Q3 2018 NEWSLETTER

What a Busy Quarter of Travel!

Over the third quarter, there was a real uptick in travel. Ashley was in the Bay Area, Brisbane (Australia), Duluth, MN, Las Vegas NV, and St. Louis, MO!

XYPN Live 2018 and DFA Foundations Conference

Ashley and his associate, Kellen, attended these two conferences in St. Louis, MO, the last week of the quarter. Ashley presented about how credit scores affect clients and some ways to help clients improve their credit scores. The week concluded with a DFA (Dimensional Fund Advisors) conference where Ashley and Kellen learned more about the background of DFA, their investment philosophy, and how DFA funds can be implemented in clients' portfolios.

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2018 Third Quarter Market Report

If you believe that the trend is your friend, then perhaps the U.S. stock market is in for an excellent fourth quarter. U.S. equity markets suffered small losses in the first quarter, followed by decent single-digit gains in the second quarter. Now that the third quarter is in the books, a somewhat larger gain has put stocks in solid positive territory for the year.

The Wilshire 5000 Total Market Index—the broadest measure of U.S. stocks—finished the quarter up 7.27% and has gained 10.68% so far this year. The comparable Russell 3000 index is up 10.57% in calendar 2018. Large cap stocks led the way. The Wilshire U.S. Large Cap index was up 7.68% over the past three months, and has gained 10.50% for the first three quarters of the

Household Level and Portfolio Level Reports Now in Your Vault

We've been busy training ourselves on Morningstar Office and after much testing are pleased to announce that we have uploaded your Q3 reports to your Morningstar portal (note - there are two reports).

Financial Planning Association National Conference

Not long after arriving home from St. Louis, Ashley headed off to Chicago for the 2018 FPA National Conference. At this conference, Ashley presented on the Royal Commission in Australia and made his case for a creating a global community of global professionals. Ashley is looking forward to attending the FPA Conference in Sydney, Australia, later next month.

Upcoming Travel

San Francisco: Oct 24th - 27th
Sydney: Nov 16th - 23rd
Brisbane: Nov 24th - 26th
San Francisco: January 9th - 12th

year, while the Russell 1000 large-cap index stands at a 10.49% gain so far this year. The widely-quoted S&P 500 index of large company stocks gained 7.20% in value during the year's third quarter, rallying to an 8.99% gain so far in 2018. Meanwhile, mid-cap stocks, as measured by the Russell Mid-Cap Index, are up 7.46% in the first nine months of the year. The Wilshire U.S. Small-Cap index posted a 3.65% gain over the third quarter of the year, and now stands up 10.99% so far in 2018.

International stocks are not faring quite so well. The broad-based MSCI EAFE index of companies in developed foreign economies gained just 0.76% in the recent quarter, and is now minus 3.76% for the year. In aggregate, European stocks were up a meager 0.39% over the last three months, posting an overall loss of 4.86% for the year, while MSCI's EAFE's Far East Index gained a slightly more robust 2.23% in the third quarter, losing 1.18% so far in 2018. Emerging market stocks of less developed countries, as represented by the MSCI EAFE EM index, went into negative territory for the quarter, down 2.02%, for a loss of 9.54% for the year.

Looking over the other investment categories, real estate, as measured by the Wilshire U.S. REIT index, gained 0.72% during the year's third quarter, and is just eking out a 2.25% gain for the year. The S&P GSCI index, which measures commodities returns, gained 1.34% in the second quarter, up 11.84% for the year.

In the bond markets, coupon rates on 10-year Treasury bonds have continued an incremental rise to a 3.06% annual coupon rate, while the yields on 30-year government bond yields have risen slightly to 3.21%. But short-term yields are catching up; 3-month Treasury bills are now paying investors 2.20%, and one-year Treasuries yield 2.56% on an unusually flat yield curve. Normally, bond investors have to be paid much more to hold longer-term paper, due to the always-present uncertainties in interest rate movements and other factors.

What's going on? The American economy roared in the second quarter of the year, but most economists believe that the 4.2% GDP growth number was inflated, both by short-term corporate earnings as a result of the tax cuts, and by a short-term effort by multinational companies to complete as much overseas business as possible—including via their manufacturing supply chains—before the widely-publicized tariffs took effect. That suspicion seems to have been confirmed by a variety of new economic statistics. On the jobs front, initial claims for state unemployment benefits rose by 12,000 to a seasonally-adjusted level of 214,000 above expectations. On the manufacturing front, non-defense

capital goods orders excluding aircraft, a proxy for business investment, fell 0.5% in the recent quarter. As a result, Morgan Stanley and Barclay's economists lowered their growth estimates to 2.7% and 2.8% for the third quarter. This is solid but not spectacular growth, a bit above the 2.2% growth rate the U.S. economy has experienced, on average, since mid-2009. Altogether, we may be looking at a year of 3% growth.

But then you have the Federal Reserve Board's recent (and widely anticipated) decision to nudge the Fed Funds rate up to a range of 2-2.25% in September and to raise short-term rates again in December. Higher short-term rates are not necessarily bad for the market, and it is certainly a good sign that Fed economists believe the U.S. market is strong enough not to need additional stimulus. But the Fed seems to be intent on continued raises next year, when the biggest impact of the corporate tax rate reduction will be behind us, and when we enter unknown global trade territory due to the imposition of tariffs on U.S. trade partners. It's never possible to predict the next downturn, but perhaps we can evaluate the impact the unprecedented 25% tariffs on Chinese goods will have on our collective stock portfolios. Tech companies have massive manufacturing operations in China, and China is also a large purchaser of finished tech products from the U.S. You can expect reduced earnings for many tech companies—including Apple, which has signaled that the tariffs will hurt its bottom line, but has so far declined to put a number on the impact. Commodities funds that invest in products that are being hit by retaliatory tariffs—like soybeans—could see a negative impact. And the overall inflation rate will rise by some undetermined amount as many foreign-manufactured products, and things like cars (which have components that are manufactured overseas) become more expensive.

Meanwhile, small cap companies typically buy and sell domestically, so they will be less affected by the new tariff regime—and might even benefit, if foreign competitors are impacted by higher border taxes.

Another interesting question is how investors will be affected by the ballooning U.S. federal deficit. This year, the $21.5 trillion national debt quietly passed the size of the U.S. GDP—or, put another way, it is now greater than the GDP of the next three largest nations combined (that's China, Japan and Germany). The Congressional Budget Office estimates that this debt level will more than triple in the next 30 years, and that by 2028, the debt-to-GDP ratio will be the largest it's been since the end of World War II.

So what? As the U.S. government begins flooding the world with Treasury bonds, they are likely to become cheaper—which means their interest rates will be higher. Higher interest rates are normally associated with lower stock market returns, due to the increased cost of borrowing. Also, consumer debt—credit cards, home mortgages and student loans—becomes more expensive, taking a bite out of disposable income. Disposable income is the fuel that drives GDP growth, in the form of consumer expenditures.

These are all things to ponder, not things that will help you pinpoint the hour and the day when the bull market finally comes to an end. If we knew that time, chances are we would all be selling out before—causing it to happen before the appointed time. All we can do for now is wait and wonder.

The Happiness Equation

As an investor, your happiness depends on having realistic expectations about returns and viewing market events in proper context. These two factors can drive your sense of financial well-being and influence your financial outcome.

To say that "money isn't everything" is more than a cliché. Studies in the early 1970s demonstrated that a sense of well-being, or happiness, had not increased proportionately with income over the previous half century.

That trend continues as the modern world has arguably made well-being more elusive than ever. Fortunately, positive psychology arose in the 1990s, attempting to find the key to understanding what makes people flourish. It has spawned the so-called happiness literature that seeks modern truth by weaving together science and ancient wisdom. How to be happier is now the most popular course at Harvard and Yale.

Business people and entrepreneurs are also contemplating some of these age-old questions. Mo Gawdat, a serial entrepreneur and Chief Business Officer at Google X, tried to engineer a path to joy in his book, Solve for Happy, by expressing happiness as an equation.

HAPPINESS ≥ Your Perception of the EVENTS of your life – Your EXPECTATIONS of how life should behave.

According to Gawdat's model, if you perceive events as equal to or greater than your expectations, then you're happy—or at least not unhappy.

Investors wanting to increase their wealth and well-being should consider his model. You can't control many events that affect your portfolio, but events themselves are not part of the equation. Fortunately, you have some control over the two variables driving happiness—your perception of the events and your expectations.

EXPECTATIONS

First, let's review some fundamentals about expectations in the financial markets.

1. Stocks have higher expected returns than safer investments like Treasury bills.

If it is widely known that stocks are riskier, prices should reflect that information, and, for the market to clear, investors are incentivized to bear that risk with higher expected returns. The higher expected return for stocks is known as the equity premium and, historically, it has been about 8% annually in the US.

Therefore, expected returns are a function of the price you pay and cash flows you expect to receive. Companies that are smaller and more profitable, with lower relative prices, have higher expected returns than those that are larger and less profitable, with high relative prices. These patterns are referred to as size, profitability, and value premiums. They have historically ranged from slightly more than 3.5% to just under 5% in the US.

2. All stocks don't have the same expected return.

The price of a good and service is set by market forces and results from many inputs, such as the costs of raw materials, labor, shipping, and advertising, as well as competition and perceived value. As a consumer, you don't need to understand all the inputs to make an informed purchase. You look at the price relative to alternatives in the market and ask if the product is worth the price—and the lower the price or the more you get, either in quality or quantity, the better the purchase.

Similarly, a stock's price has many inputs. Expectations about future profits, different types of risk, and investor preferences are just a few examples, but you don't need a model to understand all those inputs or how they impact market prices. All available information should already be reflected in the price, which tells you something about expected returns. Whether you are a consumer or an investor, you want to pay less and receive more.

3. Expected premiums are positive but not guaranteed.

Although expected premiums are always positive, realized premiums may be positive in some years and negative in others. You may even experience a negative premium for several years in a row. The probability of earning a positive premium also increases with your time horizon, but it isn't a sure thing since underperformance is possible over any time frame. Nobel laureate Paul Samuelson said, "In competitive markets there is a buyer for every seller. If one could be sure that a price will rise, it would have already risen."

PERCEPTION

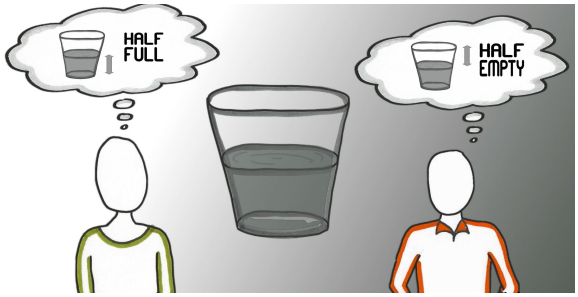
The other half of the equation is your perception of an event.

Consider an event, such as realizing a negative premium over 10 years, a time frame that some investors consider long term. This is not just a hypothetical exercise because the cumulative value premium has been negative for the past 10 years in the US, while the market and size premiums were negative in the 10-year periods ending in 2009 and 1999, respectively.

Lengthy periods of underperformance are disappointing, as investors obviously prefer higher rather than lower returns. Nonetheless, disappointment shouldn't turn into anger or regret if you know in advance that periods like these will occur and recognize you can't predict them. Ancient wisdom teaches acceptance, as resistance often fuels anxiety. Instead of resisting periods of underperformance, which might cause you to abandon a well-designed investment plan, try to lean into the outcome. Embrace it by considering that if positive premiums were absolutely certain, even over periods of 10 years or longer, you shouldn't expect those premiums to materialize going forward. Why is this? Because in a well-functioning capital market, competition would drive down expected returns to the levels of other low-risk investments, such as short-term Treasury bills. Risk and return are related.

The good news is there are sensible and empirically sound ways to increase expected returns. The bad news is there will be periods of underperformance along the way.

Your happiness as an investor depends on how your perception of events stacks up against your expectations. Proper expectations alongside the appropriate perception can help you stay the course and may improve your wealth and well-being. As David Booth, Executive Chairman and Founder of Dimensional Fund Advisors, says, "The most important thing about an investment philosophy is having one you can stick with."



September 2018 | Brad Steiman, Dimensional Fund Advisors

The Uneven Recovery of Americans after the Great Recession

One of the consistent themes we've been hearing in the political arena is that the economy and stock markets are doing very well, and that we've finally recovered from the Great Recession. But recovery to market highs and the personal recovery from the losses experienced during the downturn can be very different things. A recent survey by the Joint Center for Housing Studies at Harvard University has taken a look at how different groups of Americans weathered the storm, and whether they've recovered their former wealth.

The study is broken down into several areas. Using broad statistics, real (after inflation) housing prices were down 9% in 2016 from where they had been in 2006—a real and persistent decline in wealth for many Americans. Foreclosure activity, meanwhile, had the smallest impact on retired households, whose rate of home ownership fell modestly from 81% in 2004 to 79% in 2017. Among households aged 55 to 64, however, the homeownership rate dropped from 82% in 2004 down to 75% in 2017—meaning that a significant number of people are going to reach retirement age with zero or very little home equity. In addition, the study found that volatile rental costs were taking a toll on people

who didn't own their homes; more than 47% of renters were paying more than 30% of their incomes for housing.

Of course, the stock market has roared back, and those gains are reflected in IRA accounts. Traditional IRAs held $6.9 trillion at the end of 2016, up from $4.2 trillion at the end of 2007. However, those gains didn't make it all the way down to the bottom two-thirds of all earners; the top third owned 87% of all equities in 2016. For middle-income Americans, account values were stagnant or slightly down, despite the strong market gains, and just 11% of the lowest-income families had any retirement account at all. The market boom meant little to them.

The big picture painted by the research tells us that ten years after the collapse of Lehman Brothers, those who were already affluent have recovered just fine from the Great Recession and stock market decline. Middle and lower-class households did not, and face a very uncertain retirement.

Source:

https://www.reuters.com/article/us-column-miller-retirement/ten-years-after-onset-of-great-recession-how-are-u-s-retirees-doing-idUSKCN1M7165

The New Manufacturing

We hear about how artificial intelligence is going to change the workforce, and how computers are taking over the world. But perhaps the biggest shift in our industrial lives has been flying under the radar: rather than making things, we will soon be "printing" them.

A new "metal printing press" developed by Desktop Metal, uses a variety of metal powders to lay down many thin layers of material in rapid succession, according to the specifications in a digital file, to build three-dimensional objects. It employs more than 32,000 juts in conjunction with powder spreaders to jet millions of droplets per second, creating metal parts in minutes instead of hours. The one-million-dollar printing device is designed to replace metal fabrication activities, many of which are currently handled by hand. Among the early customers: Ford, Caterpillar and Google's advanced technology and project group. BMW has tested a steel prototype of a water impeller pump that costs $80 to make currently. It can be 3D "printed" for just over $5, and the printed version is 50% lighter.

The goal is to have a "factory" of 3D metal printing units that can print parts and products on demand, with no minimum order size. The parts will be lighter, cheaper and more efficient than what could have been fabricated in the past. One analyst is forecasting that sales of industrial 3D printers could reach $18 billion by 2021.

Source:
https://www.forbes.com/sites/amyfeldman/2018/09/27/the-next-industrial-revolution-how-a-tech-unicorns-3-d-metal-printers-could-remake-manufacturing/?utm

The Tao of Wealth Management

The path to success in many areas of life is paved with continual hard work, intense activity, and a day-to-day focus on results. However, for many investors who adopt this approach to managing their wealth, that can be turned upside down.

The Chinese philosophy of Taoism has a phrase for this: "wei wu-wei." In English, this translates as "do without doing." It means that in some areas of life, such as investing, greater activity does not necessarily translate into better results.

In Taoism, students are taught to let go of things they cannot control. To use an analogy, when you plant a tree, you choose a sunny spot with good soil and water. Apart from regular pruning, you let the tree grow.

This doesn't mean that we should always do nothing. In fact, insights from financial science suggest you should direct your investment efforts to the things you can control. These include taking account of your own preferences and sensitivities when choosing investment strategies, diversifying your allocation to moderate the ups and downs, being mindful of the impact of fees, and exercising discipline when emotions threaten to blow you off course.

Successful investing requires taking actions that can have a positive impact on the outcome. For instance, to maintain their desired asset allocation, investors should regularly rebalance their portfolio by reallocating money away from strongly performing assets.

But rebalancing is a disciplined, premeditated activity based on each person's circumstances. It contrasts with the "busyness" of reflexively following investment trends and chasing past returns promoted through financial media. Look at the person who fitfully watches business TV or who sits up at night researching stock tips. That sort of activity is likely counter-productive and can add cost without any associated benefit. With investing, constantly tinkering with an allocation does not perfectly correlate with success.

Now, while that makes sense, many people struggle to apply those principles because the media tends to look at investing through a different lens, focusing on today's news, which is already priced in, or on speculating about tomorrow. Guesswork can surely be interesting. But is it relevant to your long-term plan? Probably not.

People caught up in the day-to-day may constantly switch money managers based on past performance, or attempt tactical changes in their allocation, or respond in a knee-jerk way to news events that turn out to be noise.

Again, the assumption underlying these approaches is that if you put more effort into the external factors and adjust your position constantly, you will get better results. Unfortunately, people may end up earning poorer long-term returns from trading too much, chasing past performers, or attempting to time the market. Ultimately, that's just another reminder of the potential benefits available to disciplined investors who stay focused on what they can control. As the ancient Chinese proverb says: "By letting it go, it all gets done. The world is won by those who let it go. But when you try and try, the world is beyond the winning."

July 2018 | Jim Parker, DFA Australia Limited, a subsidiary of Dimensional Fund Advisors LP

What High-Achieving People Have Learned to Give Up

High-achieving people will tell you that they sacrificed to get where they are, but what, exactly, did they sacrifice? An article in Forbes magazine lists 18 things that high-achieving people routinely give up—and many of them are not what you would expect.

Number one on the list: a fear of uncertainty. The article notes that there really are no guarantees in life, so when you start a new business, you aren't really giving up certainty for the reckless unknown. You're giving up one kind of uncertainty for another—and the old one, which feels more certain, may be holding you back.

Two: *Ignoring your feelings*. Your feelings actually give you a lot of clues about your situation. Anger tells you where you feel powerless. Anxiety tells you when something in your life is off-balance. Fear tells you what you care about. If you treat your feelings as messengers, you might learn what you need to do next to move ahead.

Three: *Pretending your problems don't exist.* The advice: make a spreadsheet of your debt, and list the habits you now are detrimental to your health. Think of who you owe apologies to and address your problems rather than sticking your head in the sand.

Four: *Avoiding discomfort*. This is kind of like number one: if you build your life around just the things that make you feel at ease, that is a fast track to complacency.

Five: *Your unhealthy habits*. Identify your worst habits and work on them, so you have a sound basis of health to build your life on.

Six: *A victim mentality*. Whatever your back story, don't let it define your life. Don't let your current circumstances do so either. What will make the difference is what you choose to do in response to them. Everybody struggles, but some are willing to act in spite of it.

Seven: *Excuses*. Justifying failure tends to leads to more of it. In life, you either do or you don't, and the don't option often, when looked at objectively, means wasting time. Your excuses make you feel better about why you aren't doing what you know you need to do.

Eight: *Learned helplessness*. When you face many challenges, it makes you feel powerless in your fight against the world.

Nine: *Defending your problems*. You will often get advice on how to address a problem you've been complaining about. Do you consider it, or respond with an excuse for why it would never work? Defend your potential, not your problems.
Ten: *Distractions*. Everything that isn't helping you move forward is a distraction.
Eleven: *The need to be liked.* Recognize that nobody is universally liked, for reasons that have nothing to do with you. There are a few people who won't like you no matter what, and any energy spent trying to change that is taking away from more productive activities.
Twelve: *Trying to do everything yourself*. Nobody can take on every role, job and responsibility in your life. High-achieving people hire the right people, surround themselves with experts and rely on others. Refusing to rely on others wastes your energy.
Thirteen: *Resistance*. This is the normal response to stepping out of your comfort zone, but if you experience resistance to work, then something needs to be addressed. Too much hesitation may mean you aren't on the right path.
Fourteen: *Quick fixes and shortcuts*. Whatever you are building won't get built overnight, and you shouldn't expect it to. Real change happens gradually. Try to do everything 1% better each day, and over time the effort will compound.
Fifteen: *The fear of failure*. This can hold you back in many ways; it makes you unwilling to take chances, or change your circumstances, or avoid learning opportunities and experiments that might prove useful.
Sixteen: *Waiting until you "feel like it" to get started.* Motivation isn't something you wait for; you know you need to work through late nights and difficult days. High achieving people need strong principles and habits.
Seventeen: *Envying those who have what you want.* Envy will hinder you from getting those things yourself. The more you judge others, the more you put yourself in a box.
Eighteen: *Waiting for your circumstances to change before you do.* If you wait for a new relationship, or a new opportunity, or some change in life, then you might find yourself waiting forever. Life unfolds from the inside out, when we change our circumstances through focused effort.

Source:
https://www.forbes.com/sites/briannawiest/2018/03/20/18-things-you-need-to-give-up-to-become-a-high-achieving-person/#486237de11fa

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