The Future Direction of

PERSONAL INVESTING:

SELECTING INVESTMENTS:

WHAT & WHEN

I.S.S.U.E.® INC., IA

Investment **S**trategies **S**imply **U**nderstood & **E**xecuted®

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Investors……Consider These Issues!

This most recent report looked at all the mutual funds that finished in the top quartile (top 25%) for returns in one year and tracked how they performed over subsequent years. It found that just 1.94% of those funds were able to maintain that top-quartile performance over three years, and a measly 0.34% we able to keep it up over five years.

Those percentages are less than what you'd expect from pure chance, and the results are the same even if you look at longer periods of performance to try and account for random year-to-year variation.

When these same mutual funds are evaluated over two consecutive five-year periods of performance, only 39.86% of the mutual funds that outperformed over the first five years continued to outperform over the second five years.

Again, random chance would expect 50% of them to continue their outperformance, so these professional investors are less consistent than a coin flip. In fact, the report concludes that "the data show a stronger likelihood for the best-performing funds to become the worst-performing funds than vice versa."

All of which is simply to say that there is no consistency to the performance of these professional investors. The vast majority of those who are outperforming are doing so out of pure luck and are more likely to significantly underperform the market going forward than they are to continue beating it.

"https://www.thesimpledollar.com/even-the-experts-cant-beat-the-market-why-would-you/"

Yes, you may be able to beat the market, but with investment fees, taxes and human emotion working against you, you're more likely to do so through luck. If you can merely earn the same returns as the market, you'll be doing better than most people.

"https://www.investopedia.com/ask/answers/12/beating-the-market.asp"

The studies collectively demonstrate the importance of (1) being in the market, and (2) doing a strategic asset allocation.

"https://blogs.cfainstitute.org/investor/2012/02/16/setting-the-record-straight-on-asset-allocation/"

However, we believe that investors should consider adapting their asset allocation strategies to account for higher correlations and new investment choices.

"http://content.schwab.com/web/retail/public/asset_allocation/assets/MKT81752HL-02.pdf"

You're making enough money and you're saving enough, but you're putting it all in conservative investments. That's fine, right? Wrong! If you want to build a sizable portfolio, you have to take on risk, which means you'll have to invest in equities. So how do you determine what's the right level of exposure for you?

"https://www.investopedia.com/managing-wealth/simple-steps-building-wealth/"

It is important that investors follow a disciplined approach to asset allocation that seeks to manage risk and produce superior returns over the long run.

Holding fixed income securities or cash might make you feel good in the moment, but will most certainly rob you of your ability to build wealth over the long term.

"https://seekingalpha.com/article/4137986-build-long-term-wealth"

The following chart is the Callan Periodic Table of Investment Returns taken from their website at "callan.com".

Small Cap, Emerging Markets, and Large Cap dominate the yearly highest returns from 1998 through 2017. I am sure any investor would be satisfied with those yearly returns from 2009 through 2017, assuming they had been invested in those equity categories.

What should individual investors take away from everything mentioned above?

Trying to beat the stock market is frivolous.

Strive for stock market returns.

Stay invested at all times (during a business cycle expansion).

Utilize strategic asset allocation.

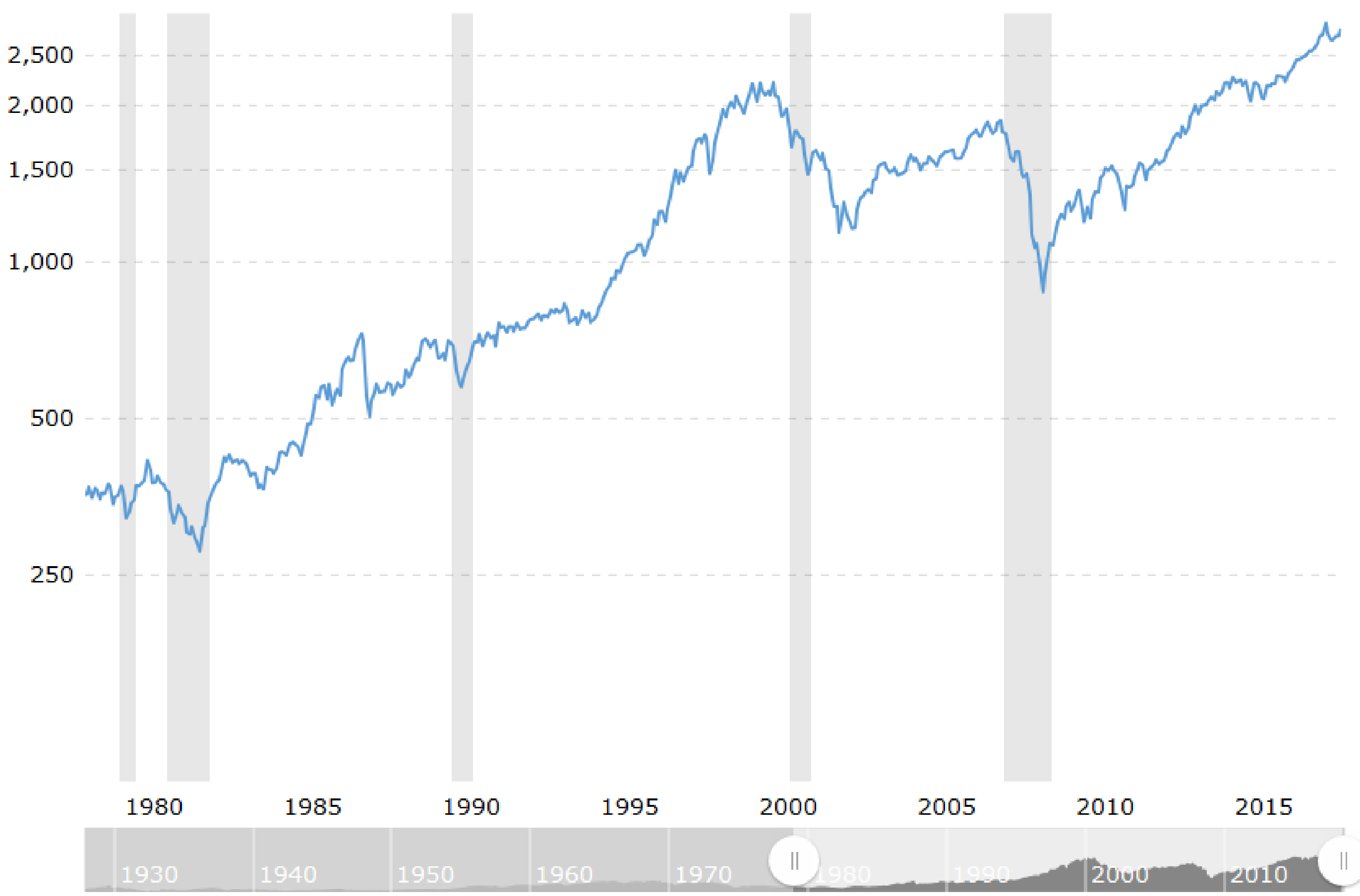
Do not assume your financial professional, or the fund manager of your investments, will be able to improve upon general stock market returns, regardless of their credentials, experience, and past results.

Make Hay While the Sun Shines!

This proverb, which was first recorded in the 1500s, means simply to make the most of one's opportunities while you have the chance.

Business cycle expansions, since the early 1980s, have provided investors the greatest opportunities to increase their wealth through equity investments, with minimal downside risk over an 8 to 10 year periods, than has occurred in the last 90 years. Even with the inevitable stock market corrections which occur throughout a business cycle expansion, the equity returns during the expansions are often dramatic due to the upward bias of stocks.

Following are the historical charts for the S&P 500 and Nasdaq since 1980.



"https://www.macrotrends.net/2324/sp-500-historical-chart-data"

"https://www.macrotrends.net/1320/nasdaq-historical-chart"

Although the charts appear similar, the losses incurred from 2000 through 2002 were much greater for the Nasdaq (-77%) than for the S&P 500 (-49%).

Let's look at the stock market values coming from the lows (around the beginning of an expansion) to the highs (around the end of an expansion) associated with the previous three business cycle expansions plus the current expansion to the end of July, 2018. Dramatic returns have been experienced.

	S&P 500	NASDAQ
1982 - 1990	157%	121%
1991 - 2001	285%	1021%
2002 - 2007	65%	111%
2009 - 2018	221%	378%

Who wouldn't want even a portion of those returns for their portfolio!

Surprisingly, those returns included many periodic stock market corrections. Both the duration and depth of each correction varied, especially between the S&P 500 and Nasdaq. They were and will continue to be both unpredictable and unavoidable. Even with the periodic stock market corrections, overall returns for any equity category, during a business cycle expansion, can add significant wealth to any portfolio.

Following are the actual stock market corrections (from peak to trough which were greater than or equal to -10%) which occurred during the corresponding business cycle expansions:

	S&P 500	NASDAQ
1982 - 1990	-14%	-31%
	-31%	-15%
		-33%
		-14%
1991 - 2001	-16%	-13%
	-25%	-13%
		-13%
		-12%
		-21%
2002 - 2007	NA	-11%
		-13%
		-14%
		-12%
2009 - 6/2018	-13%	-14%
	-18%	-17%
	-10%	-11%

The historical results demonstrate that, regardless of the actual figures or timeframes, staying invested in equities throughout a business cycle expansion, even with periodic corrections, will add significant wealth to a portfolio. However, investment returns for different equity categories will vary. Selecting categories with expected higher returns over general stock market increases will enhance overall portfolio returns.

Diversification Will Decrease Your Wealth!

Diversification (creating a portfolio with a mix of asset classes like equities and bonds) is the gold standard for risk management embraced by the financial industry.

But gold for who?

As discussed in my article entitled, “The Future Direction of Personal Investing: Heresy or Destiny”, even having diversified assets while staying in the stock market during business cycle contractions will to extremely detrimental losses for the individual investor. Equity losses in the last two contractions were 30 - 50% or greater. Diversification only benefits the financial industry because they still make money even when investors are losing money, lots if it!

Assume a diversified portfolio contains 60% equities and 40% bonds. This would be a typical diversified portfolio. If future equity and bond returns average 8% and 4% a year, respectively, $10,000 today would be worth $36,700 in 20 years. If the portfolio were 80% equities and 20% bonds, the value in 20 years would be $41,700 (+13.6%). Obviously, a greater exposure to equities provides greater returns, on average. Also, any investor with long timeframes (>5 years) and maintaining 100% in equities would have $46,600 in 20 years (+26.8%).

Look at the 2009 - 2017 investment return leaders from the previous chart. Bonds were slightly better than equities in only one year, 2011. In all other years, equity returns far exceeded bond returns, even with periodic stock market corrections. 2009 - 2017 is part of the current business cycle expansion. Long-term investors (>5 years) should be 100% in equities during *business cycle expansions*!

Based on the historical returns from 2009 - 2017, what would have $10,00 in a Russell 2000 investment (blend or index) starting in 2009 been worth at the end of 2017?

YEAR	% RETURN	VALUE
2009	27.17	$12,717
2010	26.85	$16,132
2011	-4.18	$15,457
2012	16.35	$17,984
2013	38.82	$24,966
2014	4.89	$26,187
2015	-4.41	$25,032
2016	21.31	$30,366
2017	14.65	$34,815

A gain of $24,815 in nine years equates to an average annual return of 14.87%. That would have been accomplished with a simple buy and hold strategy.

A similar evaluation looking at the Bloomberg Barclays Aggregate Bond index would have ended with a gain of only $4,073 after nine years at an annual average return of 3.87%. Clearly, being invested 100% in equities throughout a business cycle expansion will add considerably more wealth.

Since the periodic stock market corrections did not appear to have a significant impact on the overall equity returns in the past three and current business cycle expansions, why would there have been a need for diversification away from equities (assuming there were no income requirements)? Remember, business cycle contractions are a completely different subject.

Diversification from unsystematic risk, risk related to specific stocks or industries, can be easily accomplished by investing in mutual funds or ETFs that contain a broad universe of individual stocks, even if they all fall within a single equity category like small caps.

The entire financial industry, and all it's associates, are only supported by investor's monies. If those monies are not invested, no one gets paid. Investors need to become smarter about the what and when of investing in order to maximize their investment returns while minimizing the costs paid to achieve them. In other words, due diligence coupled with an effective value analysis approach (cost versus return).

What additional value have you or your financial professional added to your portfolio beyond general stock market returns? Should you consider a change?

The ABCs of Equities

Equities are instruments of ownership in companies. They are individual stocks or groupings of stocks in the form of mutual funds or ETFs (Exchange - Traded Fund).

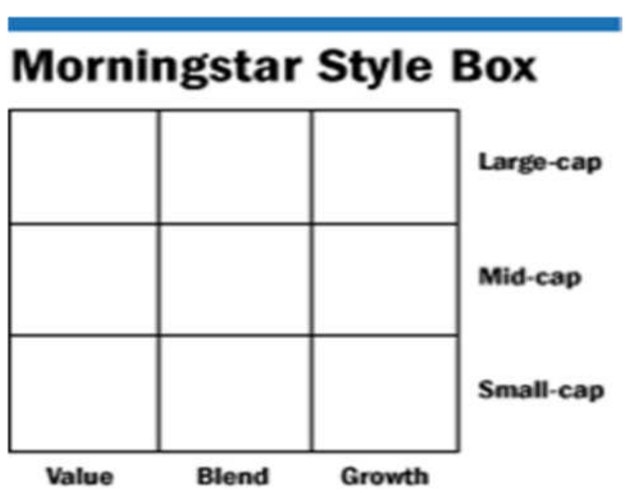
No two equities are exactly alike. Domestic and global economic and political activity, as well as general stock market randomness, will have different effects on all equities.

Some equities share certain characteristics such as same the industry, country, or relative size. Most equities are grouped into categories like large-cap, small-cap, emerging markets, international, etc. Also, sub-categories like growth, value, and blend (sometimes referred to as index) further define groupings.

Equities are the primary vehicle by which most investors accumulate wealth for retirement. Other asset classes such as cash, bonds, real estate, commodities, etc. provide other avenues for wealth but are unlikely to provide the necessary growth needed for future requirements. For every investor, the equity categories chosen, acquisition and maintenance costs, and holding periods selected are extremely critical for financial success in long-term investing.

Unfortunately, the creation, promotion, purchase and sale, cost, advice, management, and education of equities are mostly controlled by the financial industry. All of these factors therefore favor the financial industry and not the individual investor.

Due to the lack of uniformity in the financial industry, trying to describe and list all the different types of equities by generalized names or definitions is difficult. There can be overlapping and the use of terms like sectors, objectives, styles, etc. may not be consistent. Morningstar created their style box (morningstar.com) to help the description process.



Even though the above terms are used extensively in the financial industry, investors should have a better grasp of how all the equity investments, especially mutual funds and ETFs, are often classified or described (Following are some but not nearly all the possible examples).

Global View

Country or Region: US, China, Europe, Emerging Markets, EAFE

Perspective View

Domestic or Foreign

Industry View

Consumer, Industrials, Financials, Health Care

Size View

Mega Cap, Large Cap, Mid Cap, Small Cap, Micro Cap

Operations View

Growth, Value, Blend, Income (Dividend)

Weighted View

Market Cap, Price Cap, Equal, Dogs of the Dow

Managed View

Active, Passive

Speculation View

Leveraged, Inverse

Specialty View

Target Date, ESG (Environmental, Social, Governance)

There are equity investments which mix and match various views to create a “specialized” investment. In fact, that approach is often the only way for active managers to attract new investment monies. Passive or index equity investments usually take a single view approach to create the investment. However, when comparing two similar investments, different stock selections and the different percentages of the same stocks held will result in different returns.

The following excerpts are taken from a 2016 year end SPIVA® U.S. Scorecard summary located at “https://us.spindices.com/documents/spiva/spiva-us-year-end-2016.pdf” which analyzed the historical results during a 15 year timeframe from 2002 through 2016.

During the five-year period ending Dec.31, 2016, 88.3% of large-cap managers, 89.95% of mid-cap managers, and 96.57% of small-cap managers underperformed their respective benchmarks.

Over the 15-year period ending Dec.2016, 92.15% of large-cap, 95.4% of mid-cap, and 93.21% of small-cap managers trailed their respective benchmarks.

Funds disappear at a significant rate. Over the 15-year period, more than 58% of domestic equity funds were either merged or liquidated. Similarly, almost 52% of global/ international equity funds and 49% of fixed income funds were merged or liquidated. This finding highlights the importance of addressing survivorship bias in mutual fund analysis.

Although the report did not specifically address active versus passive in survivorship, it can be assumed that a majority of the non-survivors were actively managed and therefore liquidated or merged due to poor performance. Certainly, there are some actively managed equity investments which can be superior selections over passive or index investments for investors. However, consistency is a difficult headwind to overcome.

Following is a table created from the results reported in the Callan Periodic Table of Investment Returns for the last 20 years (1998 - 2017).

Asset Category Trends -
Historical Investment Returns

Data Years: 1983 - 2017 (Emrg Mkts: 1991→ & High Yield: 1994→)

	YEARLY AVERAGES										
	LAST 20	LAST 15	LAST 10	LAST 9	LAST 8	LAST 7	LAST 6	LAST 5	LAST 4	LAST 3	LAST 2
MSCI EAFE	7.49%	10.29%	4.44%	9.76%	7.00%	6.90%	10.07%	8.62%	5.08%	8.41%	13.02%
MSCI EMERGING MARKETS	13.35%	17.66%	7.57%	14.32%	6.23%	4.38%	8.14%	6.04%	8.12%	11.43%	24.44%
RUSSELL 2000 - VALUE	10.19%	12.42%	9.96%	14.28%	13.49%	11.91%	14.82%	14.17%	9.08%	10.70%	19.79%
RUSSELL 2000 - GROWTH	9.38%	13.67%	11.77%	17.36%	15.22%	13.24%	15.93%	16.20%	9.43%	10.70%	16.75%
RUSSELL 2000 - INDEX	9.61%	12.97%	10.77%	15.72%	14.29%	12.49%	15.27%	15.05%	9.11%	10.52%	17.98%
S & P 500 - VALUE	8.26%	10.96%	8.82%	14.16%	13.29%	13.03%	15.28%	14.80%	10.50%	9.88%	16.38%
S & P 500 - GROWTH	9.32%	11.63%	11.85%	17.04%	15.23%	15.25%	17.02%	17.50%	13.69%	13.28%	17.17%
S & P 500 - INDEX	8.86%	11.38%	10.49%	15.77%	14.30%	14.19%	16.21%	16.25%	12.22%	11.72%	16.90%
BB AGGREGATE BOND	5.04%	4.17%	4.05%	3.91%	3.66%	3.25%	2.48%	2.14%	3.18%	2.25%	3.10%
BB HIGH YIELD	7.84%	10.30%	9.80%	13.80%	8.25%	7.26%	7.64%	6.01%	5.65%	6.72%	12.32%
NUMERICAL AVERAGE	8.93%	11.54%	8.95%	13.61%	11.09%	10.19%	12.29%	11.68%	8.60%	9.56%	15.78%

1st 2nd 3rd

CONTACT: investools101@gmail.com VISIT: http://investescent.com/

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Data accuracy is not guaranteed.

Revision 3

Proprietary Document Created by
Mark T. Wurtz: January, 2007

There are several items which should to be emphasized regarding the yearly average trends and individual year performances for the last 20 years shown above:

The value categories for both S&P 500 and Russell 2000 have never been 1st.

The value categories for both S&P 500 and Russell 2000 have seldom been 2nd or 3rd.

S&P 500 value beat S&P 500 growth in the years 2010, 2012, and 2016.

Russell 2000 value beat Russell 2000 growth in 2012 and 2016.

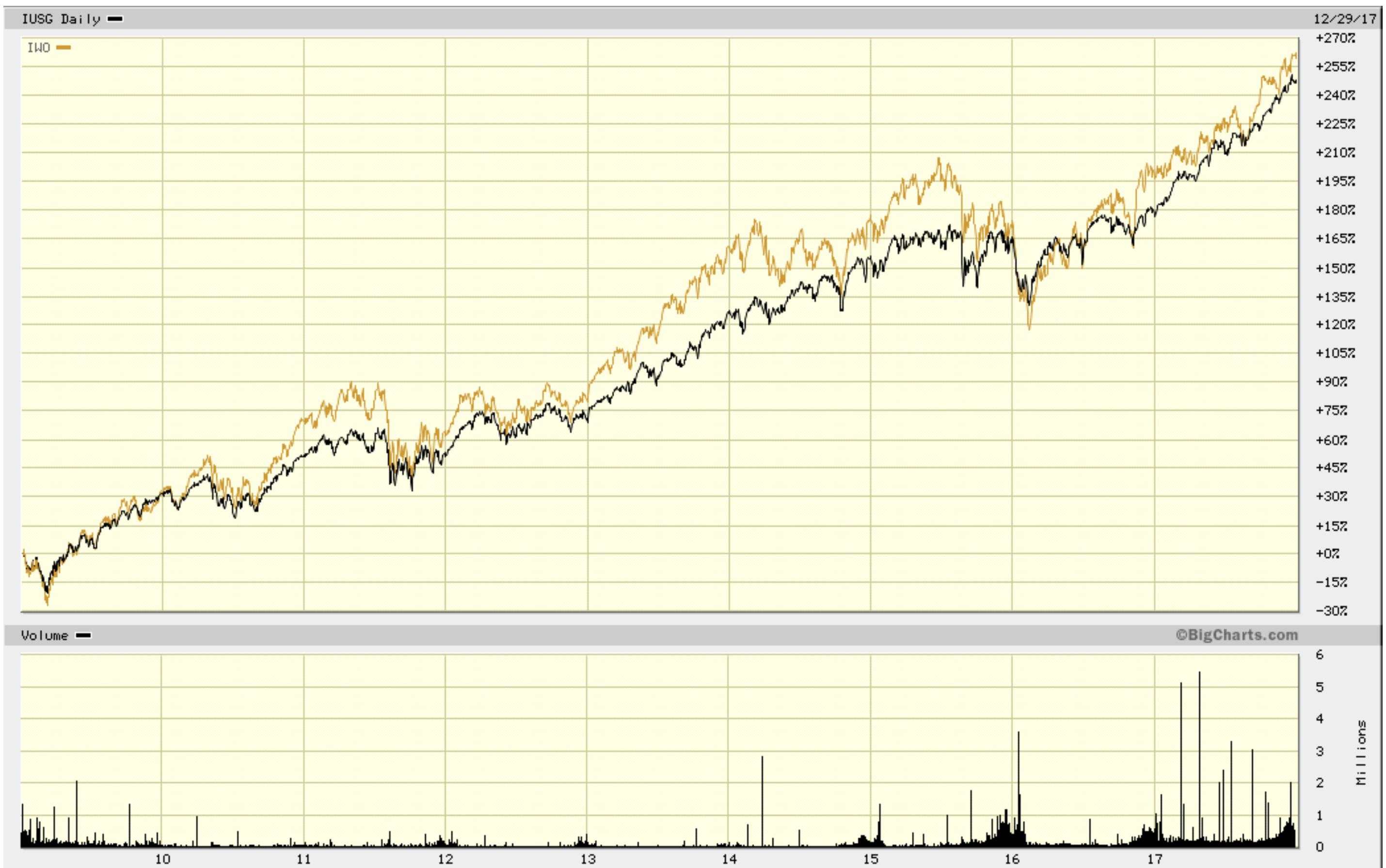
The S&P 500 has been dominate in the last 3 to 10 yearly average periods.

The S&P 500 has been 1st only in the years of 2014 and 2015 during last 10 years.

The S&P 500 has been 1st only in the years of 1998, 2014, and 2015 during last 20 years.

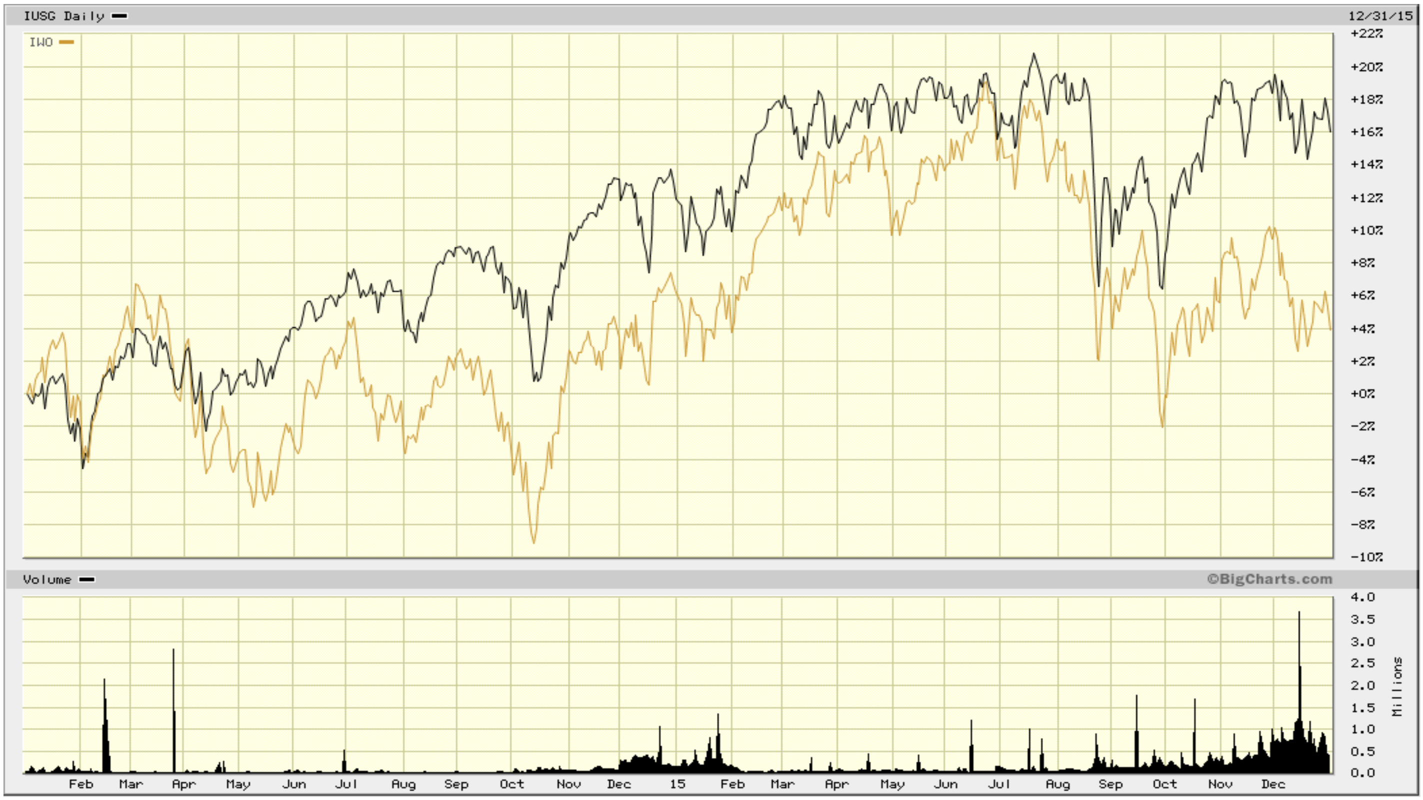
Russell 2000 beat S&P 500 in the years of 2010, 2013, and 2016.

The following chart compares the ETFs IUSG (S&P 500 growth) to IWO (Russell 2000 growth) from 2009 through 2017, 9 years.



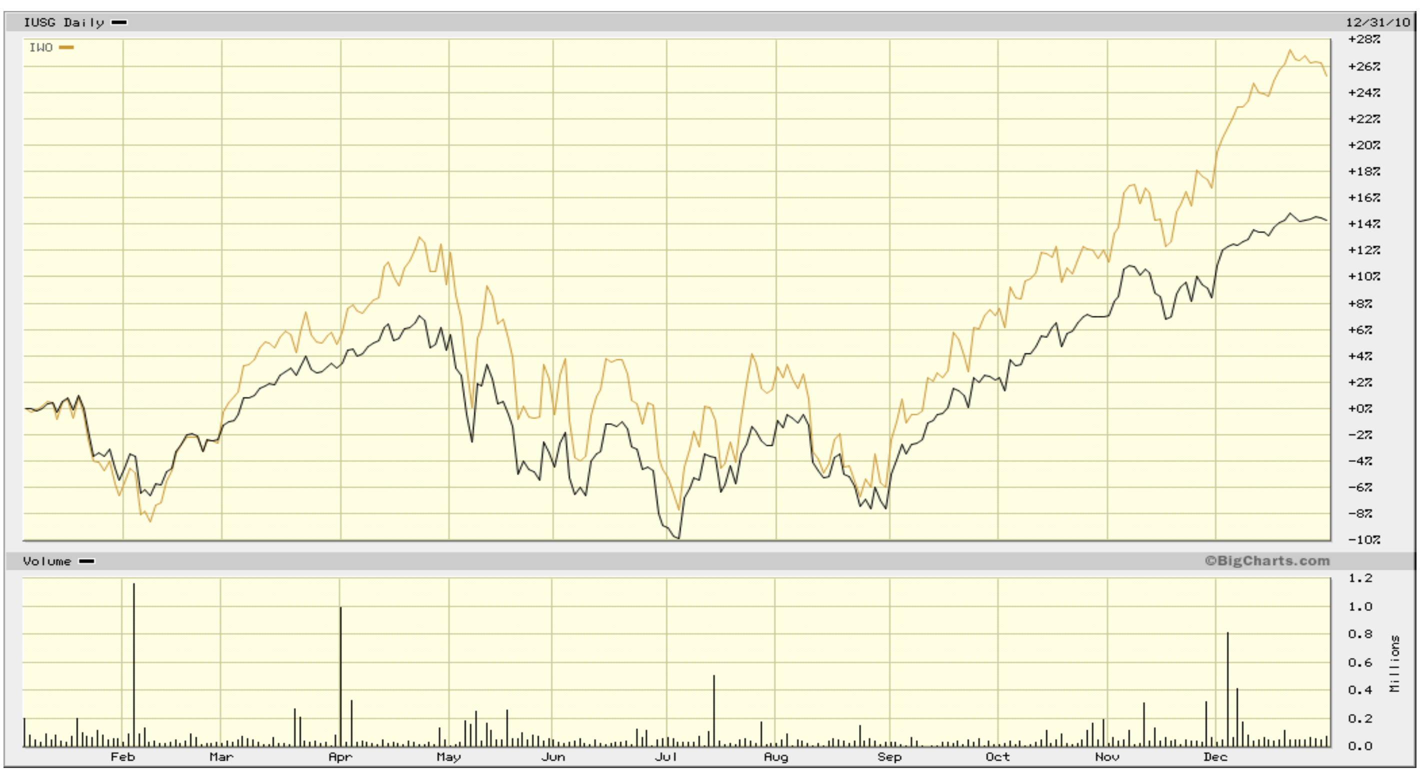
For the 9 years, there was only a 15% difference between them.

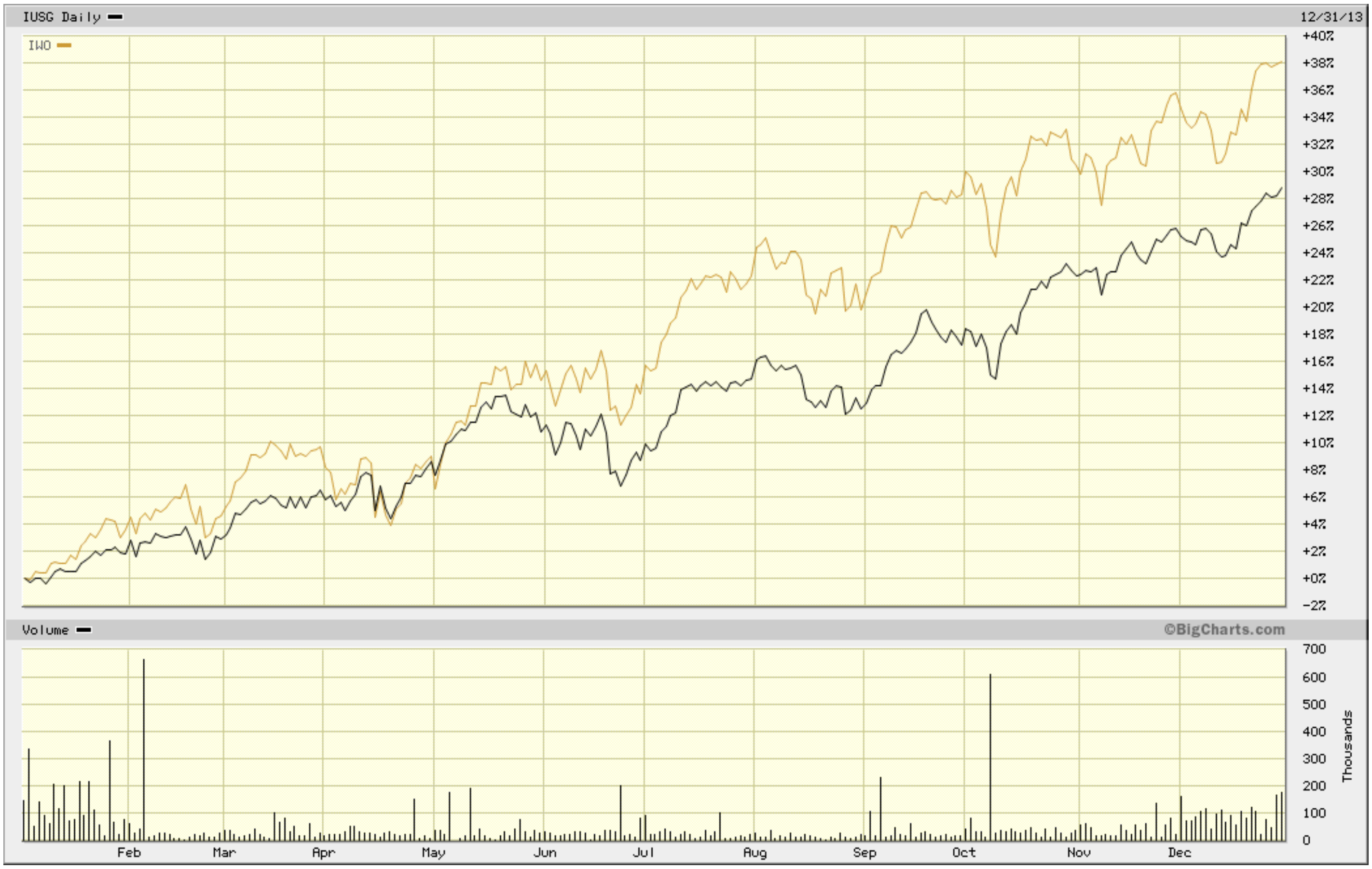
This next chart compares IUSG to IWO for the years 2014 through 2015.

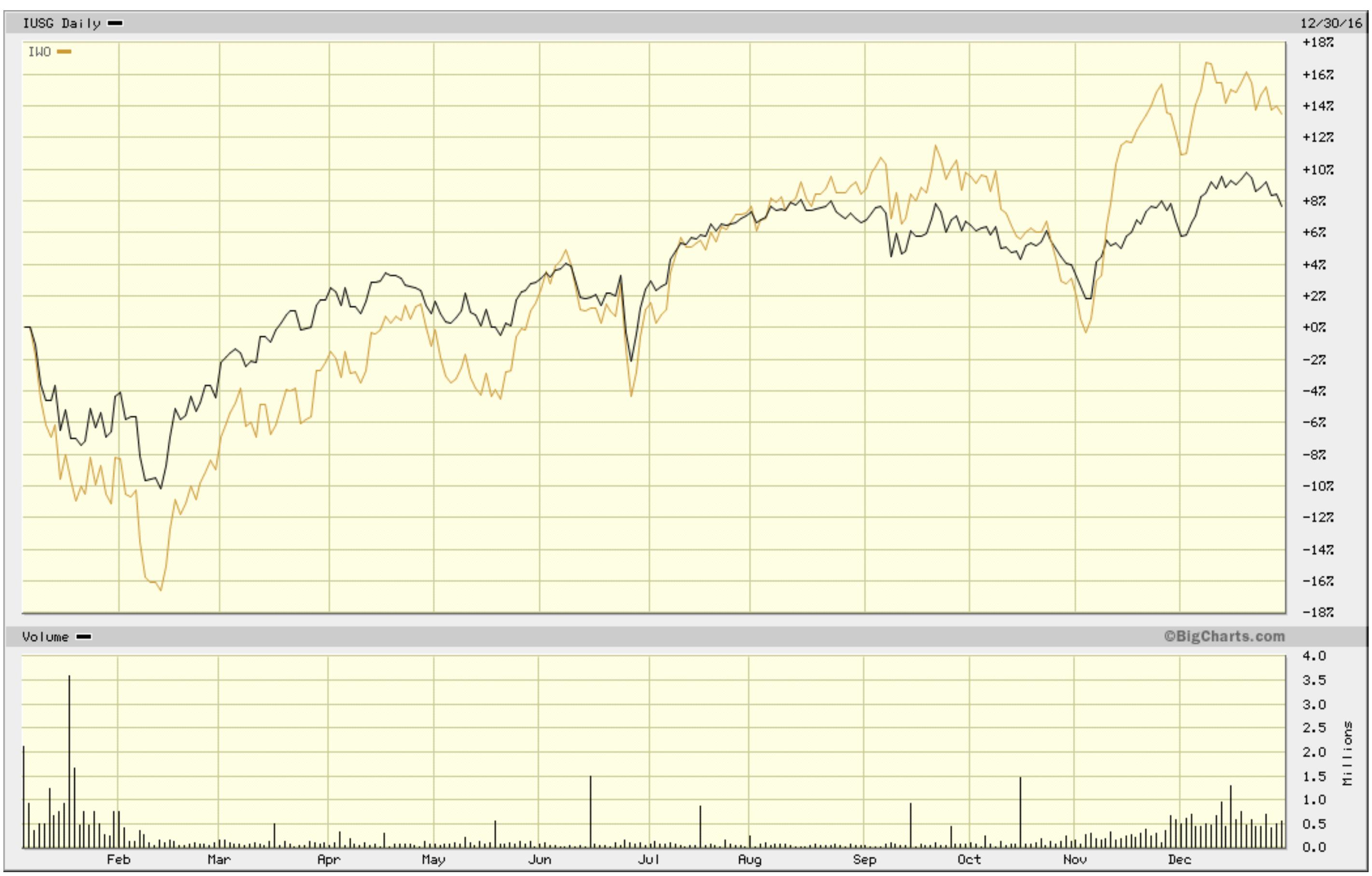


For the 2 years there was about a 12% difference.

The next 3 charts compare IUSG to IWO for the years 2010, 2013, and 2016.




IUSG Daily
12/31/13
IWO
+40%
+38%
+36%
+34%
+32%
+30%
+28%
+26%
+24%
+22%
+20%
+18%
+16%
+14%
+12%
+10%
+8%
+6%
+4%
+2%
+0%
-2%
Volume
©BigCharts.com
700
600
500
400
300
200
100
0
Thousands
Feb
Mar
Apr
May
Jun
Jul
Aug
Sep
Oct
Nov
Dec


IUSG Daily
12/30/16
IWO
+18%
+16%
+14%
+12%
+10%
+8%
+6%
+4%
+2%
+0%
-2%
-4%
-6%
-8%
-10%
-12%
-14%
-16%
-18%
Volume
©BigCharts.com
4.0
3.5
3.0
2.5
2.0
1.5
1.0
0.5
0.0
Millions
Feb
Mar
Apr
May
Jun
Jul
Aug
Sep
Oct
Nov
Dec

IWO bested IUSG by about 11% in 2010, 10% in 2013, and 6% in 2016. Remember, percentages are only comparable and additive when they are in the same time periods.

Even though the there was only a 15% difference for the total 9 years between IWO and IUSG, the individual charts and the Callan table clearly demonstrate the best investment category for 2014 and 2015 was S&P 500 (total 12%) while for 2010, 2013, and 2016 was Russell 2000. The Emerging Market yearly gains for 2009, 2012, 2017 were impressive at 78.51%, 18.23% and 37.28% respectfully.

To summarize, all equities have different characteristics which also affects the yearly returns, even if they are in the same category. Over a long-term period, like a business cycle expansion, a simple buy and hold strategy may appear to be a successful approach to achieving very good stock market returns. However, if equity investments were periodically exchanged to potential category leaders, enhance stock market returns could also be achieved.

Strategic Momentum Investing—SMI

Fool me once, shame on you. Fool me twice, shame on me.

Based upon the last two extreme stock market downturns, investors should be very concerned about stock market losses associated with future business cycle contractions, as well as the likelihood of drastically long recovery time frames. Should individual investors, especially boomers at, near, or in retirement, suffer another if avoidance is possible?

Effective retirement and wealth planning by all investors should assume there will continue to be extreme volatility (losses) in the stock market during future business cycle contractions. Prudent investors should seek out whatever means are available to preserve and grow their wealth. Based upon the losses sustained in the last two business cycle contractions, diversification DOES NOT work to effectively reduce stock market risk for the individual investor! But it DOES keep the money flowing for the Financial Industry!

Being human, our wheelhouse for decision making is based upon instant gratification, not something 20 - 30 - 40 or more years in the future. We are inherently lazy and prone to put off decisions and changes, especially if we feel inadequately prepared to make a decision. Our biases create an immediate roadblock for effective investing. Please read the following articles "Opinion: Americans are still terrible at investing, annual study once again shows" and "Poor investor performance: What can be done?" at the following websites.

"*https://www.marketwatch.com/story/americans-are-still-terrible-at-investing-annual-study-once-again-shows-2017-10-19*"

"*http://mathinvestor.org/poor-investor-performance-what-can-be-done*"

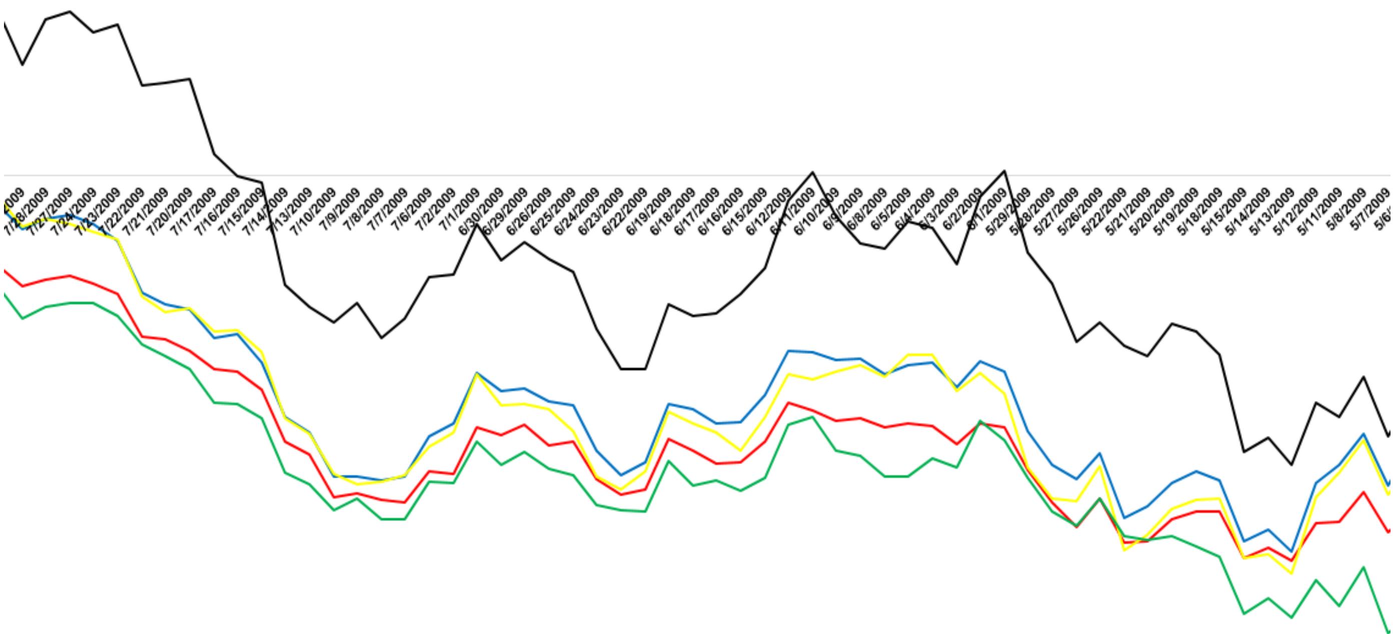
Financial professionals spend 80 – 90% of their client time dealing with behavioral finance issues. How much money are you wasting by having someone manage **YOU**? The W5000 (Wilshire 5000 Total Market Index) had very little volatility throughout 2017. The value increased 18.6%. How did the early 2018 stock market correction affected you? Did you start thinking about the 2008 - 2009? Did you make any investment changes?

We are very poor long-term investors. Human nature makes us all vulnerable to be deceived just as it cripples us, through our physiological biases and emotions, to make the appropriate changes for reducing our vulnerability and improving our decision making. No one is immune and even financial professionals succumb by making poor decisions from time to time.

Historically, three equity categories tend to dominate the highest yearly equity returns: small cap, large cap, and emerging markets. Enhanced stock market returns are achievable using just these three equity categories during a business cycle expansion.

Equity category comparisons can be made using the percentage value of current price activity to long-term price averages for each category. It provides an apple to apple basis for evaluation.

Look at the following break out of emerging markets (black line) which started in the beginning of the current business cycle expansion in 2009.



Emerging markets had a 78.51% return for 2009!

Historical results prove that certain equity categories do, in fact, have enhanced performance trends during certain time periods over other equity categories. By identifying those equity categories in the appropriate time frames, enhance returns are achievable. You might call this strategy timing the trend.

My Strategic Momentum Investing (SMI) strategy will notify the investor **WHAT** equity category to invest in and **WHEN** to invest in it, throughout the entire business cycle expansion. This strategy can be used for any 401k, IRA, 403b, 457b or brokerage account regardless of where it is or who manages it. My SMI whitepaper discusses the details of this strategy.

Visit my website, “Investescent.com” for all this content and more.

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