SMI - Strategic Momentum Investing

November, 2018

Successful long-term investing is only accomplished when the following axioms are practiced:

Stay invested throughout a business cycle expansion.

Do not attempt stock market timing with short term trading.

Build wealth through monthly dollar cost averaging.

Minimize the impact of Behavioral Finance issues associated with investing.

The primary decisions all investors, including financial professionals, struggle with are 1) what to invest in, 2) when to invest in it, and 3) mitigating risk. Since no one can accurately predict future returns or market risk, investment decisions seldom result in maximized returns or minimized risk.

Most investors should be familiar with the various equity asset categories like large-cap, mid-cap, small-cap, emerging markets, and international growth. Contained within many of these categories are the sub-categories of growth, blend, and value. There have been and will continue to be a myriad of studies detailing the pros and cons of which categories and sub-categories are best for investors to maximize long-term wealth. ***One constant throughout these studies however is that the equity category selected has the most impact on overall investment results rather than which actual investment is selected****.* If the experts cannot agree and historical results are always mixed, how can individual investors, or even financial professionals, determine which investments are appropriate, effective, and timely for maximizing investment returns and therefore achieving investing goals?

Daily stock market activity, and its related risk and reward, is random and is driven by domestic and global economic and political activity which can not be predicted. However, investment returns and systematic risk (market risk) are variable for all equity categories in different degrees and timeframes. While reviewing the following Callan Periodic Table of Investment Returns for 2017 (at callan.com) you will notice the historical yearly differences of investment returns and losses associated with the listed asset classes, categories and subcategories.

1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
S&P 500 Growth 42.16%	MSCI Emerging Markets 66.84%	Russell 2000 Value 22.83%	Russell 2000 Value 14.02%	Bloomberg Barclays Agg 10.26%	MSCI Emerging Markets 55.82%	MSCI Emerging Markets 25.55%	MSCI Emerging Markets 34.00%	MSCI Emerging Markets 32.17%	MSCI Emerging Markets 39.38%
S&P 500 28.58%	Russell 2000 Growth 43.09%	Bloomberg Barclays Agg 11.63%	Bloomberg Barclays Agg 8.43%	Bloomberg Barclays High Yield -1.37%	Russell 2000 Growth 48.54%	Russell 2000 Value 22.25%	MSCI World ex USA 14.47%	MSCI World ex USA 25.71%	MSCI World ex USA 12.44%
MSCI World ex USA 18.77%	S&P 500 Growth 28.24%	S&P 500 Value 6.08%	Bloomberg Barclays High Yield 5.28%	MSCI Emerging Markets -6.16%	Russell 2000 47.25%	MSCI World ex USA 20.38%	S&P 500 Value 5.82%	Russell 2000 Value 23.48%	S&P 500 Growth 9.13%
S&P 500 Value 14.68%	MSCI World ex USA 27.92%	Russell 2000 -3.02%	Russell 2000 2.49%	Russell 2000 Value -11.43%	Russell 2000 Value 46.03%	Russell 2000 18.33%	S&P 500 4.91%	S&P 500 Value 20.81%	Russell 2000 Growth 7.05%
Bloomberg Barclays Agg 8.67%	Russell 2000 21.26%	Bloomberg Barclays High Yield -5.86%	MSCI Emerging Markets -2.61%	MSCI World ex USA -15.80%	MSCI World ex USA 39.42%	S&P 500 Value 15.71%	Russell 2000 Value 4.71%	Russell 2000 18.37%	Bloomberg Barclays Agg 6.97%
Bloomberg Barclays High Yield 1.87%	S&P 500 21.04%	S&P 500 -9.11%	Russell 2000 Growth -9.23%	Russell 2000 -20.48%	S&P 500 Value 31.79%	Russell 2000 Growth 14.31%	Russell 2000 4.55%	S&P 500 15.79%	S&P 500 5.49%
Russell 2000 Growth 1.23%	S&P 500 Value 12.73%	MSCI World ex USA -13.37%	S&P 500 Value -11.71%	S&P 500 Value -20.85%	Bloomberg Barclays High Yield 28.97%	Bloomberg Barclays High Yield 11.13%	Russell 2000 Growth 4.15%	Russell 2000 Growth 13.35%	S&P 500 Value 1.99%
Russell 2000 -2.55%	Bloomberg Barclays High Yield 2.39%	S&P 500 Growth -22.08%	S&P 500 -11.89%	S&P 500 -22.10%	S&P 500 28.68%	S&P 500 10.88%	S&P 500 Growth 4.00%	Bloomberg Barclays High Yield 11.85%	Bloomberg Barclays High Yield 1.87%
Russell 2000 Value -6.45%	Bloomberg Barclays Agg -0.83%	Russell 2000 Growth -22.43%	S&P 500 Growth -12.73%	S&P 500 Growth -23.59%	S&P 500 Growth 25.66%	S&P 500 Growth 6.13%	Bloomberg Barclays High Yield 2.74%	S&P 500 Growth 11.01%	Russell 2000 -1.57%
MSCI Emerging Markets -25.34%	Russell 2000 Value -1.49%	MSCI Emerging Markets -30.71%	MSCI World ex USA -21.40%	Russell 2000 Growth -30.26%	Bloomberg Barclays Agg 4.10%	Bloomberg Barclays Agg 4.34%	Bloomberg Barclays Agg 2.43%	Bloomberg Barclays Agg 4.33%	Russell 2000 Value -9.78%

2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Bloomberg Barclays Agg 5.24%	MSCI Emerging Markets 78.51%	Russell 2000 Growth 29.09%	Bloomberg Barclays Agg 7.84%	MSCI Emerging Markets 18.23%	Russell 2000 Growth 43.30%	S&P 500 Growth 14.89%	S&P 500 Growth 5.52%	Russell 2000 Value 31.74%	MSCI Emerging Markets 37.28%
Bloomberg Barclays High Yield -26.16%	Bloomberg Barclays High Yield 58.21%	Russell 2000 26.85%	Bloomberg Barclays High Yield 4.98%	Russell 2000 Value 18.05%	Russell 2000 38.82%	S&P 500 13.69%	S&P 500 1.38%	Russell 2000 21.31%	S&P 500 Growth 27.44%
Russell 2000 Value -28.92%	Russell 2000 Growth 34.47%	Russell 2000 Value 24.50%	S&P 500 Growth 4.65%	S&P 500 Value 17.68%	Russell 2000 Value 34.52%	S&P 500 Value 12.36%	Bloomberg Barclays Agg 0.55%	S&P 500 Value 17.40%	MSCI World ex USA 24.21%
Russell 2000 -33.79%	MSCI World ex USA 33.67%	MSCI Emerging Markets 18.88%	S&P 500 2.11%	MSCI World ex USA 16.41%	S&P 500 Growth 32.75%	Bloomberg Barclays Agg 5.97%	Russell 2000 Growth -1.38%	Bloomberg Barclays High Yield 17.13%	Russell 2000 Growth 22.17%
S&P 500 Growth -34.92%	S&P 500 Growth 31.57%	Bloomberg Barclays High Yield 15.12%	S&P 500 Value -0.48%	Russell 2000 16.35%	S&P 500 32.39%	Russell 2000 Growth 5.60%	MSCI World ex USA -3.04%	S&P 500 11.96%	S&P 500 21.83%
S&P 500 -37.00%	Russell 2000 27.17%	S&P 500 Value 15.10%	Russell 2000 Growth -2.91%	S&P 500 16.00%	S&P 500 Value 31.99%	Russell 2000 4.89%	S&P 500 Value -3.13%	Russell 2000 Growth 11.32%	S&P 500 Value 15.36%
Russell 2000 Growth -38.54%	S&P 500 26.47%	S&P 500 15.06%	Russell 2000 -4.18%	Bloomberg Barclays High Yield 15.81%	MSCI World ex USA 21.02%	Russell 2000 Value 4.22%	Russell 2000 -4.41%	MSCI Emerging Markets 11.19%	Russell 2000 14.65%
S&P 500 Value -39.22%	S&P 500 Value 21.17%	S&P 500 Growth 15.05%	Russell 2000 Value -5.50%	S&P 500 Growth 14.61%	Bloomberg Barclays High Yield 7.44%	Bloomberg Barclays High Yield 2.45%	Bloomberg Barclays High Yield -4.47%	S&P 500 Growth 6.89%	Russell 2000 Value 7.84%
MSCI World ex USA -43.56%	Russell 2000 Value 20.58%	MSCI World ex USA 8.95%	MSCI World ex USA -12.21%	Russell 2000 Growth 14.59%	Bloomberg Barclays Agg -2.02%	MSCI Emerging Markets -2.19%	Russell 2000 Value -7.47%	MSCI World ex USA 2.75%	Bloomberg Barclays High Yield 7.50%
MSCI Emerging Markets -53.33%	Bloomberg Barclays Agg 5.93%	Bloomberg Barclays Agg 6.54%	MSCI Emerging Markets -18.42%	Bloomberg Barclays Agg 4.21%	MSCI Emerging Markets -2.60%	MSCI World ex USA -4.32%	MSCI Emerging Markets -14.92%	Bloomberg Barclays Agg 2.65%	Bloomberg Barclays Agg 3.54%

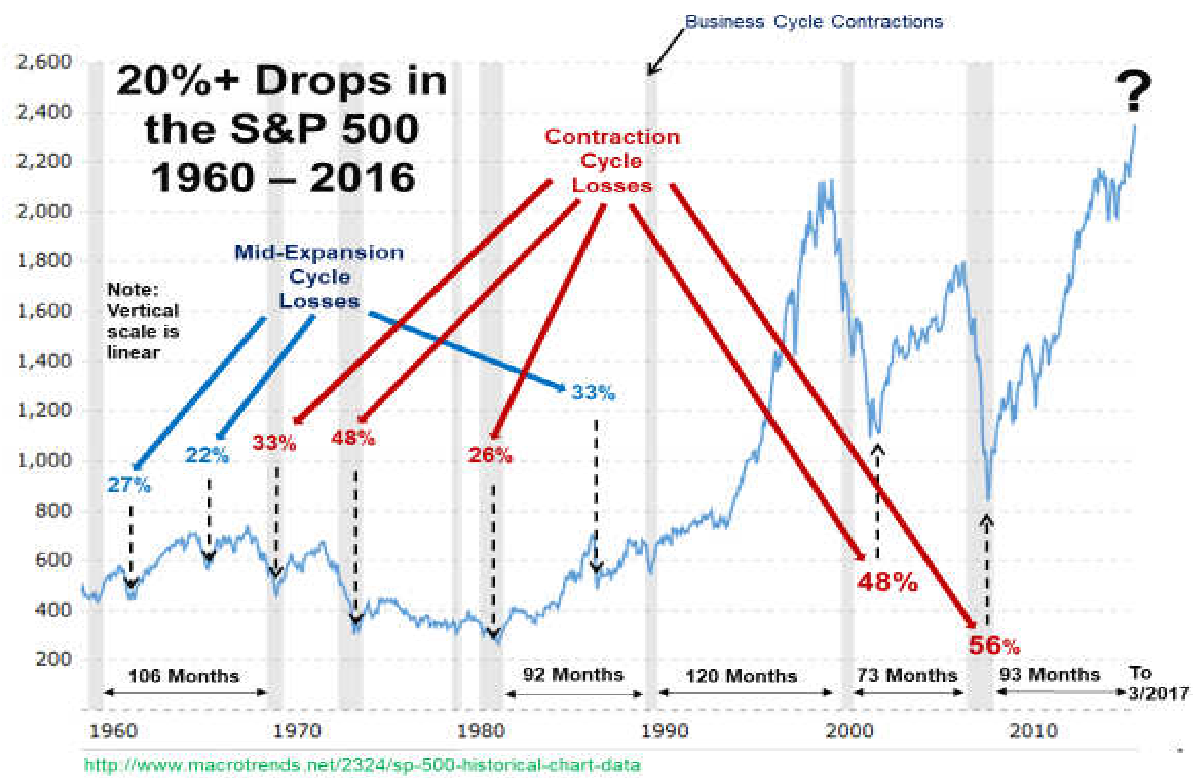
Even in stock market down years, like 2011 and 2015, there were some positive returns for certain equity categories. Emerging markets dominates both the highest and lowest percentage levels of equity gains and losses (high risk, high reward usually coincides with the greatest volatility). Russell 2000 (small-cap) and S&P 500 (large-cap) growth categories have generally performed better than value or blend (mix of growth and value, or index) as can be seen from the table above for the last 20 years.

It needs to be noted that these returns are based on calendar activity only. Any potential personal returns or losses are directly associated with personal holding periods. For example, if you owned emerging markets from the beginning of 2011 to the end of 2012, your overall return for that 2-year period would have been -3.55% (-18.42 + 14.87 (81.58 x .1823)).

Investment returns vary dramatically over different holding periods, even within a calendar year. In 2012, the small cap blend ETF of IJR (iShares Core S&P Small-Cap) had a 5.5% return over the emerging market ETF of EEM (iShares MSCI Emerging Markets Index) from 1/1/12012 through 6/30/2012. But from 6/1/2012 to 12/31/2012, EEM had a 7% greater return than IJR.

What can be gleaned from all this randomness of investment results which may or may not be useful for future investment decisions? Further details are discussed below in first, business cycles, second, stock market trends, and third, category momentum.

BUSINESS CYCLES: Business cycles are real, reoccurring, but not cyclical. Within each cycle there will be a low (trough), an expansion period, a high (peak), and a contraction period. They have been tracked and studied since the mid-1800s. The National Bureau of Economic Research (NBER at www.nber.org) contains details about past business cycles. The lengths of both expansions and contractions vary but expansions have lasted an average of 5 times longer than contractions based on the last 13 cycles (almost 22 times longer based the last 3 cycles). The stock market is a leading economic indicator. Stock market values ***increase*** during expansions and ***decrease*** during contractions. Due to randomness, stock market high and lows cannot be predicted. Within a business cycle, stock market corrections will occur where equity values can decrease during an expansion and even increase during a contraction. These occurrences are also random and cannot be predicted. See the following S&P 500 graph (investescent.com).



The current business cycle expansion has now lasted for over 10 years. As of April, 2019, it is now the longest in recorded history.

Looking again at the S&P 500 graph, notice the rate of change in S&P value (both increasing and decreasing) during the business cycles starting in 1990 (actually since the mid-1990s) as compared to pre-1990. The dramatic gains and losses should make investors both wary and concerned regarding future activity, especially since the volatile patterns are continuing. Based upon the severity of losses in the last two business cycle contractions, avoiding future devastating stock market declines must become a priority to secure future wealth.

STOCK MARKET TRENDS: As previously addressed, daily stock market activity and intra-expansion corrections are random. Stock market values generally increase in expansions. See the following personal graph of the Wilshire 5000 Total Market Index values, W5000, from April, 2009 through 2017.

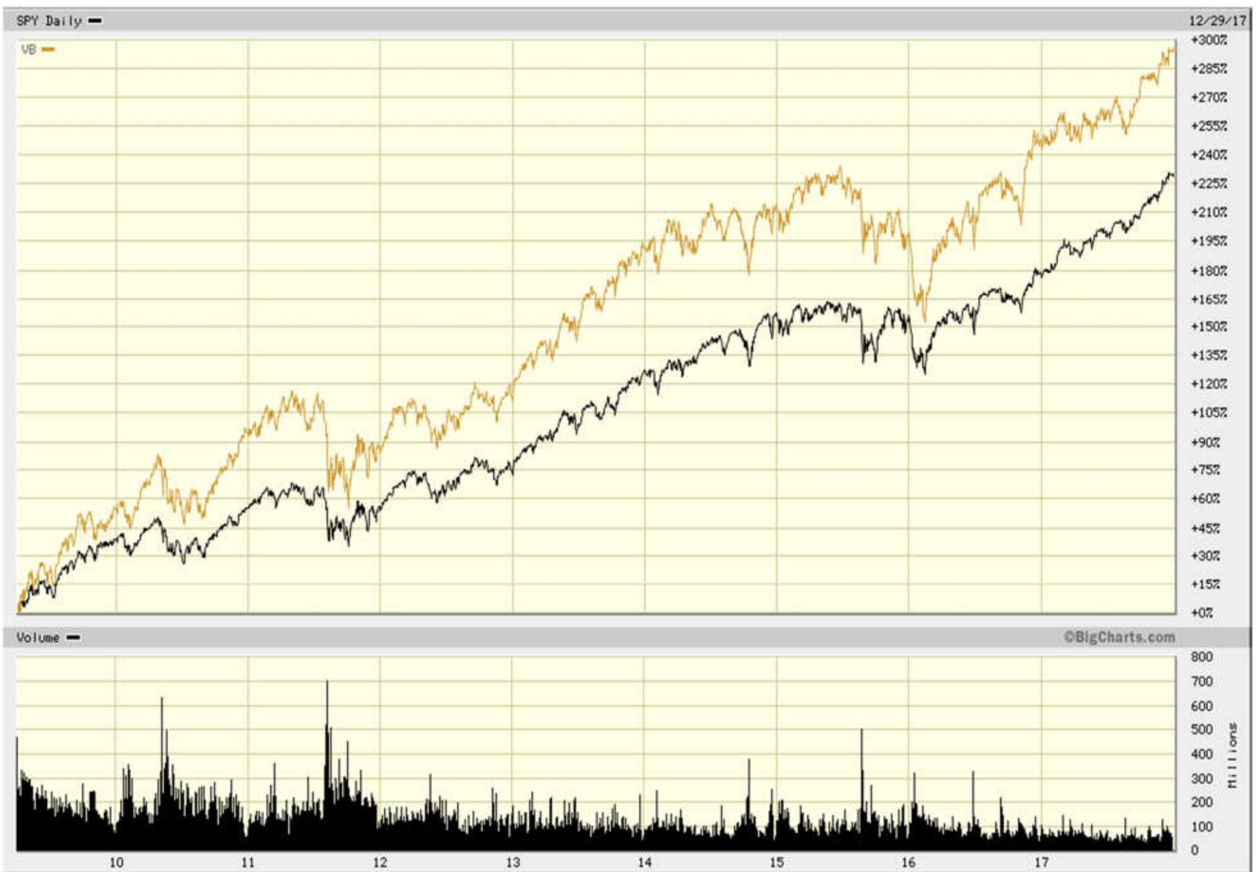
From the business cycle trough in March, 2009, there have been four significant intra-expansion corrections; 2010, 2011, 2015/2016, and 2018. However, through this current expansion, the long-term trend has been increasing. The smoothed lines are 210 and 440-day simple moving averages (SMA) of the W5000 values. They provide a long-term and ongoing view of the trending values of the W5000 at any point in the expansion timeframe. Market corrections tend to break under the 210-day SMA more so than the 440-day SMA.

As stated before, asset categories and sub-categories are affected by the same domestic, global, economic, and political activities but not by the same degree and not at the same time. During an expansion, the overall trend for all equities generally will be upward, including the specific trends for equity categories or sub-categories.

Following are the historical equity category return leaders for the years 2009 – 2017 as seen previously.

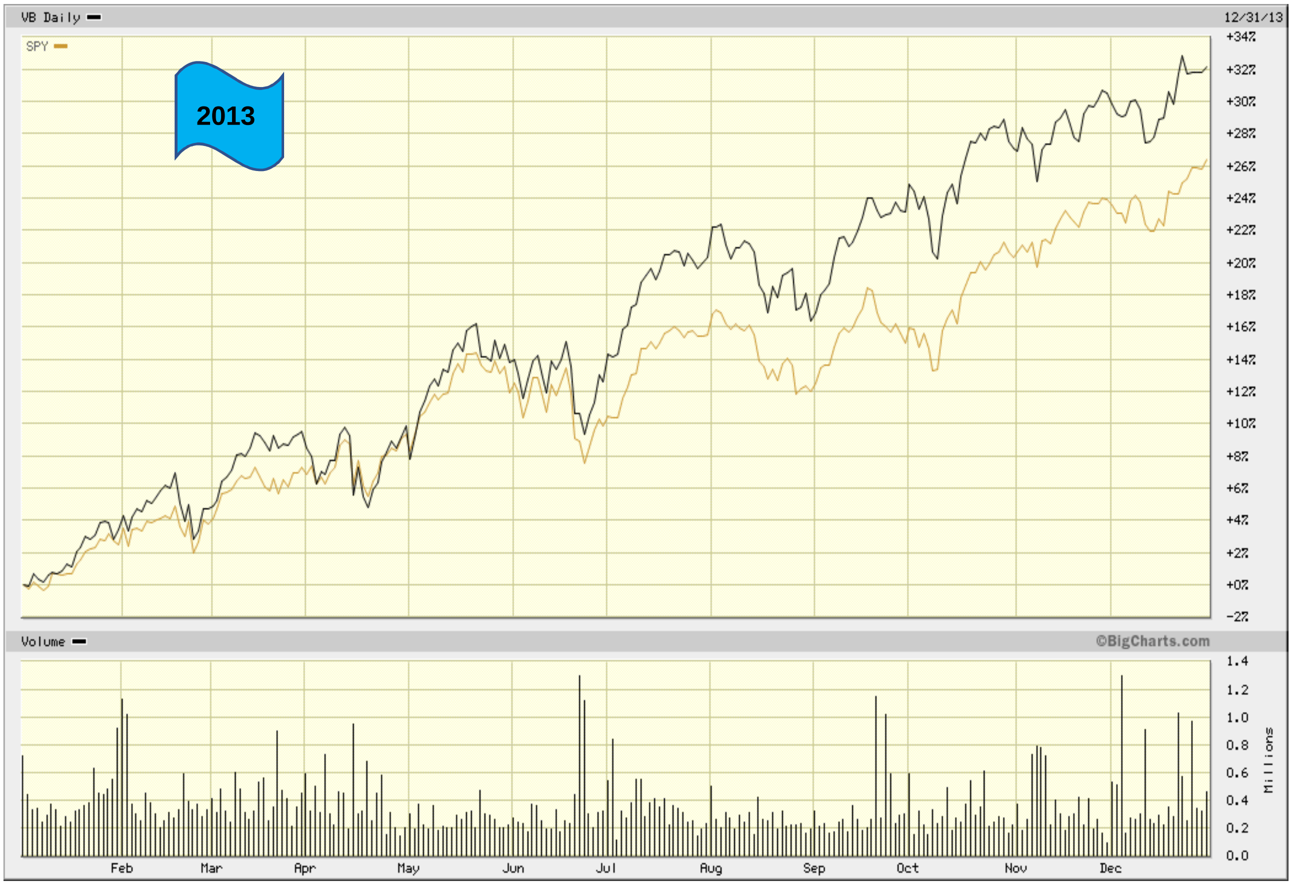
2009	Emerging Markets
2010	Russell 2000 Growth
2011	S&P 500 Growth
2012	Emerging Markets
2013	Russell 2000 Growth
2014	S&P 500 Growth
2015	S&P 500 Growth
2016	Russell 2000 Value
2017	Emerging Markets

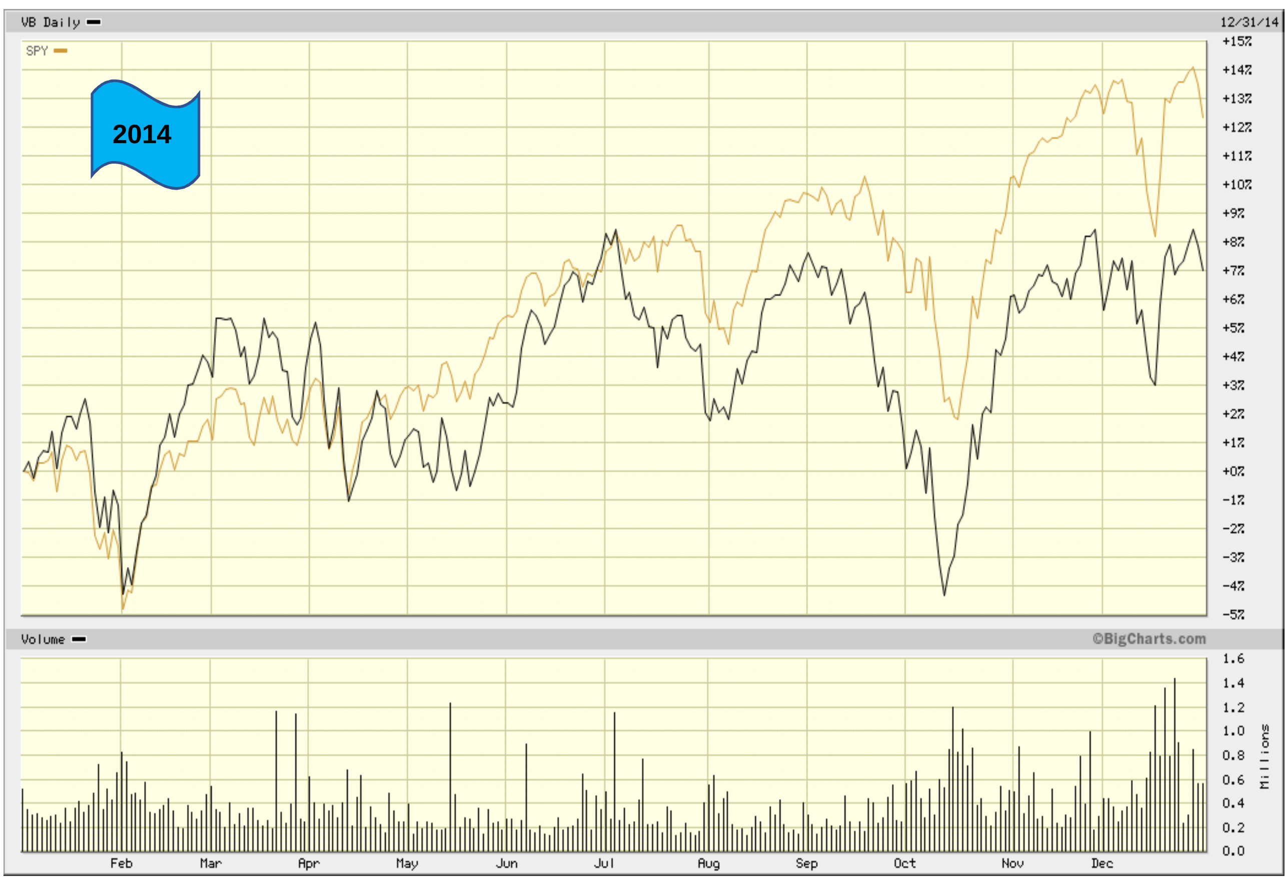
Comparisons of actual investments within these categories can be made for any timeframe. Following is a chart (from bigcharts.marketwatch.com) comparing the ETFs (Exchange-Traded Funds) of SPY, S&P 500 Large-Cap and VB, Vanguard Small-Cap from 4/1/2009 through 2017.



Overall, it appears investing in small-cap rather than large-cap throughout this entire expansion would have been the best strategy. However, the Callan return chart shows S&P 500 Growth as the top equity category in the years 2011, 2014, and 2015. Russell 2000 Growth was top in 2010, 2013, and 2016. Further comparisons will also ignore the sub-categories of growth and value and look specifically at blend or index type investments.

The following comparisons are specific years for SPY and VB.


VB Daily
12/31/13
SPY
2013
+34%
+32%
+30%
+28%
+26%
+24%
+22%
+20%
+18%
+16%
+14%
+12%
+10%
+8%
+6%
+4%
+2%
+0%
-2%
Volume
©BigCharts.com
1.4
1.2
1.0
0.8
0.6
0.4
0.2
0.0
Millions
Feb
Mar
Apr
May
Jun
Jul
Aug
Sep
Oct
Nov
Dec


VB Daily
12/31/14
SPY
2014
+15%
+14%
+13%
+12%
+11%
+10%
+9%
+8%
+7%
+6%
+5%
+4%
+3%
+2%
+1%
+0%
-1%
-2%
-3%
-4%
-5%
Volume
©BigCharts.com
1.6
1.4
1.2
1.0
0.8
0.6
0.4
0.2
0.0
Millions
Feb
Mar
Apr
May
Jun
Jul
Aug
Sep
Oct
Nov
Dec

Clearly, small-cap exceeded large-cap in 2013 and large-cap exceeded small-cap in 2014. Historically, small-cap had the largest percentage gain from 4/1/2009 through 12/31/2017 than all the other categories (as measured using IVV-Large Cap, IJR-Small Cap, and EEM-Emerging Markets):

IJR	315%
IVV	230%
EEM	80%

[Note of Caution – Percentages are only comparable when applicable to the same time period.]

A strategy of all small-cap throughout the whole expansion, as seen by the approximate gains above, appears to have been the best strategy. However, it ignores changes which occur periodically between categories. Following are the bigcharts results from 2017.

EEM	33%
IVV	19%
IJR	11%

Following are the bigcharts results from 2014.

IVV	12%
IJR	6%
EEM	-2%

CATEGORY MOMENTUM: Price activity (both in absolute values and percentage gains or losses) between categories is always different. During this upward trend in the current business cycle expansion for the 10 years, all equity categories have not increased or decreased by the same amount or even in the same timeframe. The previous two charts show an upward trend for each year and increasing price changes for both EFTs even with occasional dips. VB's price change for 2013 was 6% greater than SPY. For 2014, SPY's was 5% greater than VB. Looking closer at the 2014 chart, notice SPY actually had the greater percentage of price change from July through December not the entire year. The Callan return chart, above, displays these category differences from a calendar year standpoint.

Tracking price movement over a longer timeframe will highlight a trend. How can price changes between categories be calculated, tracked, and compared? Is there a way to take advantage of these trend differences by making appropriate investment selections within the appropriate timeframes throughout an entire business cycle expansion?

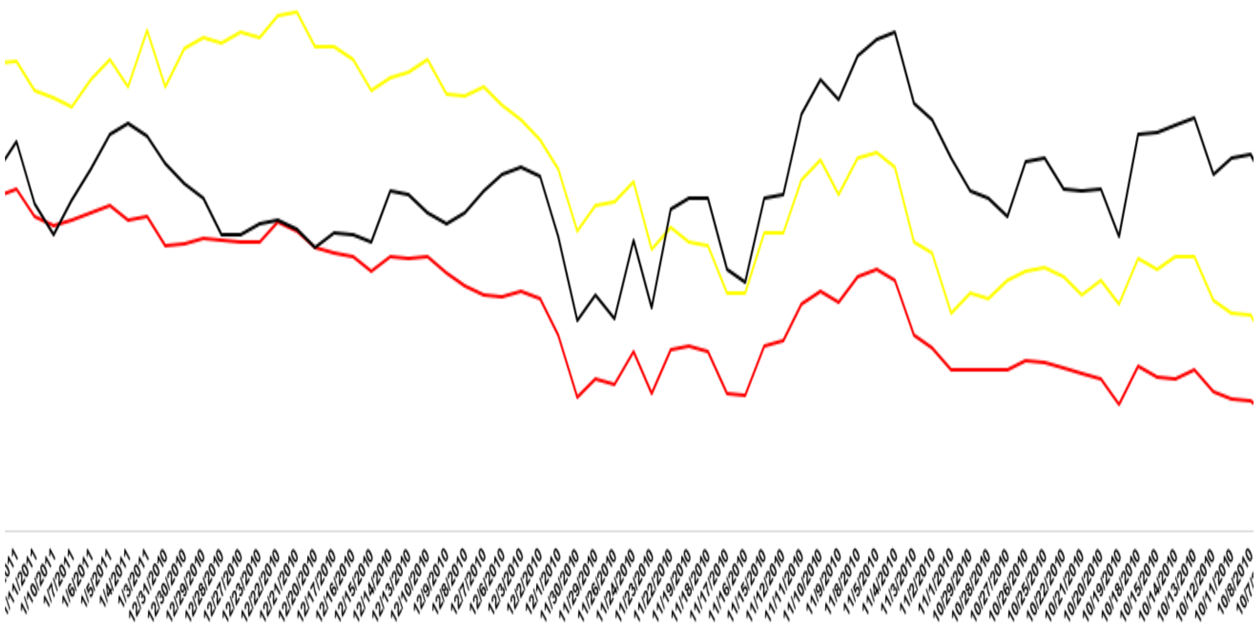
Even similar investments within each equity category have different price structures. Day to day price movement only reflects random price activity. However, by tracking daily activity, where the actual price is expressed as a percentage of an appropriate long-term price trend, you can chart relative price strength or weakness (momentum) for any actual category investment. During periods of higher percentages (higher prices) relative to the long-term price trends, the investments momentum is also higher. The opposite holds true for lower momentum. Since all these momentum figures (associated with specific equity category investments) are expressed as percentages, tracking and direct comparisons between categories can therefore be made.

The following ETF investments were used as representatives for their respective equity category.

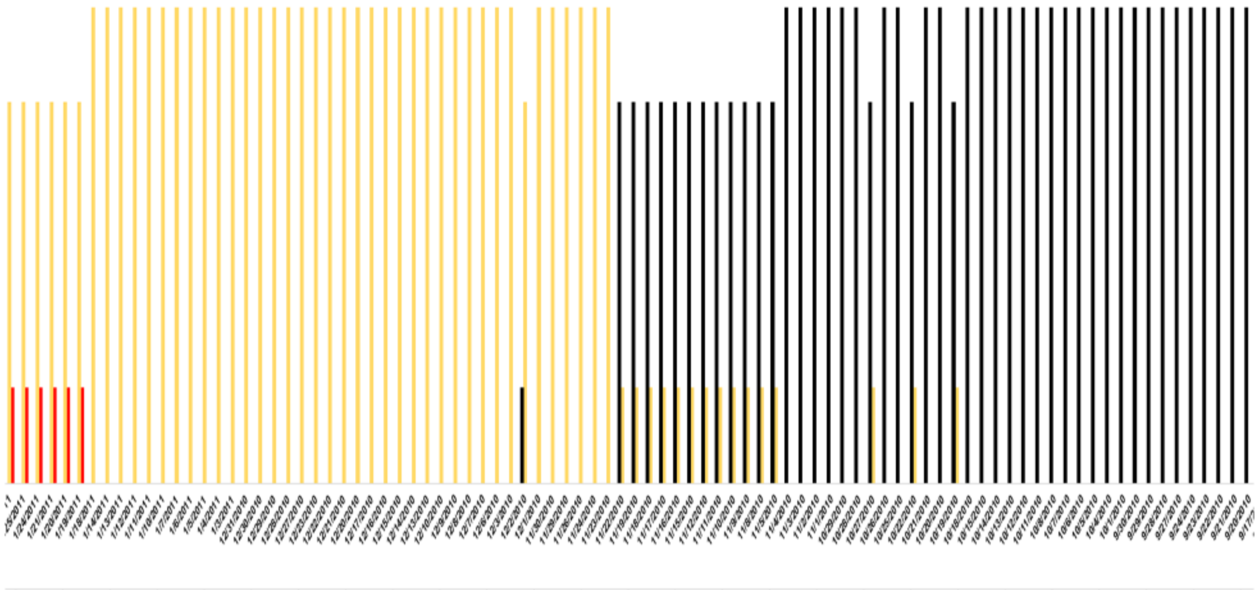
IVV	iShares S&P 500 Index – **Large Cap**
IJR	iShares Core S&P **Small Cap**
EEM	iShares MSCI **Emerging Markets** Index

While the actual return of specific equity category investments will differ slightly from each other based upon their portfolio holdings, generally any specific investment will be representative of the entire equity category. Also, whether mutual funds or ETFs are used in the comparisons, the results are effectively the same. Investment return and momentum for the equity subcategories of growth, value, and blend are different. Since blend or index is an amalgamation of both growth and value, a blend investment can be used as an evaluator for an overall equity category. Since the historical results for blend equities fall between growth and value with minimal differences, there is little incentive to track or invest in either growth or value investments.

Following is a snapshot of the chart displaying the long-term trends numerical averages in 2010 highlighting the momentum change from EEM (black) to IJR (yellow). The EEM line peaks and falls below the IJR line indicating a momentum shift in prices relative to their long-term trends. IJR now strengthens and will be maintained for approximately 9 months. Red is IVV. A stock market correction occurred in 2011 but equity investments were still maintained since the business cycle expansion was ongoing.



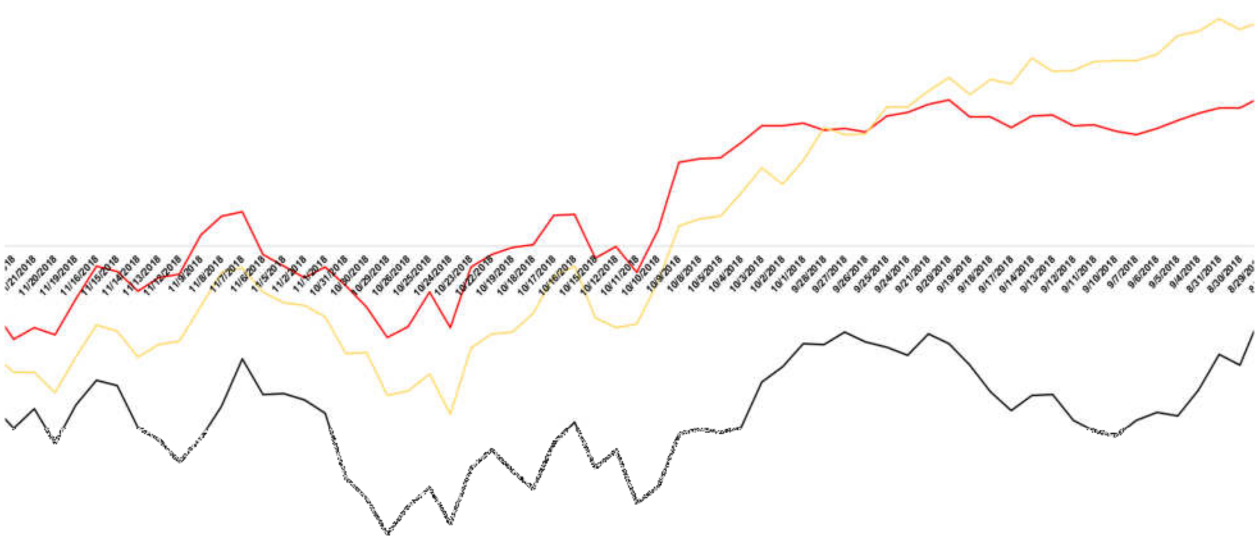
In addition to looking at the long-term trends numerical average chart, as well as the individual trend charts, the data can also be viewed from a leadership position based on all the trends. Instead of the numerical average difference, each category leader, in each long-term trend, can be scored every day and charted. This pictorial view provides a relational comparison between the categories. Following is a snapshot of the same timeframe as above. Black is EEM and gold is IJR. Notice IVV, red, does not appear until late January when is starts to strengthen compared to IJR on the right of both charts.

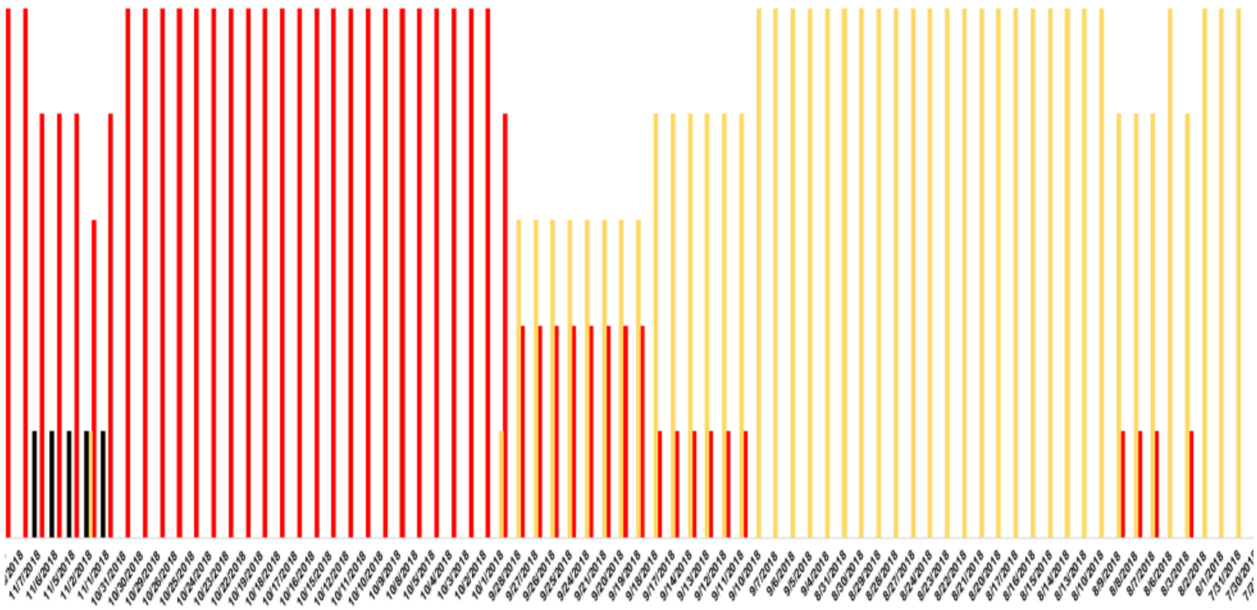


This innovative investment approach for individual investors is both unique and pioneering. Remember, the focus is not based on day to day or even week to week price activity. The goal is to identify the equity category price momentums which occur naturally throughout a business cycle expansion and direct investments toward that category within the appropriate timeframe.

This service is best used in tax-advantaged accounts where gains and losses are considered. If this service is used in taxable accounts, capital gains and losses will be experienced.

The next two snapshots display the momentum change from IJR, gold, to IVV, red in 2018.

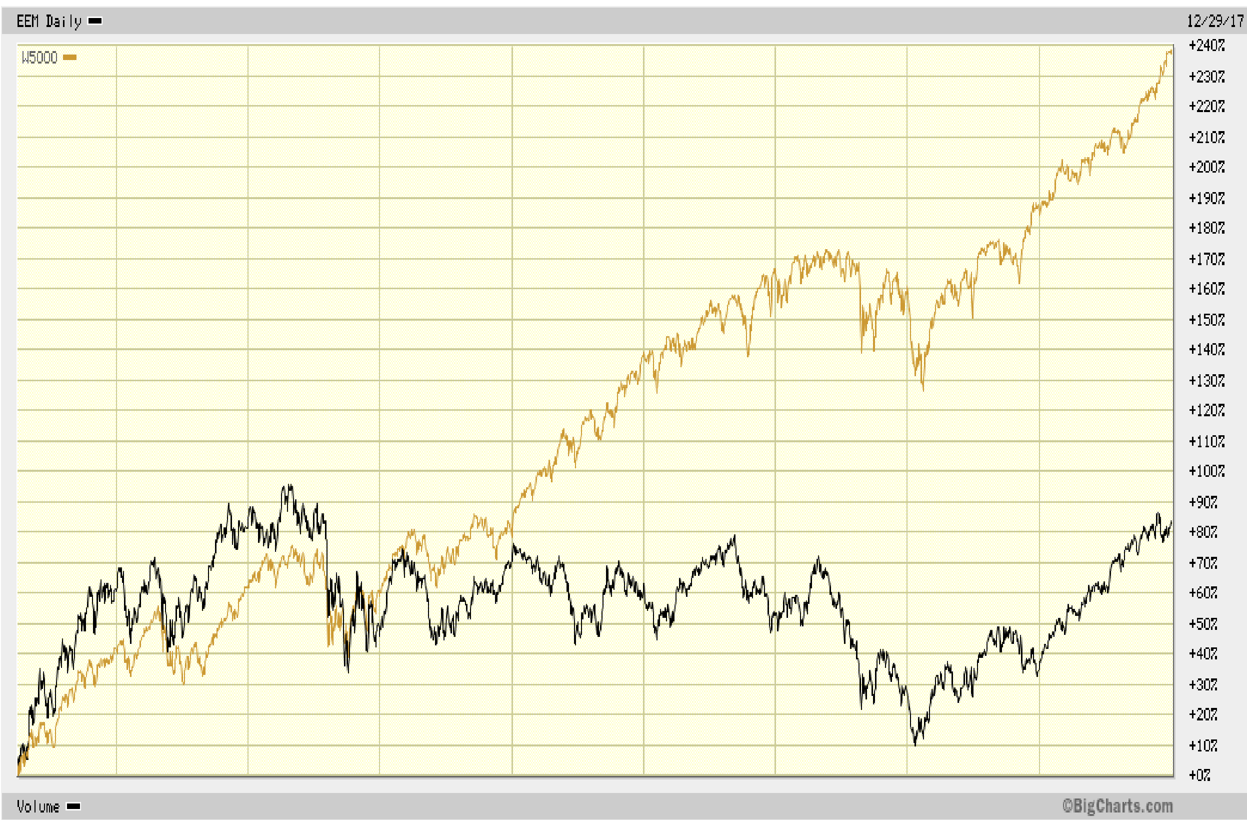




REMEMBER:

Staying invested 100% in equities during a business cycle expansion, even throughout occasional stock market corrections, will maximize investment returns.

The following charts (again from bigcharts) show the price increases from 4/1/2009 through 12/31/2107 for the investments of IJR, IVV, and EEM as well as the W5000 index:



Maximizing returns can be achieved without frequent trading by focusing on investment categories with stronger price appreciation, or momentum, during certain periods throughout a business cycle expansion. The actual investment is of little concern so long as the correct equity category is selected. Oftentimes, the few percentage points differences between applicable subcategories (value, growth, blend) is minor compared to just achieving enhanced market returns through the use of higher momentum equity categories. For evaluation purposes, the equity subcategories of growth and value within the equity categories of large cap and small cap will also be monitored.

SMI can be used for any portfolio, regardless of where the monies are maintained (401k, 403b, 457b, IRA, Regular Brokerage, etc.) or who manages them (Self, Vanguard, Fidelity, Schwab, Edward Jones, other Financial Professionals and firms or IAs).

For a small reoccurring fee, you can finally have your primary investment questions (What to Invest in and When to Invest in it) answered with the confidence you will be achieving the best possible returns throughout a business cycle expansion and the occasional stock market corrections.

I do not make a living off my clients. I only offer services with low, transparent fees. I promote investor education and self-investing. I always invest my personal monies the same way I advise my clients.

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