| DJ IA | Nasdaq | S & P 500 | Russell 2000 | MSCI EAFE | Crude Oil | Euro | 10 yr Treas. | Fed.Fund Rate | Prime Rate |
|---|---|---|---|---|---|---|---|---|---|
| 23327.46 | 6635.28 | 2506.85 | 1348.56 | 7048.07 | 45.41 | 0.8722 | 2.69 | 2.25-2.50 | 5.50 |

# Money Manager Newsletter

**December 31, 2018**

## Investment Consulting Group, Inc.

**"If You Spend 15 Minutes Studying The Economy, That Is 10 Minutes Too Much"**
**U.S. Investor Peter Lynch**

It has been a good year for the economy, with strong job growth, accelerating pay increases, and tame inflation. Will 2019 bring more of the same, something better, or something much worse? The likeliest scenario is muddling through. While growth in the past year has been strong, it is also probably temporary. Tax changes passed at the end of the 2017 boosted household incomes at the same time the government ramped up military spending. The economy could also go into a recession. There are plenty of warning signs from the financial markets. Bank share prices have been hammered. Credit spreads, particularly on the lowest-rated corporate bonds, have widened dramatically. A negative spread implies the Fed will soon be lowering interest. Matthew C. Klein — The Economy

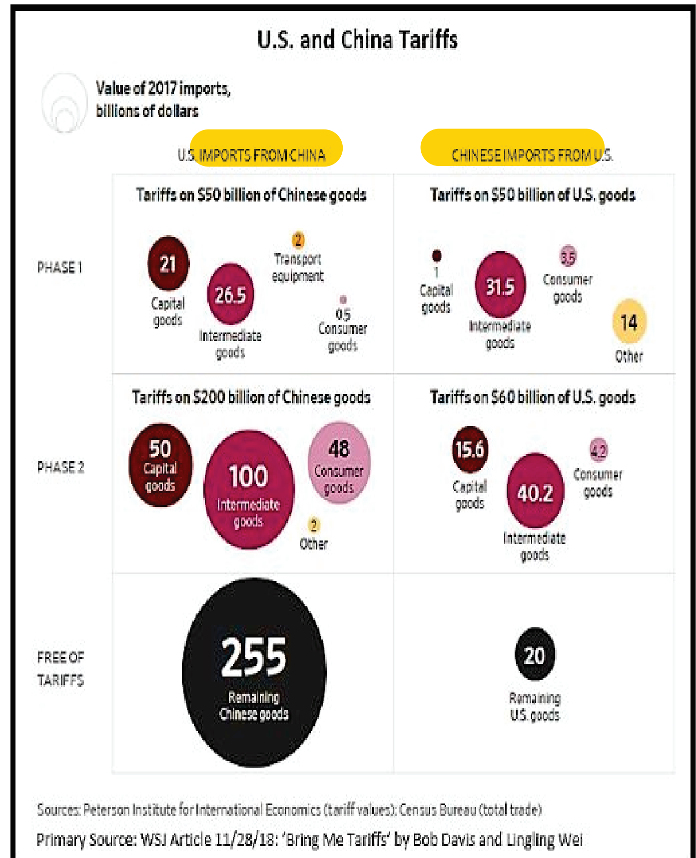
### Vicious Generational Smear

A new report from the Federal Reserve finds that people born between 1981 and 1997 are not the free wheeling, globetrotting, financially wasteful millennials that their elders have smeared them as. Realistically, millennials aged 30 to 34 have annual expenditures almost exactly on par with those born between 1965 and 1980. No, the Fed said, the reason millennials are so broke is because most came of age in a recession they did not cause and they are being paid less in real terms than their elders. The average full-time labor earnings of a millennial male was over 10 percent lower than the comparable baby boomer's in 1978, and the median labor earnings of women household heads were 3 percent lower than those comparable Gen X households in 1998. Jeremy Herron and Luke Kawa, Bloomberg, and Christopher Kurz, Geng Li, and Daniel J. Vine — Federal Reserve Board

Down markets concern me, too, but not nearly so much as it concerns others and hundreds of thousands of others who're reluctant to review the recent carnage and concede the reification of their portfolios. It doesn't concern me as much because our philosophies are as different as cheese and chalk. I don't stress capital gains because I can't spend them unless I see something, because they're difficult to predict and because they're often fleeting. I don't value my portfolio the way most investors do. Most investors measure gains as a percentage of their cost basis, hoping to grow wealth via capital gains. That's the old fashioned way. My definition of wealth is "how much money you can spend while leaving your capital alone and maintaining enough funds for important life events." We don't spend wealth; we spend the income that wealth produces. So the best measure of investing success is the income your portfolio earns. An investor with a $3 million portfolio generating $70,000 in income is less successful than an investor with a $2 million portfolio generating $100,000 in income. When the Dow Jones industrial average becomes a wrecking ball, the latter's stress level doesn't provoke the needle as much as the former's. There are hundreds of good stocks that have attractive records of annual dividend increases. Malcolm Berko

In my nearly 50 years of experience in Wall Street, I've found that I know less and less about what the stock market is going to do, but I know more and more about what investors ought to do; and that's a pretty vital change in attitude. Benjamin Graham

| 12/31/2018 | Growth Median P/E | Historical Growth Avg. | Value Median P/E | Historical Value Avg. |
|---|---|---|---|---|
| Royal Blues | 33.5x | 24.9x | 14.5x | 11.6x |
| Large Cap | 21.4x | 20.0x | 11.7x | 10.9x |
| Mid Cap | 28.9x | 23.7x | 12.1x | 12.1x |
| Sm Cap | 30.7x | 27.7x | 12.6x | 12.1x |




### Apps

Many of your apps are selling you out, A New York Times investigation has found. The location data from 200 million mobile devices can lead to 14,000 new generated location data points in a single day—one woman who movements were tracked found 8,600 location readings over four month, or roughly one every 21 minutes. Location targeted advertising is a $21 billion business, and at least 75 companies are voraciously interested in turning your location at any given moment into money. It may be a good time to figure out which seemingly innocuous apps you've allowed to access your location.
Jennifer Valentino-DeVries, Natasha Singer, Michael H. Keller and Aaron Krolik — The New York Times

Misery has prevailed throughout most of 2018 and all of the fourth quarter. Not since Richard Nixon was President has it been so hard to make money for clients; the breadth of negative returns across investment strategies and asset classes is at historical extremes. Of 102 Morningstar fund categories, only short-term bonds/loans, municipals and one economic sector, utilities, have earned positive returns year to date. In the context of a strong U.S. economy, tame inflation, low interest rates and record corporate earnings, this outcome is perplexing to say the least. Bill Parcells—Boston Partners

### Challenges to International Investing

United States accounts for roughly only 25 percent of global gross domestic product (GPD), down from about 40 percent in 1960. The United States is overrepresented in the capital markets. In other words, U.S. companies have twice the weight in global equity markets than the U.S. economy has in the global economy. Investors constructive on overseas investing suggest that the rest of the world may catch up, developing market structures conducive to increased equity investment. Skeptics, including important figures such as Warren Buffett, suggest that the overrepresentation signifies structural advantages to U.S. companies and markets that should be respected. The U.S. economy is less globalized than most of the rest of the world; non-U.S. companies have an even higher percentage of revenue coming from outside their borders. More than 70 percent of the revenues from FTSE 100 companies come from outside the United Kingdom. Investors often use equity investments in a country to benefit from economic growth in that country. Even within the United States, investors are reminded that they "invest in S&P, not GDP," re-emphasizing that it is ultimately company performance that drives investment results. One frustration of international investing is the modest connection between economic growth and stock market returns. It is intuitive, but wrong, that countries with higher economic growth rates should have greater stock market returns. Yet, very often the risks inherent in international investing come from country specific macroeconomic causes; examples include Greece (systemic debt), Venezuela (poor economic policy), United Kingdom (Brexit), etc. The biggest challenge to active investment managers with international mandates, and especially with emerging market ones, is almost certainly the increasing importance of China. Chinese stocks now make up more than 30 percent of that index. It is estimated that 234 companies were included in the index at their full market capitalization weight, the total weight to Chinese companies in the MSCI Emerging Markets Index would grow to more than 40 percent. Should either South Korea or Taiwan be promoted to developed-market status, that figure would jump to 50 percent.
Matthew Peterson — Investments & Wealth Monitor

### Move Beyond Popular TDFs

Blaine Aiken lays out the "Big 3" reasons fiduciaries have found themselves in court: 1) inappropriate investment options, 2) excessive fees, 3) self-dealing. There's another Big 3 in target-date funds that point to a different breach of the duty of care. Intermediaries, namely some-consultants, have powerful self-interests that are not in line with beneficiary self-interests (it's the easy way). A recent Mass Mutual Retirement Savings Risk Study reports that beneficiaries want to be protected near retirement, but the Big 3 TDF providers (Vanguard, Fidelity and T. Rowe Price) are about 55% in equities at the target date, an exposure that lost more than 25% in 2008, and risk has increased since. Advisers have created a Big 3 TDF oligopoly because their self-interests are to 1) keep the account and 2) avoid litigation. The Big 3 own 65% of the $2 trillion TDF industry. Fiduciaries are duty-bound to seek the best, so it's a breach of the duty of care when they choose on the basis of popularity. This breach is ironic because the Big 3 are viewed as procedurally prudent since procedural prudence is mostly about common practices. The belief is that they're safest for avoiding lawsuits, but the fact is there are other TDFs demonstrably more prudent and more in line with beneficiary best interests. Will the Big 3 TDFs get you into court? The next
market correction could provide the answer.
Ron Surz, President — Target Date Solutions.

### Confusion and Target-Date Funds

Target-Date Funds have become increasingly popular in many 401(k)-type plans. From defined contribution plans to 457s to 401(k)s to 403(b)s, it is the fund "du jure" for most professionals. With so much money being transferred into these assets, the question is whether or not plan participants actually understand what they're getting themselves into from an investment perspective.
A recent study completed by fund company AllianceBernstein attempted to answer some of these questions. Asking 6 questions of participants that acknowledged investing in these types of funds, they attempted to ascertain their competence in their chosen strategy. In our opinion, here are their responses starting from best to worst:

**Target-date funds become more conservative as you get closer to retirement:**
True: 72%
False: 13%
I don't know: 15%

**At retirement, target-date funds are invested in an appropriate mix of stocks and bonds:**
True: 70%
False: 15%
I don't know: 15%

**If you invest in target-date funds, your account balance is guaranteed to never go down:**
True: 38%
False: 44%
I don't know: 18%

**Target-date funds guarantee that you will meet your income needs in retirement:**
True: 48%
False: 37%
I don't know: 15%

**At retirement, target-date funds are invested 100% in cash:**
True: 38%
False: 35%
I don't know: 27%

**Target-date funds are insured by the federal government, like bank accounts:**
True: 45%
False: 33%
I don't know: 22%

The fact that 45% of the investors believed their accounts were insured against loss by the federal government shows a complete failing of the education around these strategies. In 2008 most 2010 target-date funds lost well over 20%. The sticker-shock from such a loss so close to retirement could be devastating.
Based on an article from Investment News by Warren Cormier from 12/1/2018

| Treasury Market Yields | 12/31/2018 | 12/31/2017 | 12/31/2016 |
|---|---|---|---|
| 2 Year | 2.48% | 1.89% | 1.20% |
| 5 Year | 2.51% | 2.20% | 1.93% |
| 10 Year | 2.69% | 2.40% | 2.45% |
| 30 Year | 3.02% | 2.74% | 3.06% |
| SP 500 | 2.15% | 1.89% | 2.07% |
| **Commodities** | | | |
| Oil ($bal) | $45.41 | $60.42 | $37.04 |
| Gold ($/oz.) | $1278.30 | $1306.30 | $1060.30 |
| CRB Index | $169.80 | $193.86 | $176.27 |