The Thoughtful Investor™

Active Investment Strategies Help Real People

Recently, it seems there's no shortage of buy-and-hold investment advice from mutual funds, news media and financial pundits. In fact, the advice usually begins by berating individuals for failing to buy and hold and then moves on to show how holding an index fund for 20, 30 or 50 years outperformed the average investor. The problem with this advice is that market risk is very real. The S&P 500 index took 13 years to regain its high in 2000. That's a long time to live with the memory that you no longer feel financially secure. The market decline in 2008 added to the insecurity of investors and the feeling that they had little if any control over their investments.

For real people, losses hurt. In fact, studies show that losses hurt a lot more than the joy one might get from making money. When your account is down 25% or much worse 50%, it isn't a theoretical loss. The loss may be three or more years of your net salary,

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The Over-65 Crowd Returns to the Workplace

Despite an official unemployment rate of 5.5%, virtually every age cohort's participation in the labor market has declined. Not so for the over-65 bracket. Their participation in the labor force has actually increased to the highest level since the Federal

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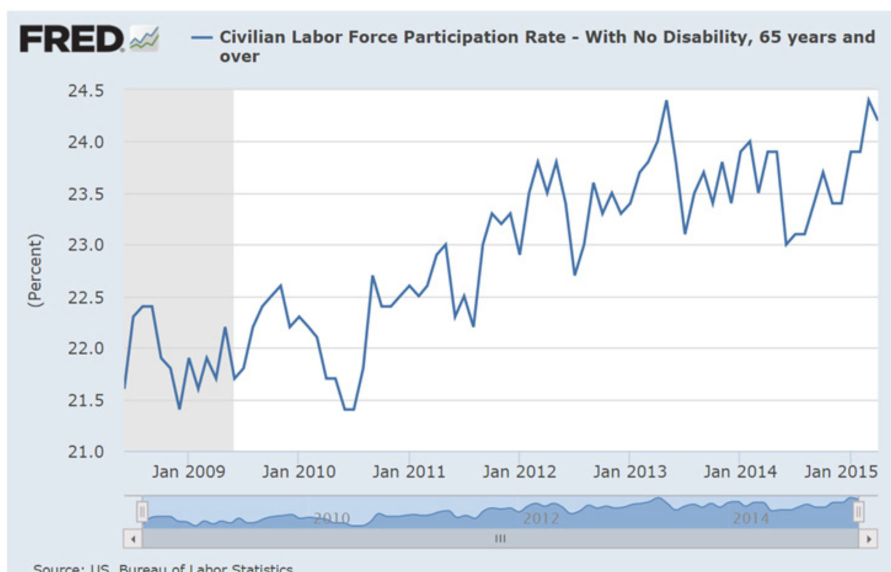

https://research.stlouisfed.org/fred2/categories/32443

Financial Advice for the Kids – Get Married

Choices are central to whether or not we achieve financial success. Among those choices are whether to get married and finding the right partner for a lifelong relationship. Couples who get and stay married can have as much as four times the wealth of their single or divorced peers.[1] Part of the reason may be who is getting married. More educated, more affluent individuals with strong value systems appear to be most likely to get married.

Once they are married, they take advantage of economies of scale and benefits such as employer-provided health insurance, but the positives tend to go beyond that to developing a working partnership. The development of a committed partnership may explain why married couples tend to financially outperform those living together, where the commitment to their success as a couple may be less.

In 2002, two European economists calculated the monetary worth of marriage at $100,000 per year. And then there's the happiness bonus. Psychologists point to marriage as the single most reliable happiness indicator. The counter balancing question is whether or not marriage is the determining factor or whether individuals who are more inclined toward wealth and happiness to begin with are also more inclined to marriage.

1 Why married people tend to be wealthier: It's complicated. By Alison Linn, TODAY Money, Feb. 13, 2013.

Which Numbers Matter?

One of the easiest ways to calculate the return on a portfolio over time is *average annual return*. All one has to do is add the return for each year and divide the total by the number of years. There's just one problem – **the resulting number is meaningless if there are negative years in the calculation.** And, it is used all too often to demonstrate portfolio performance.

The problem with using average annual return is what financial author Hans Wagner has called "The dark side of compounding." Wagner explains, "In the final analysis, one cannot spend average returns, one can only spend compounded returns."

It comes down to the math of gains and losses. In the table to the right, the annual return of the S&P 500 including dividends is shown for the 15-year period ending December 31, 2014. Calculating a simple average return for the 15 years results in 11.43%. The actual annualized return was 4.25%. That's a huge difference.

Where the calculation of average annual return goes awry is the failure to consider the cost of getting back to break even. When a portfolio loses 37%, such as the S&P 500 did in 2008, it doesn't take a 37% gain to recover. It takes a 59% gain because you are starting from a much smaller base. At the end of 2008, a $100,000 portfolio was down to $63,000. To recover to $100,000 it had to gain $37,000, or 59% of $63,000.

It's easy to regard numbers as solid facts. But misleading with numbers can be painfully easy. When you compare investment returns, make certain you are looking at compounded returns, not averages.

S&P 500 Annual Return/Growth of $100,000

Year	Total Annual Return Including Dividends	Growth of $100,000 at 11.43% annual return	Actual growth of $100,000
2000	−9.10%	$ 111,430	$ 90,900
2001	−11.89%	$ 124,166	$ 80,092
2002	−22.10%	$ 138,359	$ 62,392
2003	28.68%	$ 154,173	$ 80,286
2004	10.88%	$ 171,795	$ 89,021
2005	4.91%	$ 191,431	$ 93,392
2006	15.79%	$ 213,312	$ 108,138
2007	5.49%	$ 237,693	$ 114,075
2008	−37.00%	$ 264,862	$ 71,867
2009	26.46%	$ 295,135	$ 90,883
2010	15.06%	$ 328,869	$ 104,570
2011	2.11%	$ 366,459	$ 106,777
2012	16.00%	$ 408,345	$ 123,861
2013	32.39%	$ 455,019	$ 163,980
2014	13.69%	$ 507,028	$ 186,428
Average annual return	**11.43%**	**Actual compounded annual return**	**4.25%**

The S&P 500 is an unmanaged, capitalization-weighted index that tracks the performance of 500 large-cap companies and is widely used as a proxy for the U.S. stock market. The S&P 500 is an index and cannot be invested in directly.

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or 10 years of savings. Yes, so far the market has always recovered over time, but there's never a guarantee that the next recovery will happen fast enough, or for that matter happen at all.

Uncertainty is the greatest hazard of investing. 2014 was a good year for equities. 2015 is looking a lot shakier and there are plenty of predictions that the market is headed for a fall whether from rising interest rates, economic doldrums or political uncertainty. At the same time, history tells us that the 3rd year of president's term is best for stocks.

Active investment strategies that strive to limit losses when the market turns down are designed for real people. Who do we consider a "real person"? It's the person who buys fire insurance; the family who saves for emergencies and for retirement because they don't want to be at the mercy of fate. Real people realize that bad things can happen and they don't want to have their lives destroyed by an event beyond their control. Real people work to add some measure of risk management to their lives. Leaving their life savings to the mercy of the market is not risk management.

When active management can remove at least some of the uncertainty that comes with investing by having a carefully designed strategy for moving in and out of the financial markets in response to perceived risk and opportunity, it helps people stay invested for the long term. And that is the most important element of successful investing. Investors have a very good reason to be scared onto the sidelines by bear markets. But they have to have a plan to get out early in the decline and back into the market, or back into investments with more upside opportunity, when the correction is over.

Our firm was founded based on the belief that recognizing and managing risk is the smart way to invest. We have invested years in studying the financial markets through technical analysis; looking for clues that tell us when risk is greater than the perceived return we might achieve by staying in the market. Is our system perfect? No. Will it outperform a buy and hold investment in an index? Rarely in rising markets. But can it provide investors with a better long-term return? We believe the answer will prove to be yes over the investment lives of our clients. In part, this will be the result of the mathematics of gains and losses. Any time an investment approach limits losses, the

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The Best Financial Advice

Hanging on the wall is a quote from author Jack London – *"You can't wait for inspiration. You have to go after it with a club."* It's there because a daily reminder can be invaluable when it comes to keeping on track. With that in mind, we offer the following memorable words of financial advice. If there is one or more that particularly fit your situation, turn each into a sign and hang it where it provides a daily reminder.

(1) On Saving

- Pay yourself first.
- If you save really hard for 10 to 15 years, it's possible you will never have to work again.
- Save half. Structure your life so that you can save half of your income.
- Don't save what is left after spending; spend what is left after saving.
- Save early and save often.
- Don't pass up free money. If your employer is matching your retirement contributions, participate.

(2) Avoid Debt

- Borrowing money is like wetting your bed in the middle of the night. At first all you feel is warmth and release. But very, very quickly comes the awful, cold discomfort of reality. *Elizabeth Gilbert*
- Pay off your debt first. Freedom from debt is worth more than any amount you can earn. *Mark Cuban*
- There's good debt and bad debt. Bad debt is debt you have to pay for and makes you poor. Good debt makes you rich and someone else pays for it. *Robert T. Kiyosaki*
- All debt becomes bad debt when you don't have the cash to pay it back.

(3) Persistence

- Slow and steady wins the race, and consistency matters. Get-rich-quick never wins.
- Should you find yourself in a chronically leaking boat, energy devoted to changing vessels is likely to be more productive than energy devoted to patching leaks. *Warren Buffett*
- Know why you are invested in a particular asset. As long as the reason remains valid, so does the position.

(4) Investing

- Don't buy a financial product that you don't understand and don't buy it from a person who can't explain it so that you can understand it. *Sallie Krawcheck*
- Defense is ten times more important than offense. If you lose 50%, it takes 100% to get back to where you started — and that takes something you can never get back: time. *Paul Tudor Jones*
- Everyone has the responsibility to know what they are investing in. *Alexandra Lebenthal*
- Be straightforward, upfront and honest. Don't play games with people's finances. *Hal Steinbrenner*
- Finance is never, ever, a theoretical exercise; you're never half as detached from portfolio losses as you think you will be. *William Bernstein*
- Step away from the television and the magazines. All they serve to do is show you how stupid you are because you've missed whatever they're talking about. It's old news. It's already happened. *Neale S. Godfrey*

(5) Know Your Value

- Business and money don't breed warm feelings. Ninety-five percent of what people say about you is going to be negative. And remember, that means that you are doing a good job. *Scott Boras*
- Don't ever give up your ability to make your own money. *Michelle Smith*
- Price yourself high and see what happens. *Scott Adams*
- I just keep raising my rates until someone says no.
- Always ask. Make it a priority to always ask and always negotiate. *Stephanie Halligan*

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investor gains leverage to profit from rising markets.

The chart below was taken from a presentation by Greg Morris, former mutual fund executive, technical analyst, consultant and author of prominent active management books, including his latest, *Investing with the Trend*. Which portfolio would you be more comfortable owning?

	Investment Option A	Investment Option B
Year 1	+10%	+36%
Year 2	+6%	+8%
Year 3	+8%	-20%
Growth of $100	$126	$117
Compounded Annual Return	+8%	+5.4%

Naturally there can be no guarantee that results of a client's investment account would look like this or that active management will meet its goal of minimizing losses and participating in the majority of the market's up move. All investing has the potential for loss as well as gain. But we sleep much better at night knowing that we have a plan in place with the potential to manage the risk of investing.

The Over-65 Crowd Returns to the Workplace— *continued from page 1*

Reserve began to track the data in June of 2008. What's happening?

According to surveys by AARP and other experts, the primary economic force behind the return to work is *the growing fear among older Americans that they lack the means to support their retirement needs*.

With the shift away from company pensions to 401(k) plans and other personal savings for retirement income, individuals took on the responsibility of financing their retirements. Even those who thought they had adequate savings had their confidence rattled and account balances impacted by market declines in 2000-2002 and 2008. Near zero returns on bank deposits haven't helped retirees, either. Frank Barbera, CMT, of Sierra Investment Management, Inc., maintains the current Zero Interest Rate Policy has resulted in a $7 trillion transfer from individual savings to the banks since 2001, taking discretionary spending out of the economy along with it.

The result is that millions of Americans are rejoining the work force or staying in it longer than they might have intended. According to the Federal Reserve's 2014 Survey of Household Economics and Decisionmaking, 31% of non-retirees have no retirement savings or pension, including nearly a quarter of those older than 45. While the intent to keep working is higher among lower-income respondents, even in the higher-income brackets, the Fed's data show an inclination to keep working in retirement. Only 28% of individuals with a household income greater than $100,000 indicated they intend to stop working altogether.

On the positive side, there is clearly a market for experienced workers. With increased longevity and less physically taxing careers, the new retirement may include work if simply to keep one busy. But for those looking forward to the traditional retirement in their early to mid 60s, the importance of saving now cannot be overstated. Otherwise, the shift in retirement financing, combined with the slow economy, may reshape how you ride out the latter part of your life.

If you are concerned that you may not be ready for retirement, give our offices a call and let's talk about where you are today and where you would like to be, or need to be, to retire.

Which of the following best describes your plans for retirement (by household income)

	Less than $40,000	$40,000 - $100,000	Greater than $100,000	Overall
I do not plan to retire	17.0%	1.3%	7.5%	11.5%
Work fewer hours as I get close to retirement	9.4	10.4	7.6	9.3
Retire from my current career, but then find a different full-time job	2.5	2.5	3.0	2.6
Retire from my current career, but then find a different part-time job	8.6	12.2	15.8	12.5
Retire from my current career, but then work for myself	4.9	7.6	11.3	8.1
Work full-time until I retire then stop working altogether	11.2	23.1	28.1	21.6
Keep working as long as possible	37.8	24.6	19.9	26.5
Other	7.2	6.4	5.3	6.3
Total number of respondents – 3894 Among respondents who are not currently retired or out of work due to a disability.				

SOURCE: Table 18: Federal Reserve's 2014 Survey of Household Economics and Decisionmaking