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A Short Note on The Merits of Diversification

As year-end approaches, investors are once again faced with the challenges presented by market volatility. At Shepherd Financial Partners, many of our clients have long-term goals that are measured in years rather than months. Accordingly, we focus our investment strategies on an asset allocation philosophy that balances risk and reward via diversification. Our pragmatic approach looks across a number of asset classes in both the equity and fixed income markets. Our belief being that risks are inherent in all investments but by combining investments that are either minimally or negatively correlated, it is possible to produce a portfolio that generates attractive returns with balanced risks over the long term.

A Perfect Market for "S&P" Envy

Years	S&P 500 Index	Diversified portfolio
2000-2002	-37.6%	-13.3%
2003-2007	+82.9%	+57.8%
2008	-37.0%	-20.1%
2009-2017	+258.8%	+152.1%
Total Return	+157.9%	+175.5%
Growth of $100,000	*$257,880*	*$275,535*

Source: Morningstar as of 12/31/17. Past performance does not guarantee or indicate future results. Diversification does not guarantee a profit or protect against a loss in a declining market. Diversified Portfolio is represented by 60% S&P 500 Index and 40% in the Bloomberg Barclays U.S. Aggregate Bond Index. Index performance is for illustrative purposes only. You can not invest directly in the index.

As the table from BlackRock illustrates, since 2000 a hypothetical diversified portfolio of equities and bonds has performed well over market cycles relative to a concentrated portfolio of equities alone. While the equites excel in the bull portion of market cycles, the bond holdings of the portfolio helps to dampen volatility in periods when markets face turbulence.

The financial media is obsessed with the U.S. equity markets and many times will use the S&P 500 as a proxy for all investments. From time to time, one asset class might greatly exceed the returns of other investments. While that asset class might grab headlines, the attention may also serve as a distraction for the investing public. The over-priced securities might introduce new risk to portfolios as the winning asset class prices start to look rich. The table above represents just one example of why diversification makes sense. By running diversified portfolios based on a client's specific risk objective, we can rebalance the asset allocation to represent an appropriate balance of risk and reward.

We hope to take advantage of opportunities that present themselves throughout market cycles while working within this risk objective framework. While there is no guarantee that a diversified portfolio will enhance overall returns or outperform a non-diversified portfolio, our disciplined process keeps the investment focus on pursuing our clients' goals. Please reach out with your questions or thoughts – we are here for you and welcome all discussions.

1004 Main Street, Winchester, MA 01890
Tel 781.756.1804 Fax 781.729.4356
www.shepherdfinancialpartners.com

Rebalancing a portfolio may cause investors to incur tax liabilities and/or transaction costs and soes not assure a profit or protect against a loss.

Correlation is a statistical measure of how closely two securities move in relation to each other. A high(positive) correlation implies the securities generally move in a similar direction, whereas a low(negative) correlation implies the securities generally move I the opposite directions.

Hypothetical examples are for illustrative purposes only, and do not represent a specific investment or account.

Bloomberg Barclays U.S. aggregate bond: The Bloomberg Barclays U.S. Aggregate Bond Index is an index of the U.S. investment-grade fixed-rate bond market, including both government and corporate bonds.

S&P 500: The Standard & Poor's 500 Index is a capitalization weighted index of 500 stocks designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries.

The opinions presented in this material are for general information only and are not intended to provide specific advice or recommendations. The economic forecasts set forth in this presentation may not develop as predicted. All performance referenced is historical and is no guarantee of future results. All indices are unmanaged and may not be invested into directly.

Diversification does not protect against market risk. No strategy, including asset allocation, assures success or protects against loss. Investing involves risk, including potential loss of principal.
Fixed income investing entails credit risks and interest rate risks. When interest rates rise, bond prices generally fall.

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