



PRATO CAPITAL

THE DIVERSIFIED PORTFOLIO

OCTOBER 2018

A Diversified Portfolio

At Prato Capital Management, we believe a broad diversified portfolio is the best way to achieve long term financial success and meet the goals of your Financial Life Plan. This type of portfolio will include a balance of stocks and bonds based on your risk tolerance, financial situation and goals. A diversified portfolio will lower the risk and volatility of an all stock portfolio while still capturing some of the returns that stocks can provide over the long term. Academic research has shown that market timing is not effective over the long term and a diversified balanced portfolio does not try to 'market time'.

The graphic below of market returns from the 2nd quarter of 2018 show that not only do stocks and bonds often move in different directions, different sectors within those asset classes can also move in opposite directions. Diversification of a portfolio will often minimize some of the risk of one sector and asset class while capturing the positive returns of another.

A recent example of stocks declining sharply is the 4th quarter of 2008. The highlighted blocks below show those declines but also illustrate that global bonds had the best quarterly return since 2001. The graphic also shows that less than a year later, all of the stock sectors had significant gains and the best quarterly returns since 2001. A diversified portfolio will be best positioned to reduce risk and still capture gains during these types of very volatile markets.

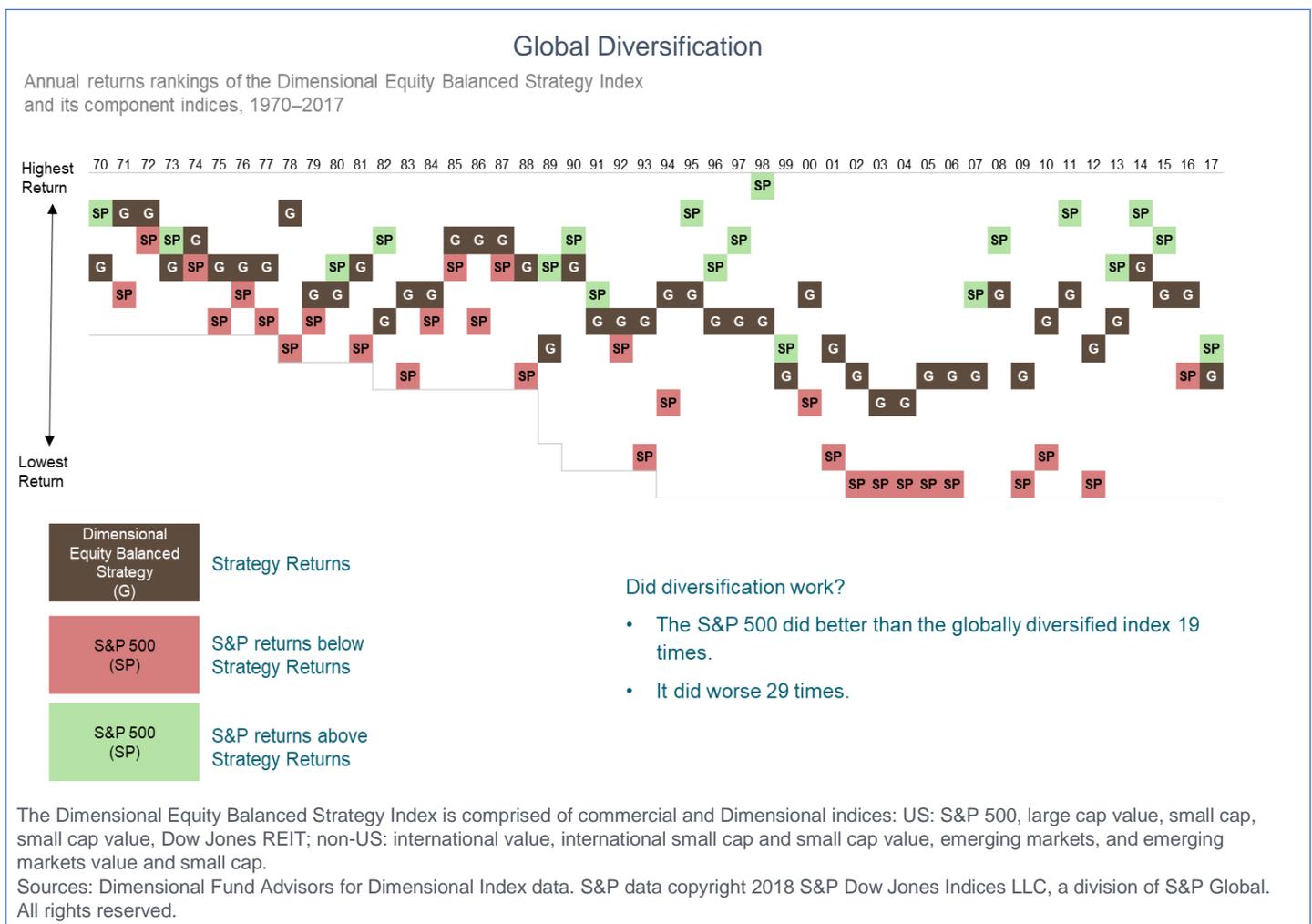
| Market Summary 2nd Quarter 2018 | | | | | | |
|---------------------------------|-----------------|--------------------------------|-------------------------|--------------------|----------------|--------------------------|
| | US Stock Market | International Developed Stocks | Emerging Markets Stocks | Global Real Estate | US Bond Market | Global Bond Market ex US |
| Q2 2018 | 3.89% | -0.75% | -7.96% | 6.05% | -0.16% | 0.48% |
| | | | | | | |
| Since Jan. 2001 | | | | | | |
| Avg. Quarterly Return | 2.0% | 1.5% | 3.0% | 2.6% | 1.1% | 1.1% |
| Best Quarter | 16.8% | 25.9% | 34.7% | 32.3% | 4.6% | 4.6% |
| | Q2 2009 | Q2 2009 | Q2 2009 | Q3 2009 | Q3 2001 | Q4 2008 |
| Worst Quarter | -22.8% | -21.2% | -27.6% | -36.1% | -3.0% | -2.7% |
| | Q4 2008 | Q4 2008 | Q4 2008 | Q4 2008 | Q4 2016 | Q2 2015 |

Diversity Within Your Portfolio

Not only is it important to diversify your portfolio with stocks and bonds, it is important to diversify within your portfolio. With stocks, we diversify portfolios across different sectors, market capitalization (small, mid and large cap) and different countries. As shown above, during the 2nd quarter of 2018, not all areas within a stock portfolio will climb or decline at the same time or at the same rate. Bonds are diversified for the same reason by selecting different government, corporate, and international securities.

Over the past year, the S&P 500 and NASDAQ have reached new highs on what seems like a daily basis. It is certainly worth wondering if a diversified portfolio is needed any longer. Why not stay just with the US stock market?

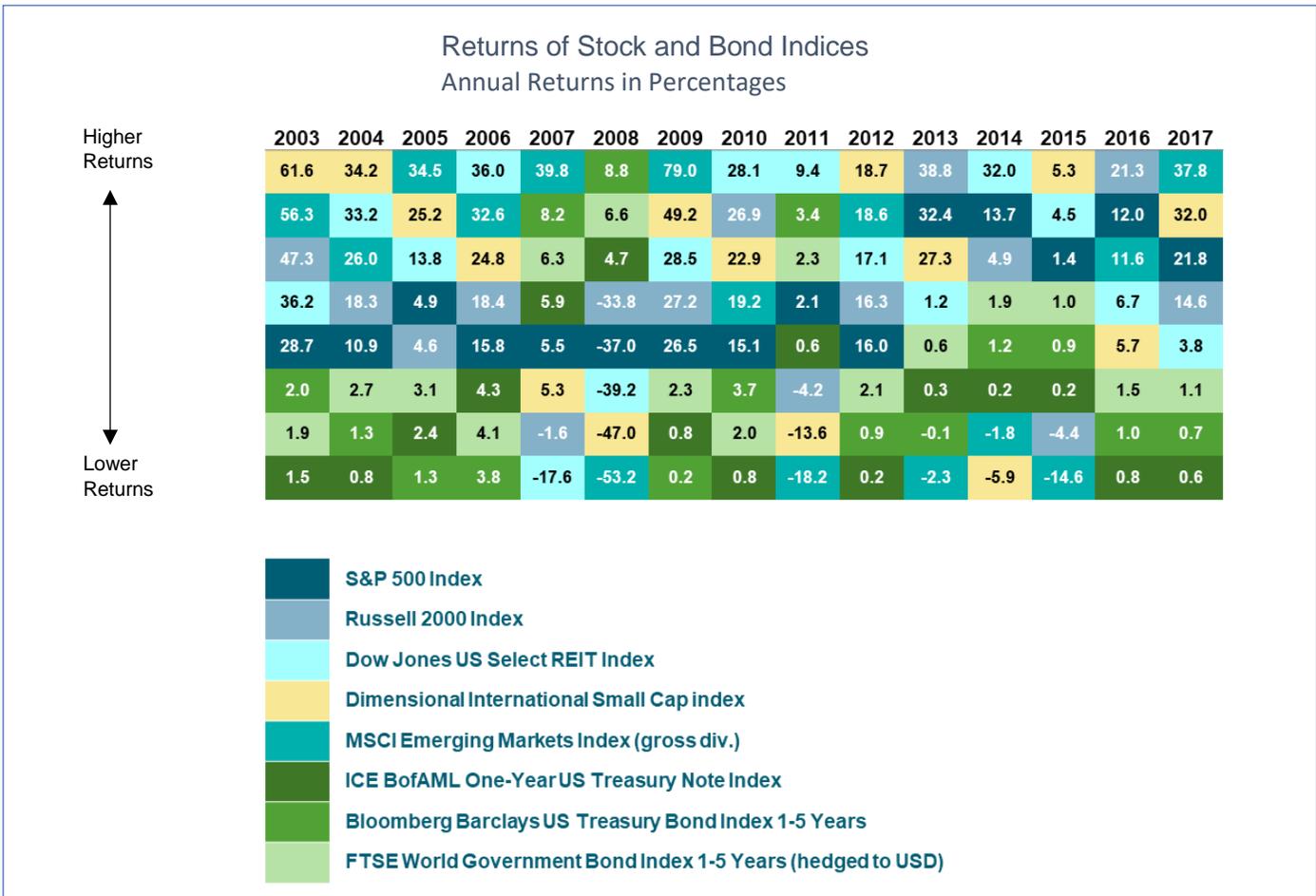
In the graphic below, the returns of the S&P 500 are compared to a diversified portfolio with US and international stocks. Over the last 48 years, a globally diversified portfolio outperformed the S&P 500 twenty nine times. This is a simple and powerful reminder of the need for diversification to capture returns wherever they may happen around the globe.



The Randomness of Returns

The chart below looks like a quilt pattern. Each color represents the returns of a different investment from 2003 to 2017. It also looks like the returns of one investment in relation to another seems random. One of the greatest advantages of a diversified portfolio is not picking where the best returns will be in the future, but already being invested in those areas.

The United States is about half of the total market capitalization of all global stock markets and, as the chart below also shows, the US markets do not always have the highest returns. It makes sense to invest in other areas, including emerging markets, to see better returns over the long term and to mitigate the risk of being concentrated in one market.



Why A Diversified Portfolio

Rather than chasing the past 'winners' in the markets, at Prato Capital Management we believe a broad diversified portfolio will be better positioned to capture returns whenever and wherever they occur. And being invested for the long term in this type of portfolio will help you reach the goals of your Financial Life Plan.

Past performance is no guarantee of future results.