored possible reasons for this change. One line of investigation considered if changes in the regulatory environment for listed companies in the US relative to other countries may explain why there are fewer listed firms. Another considered if, since the 2000s, private companies have had a greater propensity to sell themselves to larger companies rather than list themselves. In either case, the implication for investors based on the numbers alone is clear-the number of publicly listed companies around the world has increased, not decreased.

A Global Approach

In the US, with thousands of stocks available for investment today, it is unlikely that this change will meaningfully impact an investor's ability to efficiently pursue equity market returns in broadly diversified portfolios. As noted in Exhibit 2, the weight of the US in the global market is approximately 50-55%. For comparison, it was approximately 40% in 1995.

For investors looking to build diversified portfolios, the implications of the trend in listings are also clear. The global equity market is large and represents a world of investment opportunities, nearly half of which are outside of the US. While diversifying globally implies an investor's portfolio is unlikely to be the best performing relative to any one domestic stock market, it also means it is unlikely to be the worst performing. Diversification provides the means to achieve a more consistent outcome and can help reduce the risks associated with overconcentration in any one country. By having a truly global investment approach, investors have the opportunity to capture returns wherever they occur.

Exhibit 2. **Percent of World Market Capitalizations as of December 31, 2016**



Data provided by Bloomberg. Market cap data is free- oat adjusted and meets minimum liquidity and listing requirements. Many nations not displayed. Totals may not equal 100% due to rounding. China market capitalization excludes A-shares, which are generally only available to mainland China investors.

Summary

While there has been a decline in the number of US-listed, publicly traded companies, this decline has been more than offset by an increase in listings in non-US markets. While the reasons behind this trend are not clear, the implications for investors today are clearer-to build a well-diversified portfolio, an investor has to look beyond any single country's stock market and take a global approach.

We hope everyone is enjoying the first official week of summer. Please do not hesitate to reach out to us if there is anything we can do for you or your family. Have a happy 4th of July.

We appreciate your business and look forward to talking with you soon.

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[1] Source: Wilshire Associates.

Past performance is no guarantee of future results. There is no guarantee an investing strategy will be successful. Diversification does not eliminate the risk of market loss. Investing risks include loss of principal and fluctuating value. International investing involves special risks such as currency fluctuation and political instability. Investing in emerging markets may accentuate these risks.

Indices, such as the MSCI All Country World Index Investable Market Index (MSCI ACWI IMI) are not available for direct investment.