Fall 2019

Financial Outlook

Dow Theory: Curbing Emotional Investing

In addition to starting the company that publishes The Wall Street Journal, Charles Dow (1851–1902) also lent his name to one of the most popular U.S. stock market indexes (the Dow Jones Industrial Average) and created a theory regarding major shifts in stock market trends. While neither Dow nor those who refined the Dow theory after him believed they were creating a sure-fire way to beat the market, they did believe that following its principles could at least avoid the mistakes associated with greed and fear.

Three Assumptions

Behind the Dow theory is a set of assumptions about how the stock market works:

- **The stock market moves in broad cyclical trends.** According to Dow, there are primary trends, which are long lasting (from months to years), and minor trends, which don't last long and run in the opposite direction of the primary trend. Primary up trends are bull markets and primary down trends are bear markets — these are marked by peaks and troughs in price charts. Within these broader trends, there are secondary (minor) countertrends called corrections, which can retrace anywhere from 33% to 67% percent of the primary trend's movement. Of course, no one ever knows in advance how long trends will last (that's a key principle of the Dow theory). And since market prices fluctuate from day to day, it's dangerous to make too much out of a single day's movement.
- **Primary trends can't be manipulated.** While it may be possible for private interests to manipulate the price of one security for a relatively short period of time, the Dow theory holds that the primary trend in the stock market is driven by forces much bigger than any single individual, cartel, breaking news, or rumor.
- **The stock indexes reflect all available information.** The Dow theory believes that everything there is to know about a stock and the economy at a given moment is factored into the prices of stocks. This include hopes, fears, and expectations of such factors as interest rates, earnings, revenue, and product initiatives. Unexpected events can occur, but usually they affect the short-term trend, creating what are called reaction rallies. These soon lose steam and the primary trend resumes.

Three Primary Trend Phases

According to the Dow theory, major trends consist of three phases of varying length:

Stage 1: Accumulation or distribution. In this phase, the smart money — typically large institutional investors like investment banks, pension funds, and mutual funds — start major buying or selling programs. Initially, this looks like a secondary countertrend, but

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Dow Theory

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trading volume on the major exchanges noticeably increases on up days, while volume tends to be lighter on down days. In a bull market, stocks are cheap, but no one other than value investors seems to buy them. In a bear market, there's a high level of enthusiasm for stocks, and few people believe the bull market is over.

Stage 2: The big move. In this phase, there are many more days in which the indexes move in the direction of the primary trend than in the opposite direction. In bull markets, there are strings of up days, followed by shorter strings of down days, reflecting the spread of enthusiasm for stocks. In bear markets, the opposite occurs, as anxiety and pessimism mount. The result is a significant, long-term increase (bull markets) or decrease (bear markets) in the market averages.

Stage 3: Excess. The final phase of a primary trend is marked by extremely high levels of emotion — enthusiasm in bull markets and pessimism in bear markets — which are signs that the primary trend is about to change. These extremes can be seen in the behavior of individual investors: in bull markets, even the most conservative investors are buying stocks. On the other hand, in the excess stage of a bear market, everyone is concerned about safety of principal, while those who bought stocks at high prices have finally given up and sold at a loss.

The Indexes Confirm the New Trend

For Charles Dow, the primary trend was reflected in the Dow Jones Industrial Average, which today comprises 30 stocks. But Dow also looked to another index to confirm the emergence of a new trend. In his day, that was the Dow Railroad Index. Today, it's the Dow Transportation Index of 20 companies engaged in the shipping and transportation of manufactured goods, including marine transport, railroads, and trucking. The idea was a true change in the trend of business activity in the big manufacturing firms would show up in business for the companies that move the goods they make.

For the second index to confirm the first, the Dow theory looks for both averages to be moving in the same direction. New highs or lows in one index are accompanied by highs or lows at the same time or shortly thereafter in the other.

The Dow theory isn't intended to help short-term traders. What it's designed to do is tip off long-term investors to changes in the trend, so they can shift their money from stocks to another asset class, like bonds or cash, during a full business cycle.

Please call if you'd like to discuss this in more detail. ❍❍❍

How to Get a Handle on Spending

Most people wish they have more money saved away, no matter what their ultimate financial goals. It's easy to want more than what we have and think a higher income is the key to solving all of our problems. It is more difficult to see a lot of our issues are less about how much we make and more about how much we spend. When it comes to controlling our expenses, sometimes we just don't know where our money goes. This means we could all use a few tips:

- Break down monthly discretionary expenditures. Look at your bank statements and bills over the last month and see how much you really spend on dining out, groceries, entertainment, and clothing. Look for ways to reduce spending, either by cutting back or choosing less expensive options. Clean out your closet and dresser to remind yourself what you already own. It may seem like these options will only save a few dollars, but over time it adds up.
- Take a look at your major expenditures. While you may have resigned yourself to large monthly payments for your auto or homeowners insurance, you can actually save a lot by looking around for better rates. Consider strategies to reduce your income tax and research whether or not it makes sense to refinance your home to lower your mortgage payments.
- Create a written spending plan. Budget for what you need on a monthly basis and commit to abstaining from off-budget items.
- Stop using your credit cards (at least for a while). The ease of swiping a plastic card to make a purchase removes some of the psychological restraint we show when we have to count out actual dollar bills. Go old school and use paper money

How to Get a Handle on Spending

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for a few months to get a better feel for how much you are really spending.

- ❍ When faced with an impulse purchase option, sleep on it instead. You can always come back later if you've taken time to think and compare prices online.
- ❍ Before you make a major purchase, think carefully about the long-term expenses involved. If you are about to buy a new car, remember that sticker price is just the beginning — maintenance, upkeep, and insurance costs also need to be factored into the overall investment. Consider a less expensive or used car and keep it for several years instead of getting a new one every other year.
- ❍ Once you are preapproved for a mortgage amount, commit to spending much less than the maximum allowed. Remember that your monthly mortgage costs are not the only expenses of home ownership. Living well within your means also means more money left over for savings and covering unexpected expenses instead of being forced to take on more debt.

We've all made poor money decisions at some point in our lives. But that doesn't mean we're doomed to repeat them. The trick is to be intentional in making wiser choices about how we spend our resources and get our savings on track for the future. Please call if you'd like help in this area. ❍❍❍

Having the Talk

Take a moment and pretend your older sister and her husband pass away unexpectedly, leaving their three young children behind. You are called into their lawyer's office immediately. You learn that you and your husband were named guardians of your three nieces and the family dog. While you love your nieces, your life just changed in the blink of an eye. You went from being a professional, childless, young couple in a condo to a five-person family with a dog and a two-story home. Situations like this don't just happen in movies — they happen to people in real life, and not as infrequently as you might think.

Now imagine you are the parents of those three children. What if your younger sister and her husband weren't able (or willing) to care for your children? What if they decided to pass guardianship on to the next person; or worse, what if the children had to go live in foster care? Or what if your sister and her husband accept guardianship of your children, but move them into that condo in the city? These conversations are absolutely critical if you have dependents.

In many families, finances and estate talk are taboo. Talking about what will happen after a person dies can be painful and scary, but necessary. It's important to talk with your loved ones about what you want, what they want, and what is laid out in your will.

4 Tips for the Talk

- ❍ **Keep it light —** Having this discussion can bring up a lot of emotions for your loved ones; thinking about losing someone you love so dearly is painful. So keeping the conversation light but to the point can help keep it on track and productive. There may also be tensions that arise through the process — maybe multiple people want the same thing, or someone gets offended by how you've decided to split your money. You might consider conversing with people individually to avoid upset.
- ❍ **Talk openly and honestly —** A choice you have made may hurt someone's feelings, or there may be decisions you don't want to tell people about, but it is crucial to be open and honest with your beneficiaries.
- ❍ **Discuss values, not just valuables —** When you die, how do you want people to remember you? What parts of you do you want to live on? This may include traditions, values, family names, rituals, religious beliefs, and so on. This is an important matter to bring up during discussion with your family. Think back on times that meant a great deal to your family or traditions that have brought joy. Maybe it's important to you to have your grandmother's name passed on from generation to generation. Talk about this with your family to share how you feel and see how they feel.
- ❍ **Have a professional present —** Having your estate planner present can be helpful, and in some cases, necessary. Many times, a professional has a better understanding of how estate planning works and can assist by answering any questions your loved ones may have. You might have a family-only conversation first and then a second conversation with your family and the estate-planning professional.

Like any important discussion, this talk may be difficult. The best approach is to take into account who you are speaking with and how you want to present the topic. Every family is different and every talk will be different, but make sure you have it. Please call if you'd like to discuss this in more detail. ❍❍❍

Financial Data

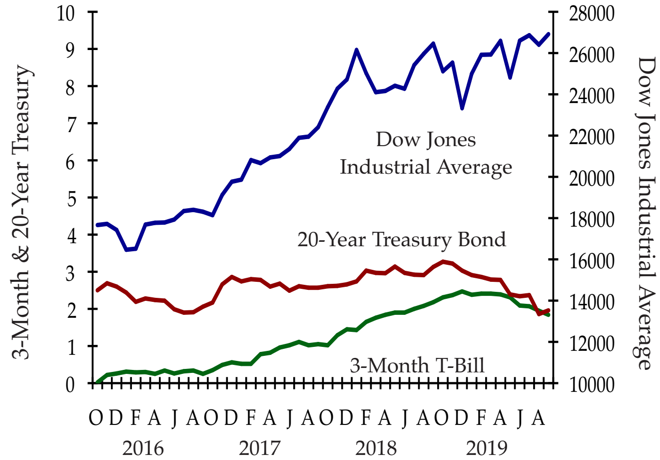
Indicator	Jul-19	Aug-19	Sep-19	Dec-18	Sep-18
	Month-end				
Prime rate	5.50	5.25	5.00	5.50	5.25
Money market rate	0.66	0.72	0.75	0.56	0.47
3-month T-bill yield	2.07	1.95	1.84	2.47	2.18
20-year T-bond yield	2.37	1.86	1.96	3.03	3.13
Dow Jones Corp.	3.21	2.86	2.94	4.40	4.14
30-year fixed mortgage	3.35	2.99	3.89	4.16	4.74
GDP (adj. annual rate)#	+2.20	+3.10	+2.00	+2.20	+4.20

Indicator	Month-end Jul-19	Month-end Aug-19	Month-end Sep-19	% Change YTD	% Change 12-Mon.
Dow Jones Industrials	26864.27	26403.28	26916.83	15.4%	1.7%
Standard & Poor's 500	2980.38	2926.46	2976.74	18.7%	2.2%
Nasdaq Composite	8175.42	7962.88	7999.34	20.6%	-0.6%
Gold	1427.55	1528.40	1485.30	15.9%	25.1%
Consumer price index@	256.14	256.57	256.56	1.8%	1.7%
Unemployment rate@	3.70	3.70	3.70	0.0%	-5.1%

\# — 4th, 1st, 2nd quarter @ — Jun, Jul, Aug Sources: *Barron's, Wall Street Journal*

4-Year Summary of Dow Jones Industrial Average, 3-Month T-Bill & 20-Year Treasury Bond Yield

October 2015 to September 2019



Past performance is not a guarantee of future results.

How Much of Your Portfolio Should Be in Stock?

One of the most often asked questions is how much of a portfolio should consist of stocks. It's a good question, and one that doesn't always have a clear-cut answer. The amount of stock you should have in your portfolio will vary depending upon a number of different factors, including your age, current net worth, and penchant for taking risks. Still, there are a few basic rules of thumb worth adhering to, which should make fleshing out your portfolio less stressful.

If you're saving for retirement, most financial planners will recommend that the younger you are, the more of your portfolio should be allocated to stocks. Stocks are a relatively risky and volatile form of investment. When we're young, taking risks tends to come along with less catastrophic consequences than when we're nearing retirement age. If formulas work for you, the general idea is to subtract your age from the number 100 to wind up with a safe percentage of stocks versus other investments. For example, 30-year-olds will often do well by allotting 70% of their portfolios to stocks, while 60-year-olds may want to reduce this percentage to 40%.

Of course, age is just one factor that influences portfolio allocations, and there are more aspects that need to be taken into consideration. The best way to ensure your portfolio is properly divided is to work with a financial planner who is fully aware of your situation and can make educated suggestions. After all, a formula can only get you so far, and personal recommendations will always be more valuable than guesswork. ❍❍❍

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