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Sound Mind Investing®

Financial Wisdom for Living Well

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A Work-Life, Well Spent

Many books have been written about how to handle finances, but few go beyond the nuts and bolts of managing money and making more money. Yet when families weigh how their money can best be used, they need an eternal perspective. In this article, Russ Crosson helps us reach a balance between prosperity (the accumulation of goods on this earth) and posterity (the heritage we leave our children and the generations that come after us). —AP

by Russ Crosson

When the boys were young, I walked into the house late from work one Thursday night. I could tell by the look on Julie's face she was not happy. My mind raced back through the prior two weeks. I had missed dinner the past three nights due to some projects at work, but I couldn't see how that would have caused her frustration. I had told her I would have some late days during that week, so she should have been expecting it. But as my eyes caught hers, she quickly began to explain how it appeared that I was never home for dinner, and the children were, as she said, "growing up without me." I was incredulous, but as we sat down on the couch and began to talk, the reason for her frustration became clear.

Over the previous two weeks I had been gone at night, not only for work-related projects, but also for two functions at the church and for two men's basketball games. In addition, Julie and I had hosted a school-board committee meeting in our home one night and had a young couple over on another night to help them with their finances. Fewer than half of the past 14 nights had been spent with our children. Since work was the culprit the last three nights, it caught the brunt of the blame. The issue, however, wasn't just work.

Balance is defined as "the ability to keep in equilibrium, to estimate the relative importance or value of something." Julie and I have found that it takes a constant effort to balance our lives and keep the pendulum from swinging wildly past center.

It can be a challenge to balance the components of family, work, church, world, and a relationship with God. It's easy to get out of balance in any of the areas by taking time away from one of the other areas. For example, we could spend so much time involved in the church that we neglect our vocational work. Or we could spend so much time evangelizing the world that we neglect our families. Obviously, being out of balance in any area could make it extremely difficult to meet the challenge of balancing posterity (the heritage we leave) and finances.

Though imbalance can occur in any area, I'm convinced that in modern society the most common and greatest threat to a balanced life occurs because of the tension between family and work. In this article we'll take a look at why this tension exists, primarily from the work perspective, and offer suggestions about how to deal with it.

Family and work

The tension between family and work is great because they both require a large time commitment. Yet

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IN THIS ISSUE

EDITORIAL

Showing Compassion for "The Least of These"

With the Thanksgiving and Christmas seasons approaching, our churches and Christian relief organizations soon will be encouraging us to have a charitable and giving spirit toward the poor. This is good. But may I suggest that care should be taken so the breadth of our compassion is neither too broad on the one hand nor too narrow on the other.

How can it be too broad? Many Christians use Jesus' parable in Matthew 25 as the basis for exhorting the church to care for society's downtrodden. Yet, picking up the text in verse 37, we read (emphasis added):

"Then the righteous will answer him, 'Lord, when did we see you hungry and feed you, or thirsty and give you something to drink? When did we see you a stranger and invite you in, or needing clothes and clothe you? When did we see you sick or in prison and go to visit you?' The King will reply, 'I tell you the truth, whatever you did for one of the least of *these brothers of mine*, you did for me.' "

To say this parable refers to all of the world's poor, both Christians and non-Christians alike, is to inappropriately broaden it far beyond its scope. Throughout the New Testament, the primary usage of the word "brothers" is in reference to Christians. The secondary use is to refer to fellow Jews. Nowhere can I find it ever used to refer to humankind in general. Also consider:

• Matthew had earlier taught who the "brothers" of Jesus were. " 'Your mother and brothers are standing outside, wanting to speak to you.' He replied to him, 'Who is my mother, and who are my brothers?' Pointing to his disciples, he said, 'Here are my mother and my brothers. *For whoever does the will of my Father in heaven is my brother* and sister and mother' " (Matthew 12).

• Paul had a similar view as to who are God's children and Jesus' brothers: "Those who are led by the Spirit of God are sons of God. For you did not receive a spirit that makes you a slave again to fear, but you received the Spirit of sonship.… For those God foreknew he also predestined to be conformed to the likeness of his Son, that *he might be the firstborn among many brothers*" (Romans 8).

• In Hebrews 2, the writer has this to say on the subject of sonship: "In bringing many sons to glory, it was fitting that God, for whom and through whom everything exists, should make the author of their salvation perfect through suffering. Both the one who makes men holy and *those who are made holy are of the same family. So Jesus is not ashamed to call them brothers.*"

• There are many verses that specifically tell us to give priority to the needs of believers in Christ versus those of society in general. Among others, they include: "Be devoted to one another in brotherly love.… Share with *God's people* who are in need" (Romans 12). "*Suppose a brother or sister is without* clothes and daily food. If one of you says to him, 'Go, I wish you well; keep warm and well fed,' but does nothing about his physical needs, what good is it? In the same way, faith by itself, if it is not accompanied by action, is dead" (James 2).

• We apparently will be rewarded in the next life for acts of mercy and charity we demonstrate in this one. However, the promise applies not to indiscriminate benevolence but to acts of kindness rendered to a specific group of people: "I tell you the truth, anyone who gives you a cup of water in my name *because you belong to Christ* will certainly not lose his reward" (Mark 9).

In Matthew 25, Jesus is not arguing for humanitarian efforts in the community at large. He is saying that love for the body of Christ is evidence that we know Him. Am I saying that we are not to assist the poor who do not share our faith? Of course not. In fact, I am arguing for demonstrating greater compassion for them, not less. I am suggesting that while our benevolence should include their material needs, it should lovingly be paired with the gospel. Should we not provide them food for their souls, which are eternal, as well as for their earthly bodies which are, after all, only temporal?

Let our teachers exhort us from John 6 rather than Matthew 25: "Then Jesus declared, 'I am the bread of life. He who comes to me will never go hungry.… I am the living bread that came down from heaven. If anyone eats of this bread, he will live forever.' "

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A Work-Life, Well Spent

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the Bible is clear about our responsibility in each of these areas. For example, Deuteronomy 6:6-8 states that I'm to teach my children as I sit in my house, as I walk by the way, and as I lie down and rise up. Sitting, walking, lying down, and rising up require a lot of time! And 1 Peter 3:7-9 tells me that husbands and wives are to live together in a harmonious and understanding way. The Bible is also clear about our responsibility to provide for our families. The apostle Paul said if we do not provide for our families, we are "worse than an unbeliever" (1 Tim. 5:8), and if we do not work we should not eat (2 Thessalonians 3:10).

The issues related to our church, world, and government also require time, and they cannot be neglected in raising godly posterity; however, these components are typically less of a time drain than family and work.

Over the years, I've kept excerpts of articles that clearly point out this tension. This sampling shows the sense of loss when the components of work and family are out of balance:

- **Billy Graham**, evangelist: "The greatest mistake was taking too many speaking engagements and not spending enough time with my family."
- **Peter Lynch**, author and legendary mutual-fund manager: "My problem is, I operate in only two gears, overdrive and neutral, and it's all been overdrive since about 1982….I had to return from [a family ski trip] early and missed seeing my daughter in a race. I was in here at the office when the market was closed and the family was skiing and I said, 'What am I doing?'.... I haven't been there for my seven-year-old, either."
- **Garth Brooks**, country music star (commenting on his daughter): "She's already taught me the greatest lesson in life—that nothing is more important than family…. I see that little girl and think, 'You've been chasing stuff that means nothing, and you've been running away from this…. The one gift that I want to give this kid is the best gift that my dad and mom ever gave me—attention—to know that every time I looked up from that bench at any sporting event, no matter how far away it was, no matter if I was playing or not, they were there."
- **Dan Stamp**, president of Priority Management Systems: "People often say, 'For now, I'll focus exclusively on my career, but in the future, I'll do more with my family.' But by the time the future comes, by the time the person is ready to be a real parent, he may find that it's too late. The kids are grown up—never to be five or 10 years old again. Once those years are missed, there's no going back."

Some readers may be further along in life and have already discovered what those busy people discovered—that we should have balanced our lives a little more. If this is the case for you, let me encourage you that it's never too late to build posterity. Even if your children are grown and have children of their own, you can still spend time with them. You can try to help them avoid making the same mistakes you may have made, and you can encourage them with their posterity.

Variable-time vs. fixed-time vocations

I'm convinced that we should earn our money by working hard, by doing our best at the vocation God has equipped us to do during our allotted time here on earth—while at the same time allowing appropriate amounts of time to be with our families.

Newly married individuals without children typically have more time available to work vocationally because the person's only other responsibility is to a spouse. If you have young children, their needs, as well as the needs of your spouse, are more acute and the amount of time available for work is squeezed. As the children grow up and move out of the home, your available time to work is once again expanded.

Your allotted time to work will be a function of whether your vocation is what I call a variable-time job or a fixed-time job. In a variable time job you do not punch a time clock. These vocations are typically not 8-to-5 types of jobs but rather work that has fluctuating hours. In my job, I'm not required to punch in and out each day, but I have certain performance standards that must be met. Some days may be 12 hours long; others are much shorter. Through it all, however, there is always more to do than can be done in a reasonable day, so the pressure to spend more time at the job always exists. This is the open-end characteristic of a variable-time job. The salesperson could always make one more sale, the doctor could always see one more patient, and the business owner could always help one more customer. More can always be done! The question is, "Where do we stop?"

Conversely, the fixed-time job is the 8-to-5 type of work that neither requires nor expects much involvement beyond the time spent in the office or shop. The factory worker, secretary, nurse, and some jobs in larger companies are examples of fixed-time vocations.

At our firm we work primarily with individuals who fall into the variable-time professions—business owners, entrepreneurs, doctors, dentists—since the variable professions typically generate the most income. On the surface it seems that variable-time workers have it made. They have time and money for vacations.

In reality these individuals have a challenge in building posterity that fixed-time workers do not have. They have to constantly guard against overworking. I define overworking as any situation in which a person is spending hours on his or her vocation to the exclusion of other priority areas, such as family, church, and personal time. The fixed-income worker punching a clock doesn't typically have the pressure to overwork. Most days, he or she puts in eight hours and goes home. However, on the surface what appears to be a positive of the variable-time job—the higher income—is in many cases a detriment to spending time with family and training up a godly posterity.

Business owners are a case in point. In most situations they are not only the visionaries of their businesses but also the primary decision makers. Though they usually have sufficient income to buy "freedom" by hiring others to do some of their work, they are typically hesitant to do so for fear of losing some control. They simply can't let go of the decision making, and, as a result, their time is not free. It's not their own. They are the ones with the cell phones glued to their ears or next to them on the bedside table. They may be physically away from the office, but mentally the office streams through their consciousness. As the business succeeds and generates more income, the opportunities to grow increase and their freedom is reduced even more. They may have more financial capital than ever, but spend less time with their families.

The medical profession offers vocations that are held in an esteemed position in the minds of most people. They typically generate significant income and appear to allow for a lot of discretionary time for workers to be with their families. However, doctors are on call at night and on weekends, an arrangement that can present significant challenges to spending time with family, especially in the early years of their practices.

What about salespersons? Their income is a function of their own efforts, and typically the more time they spend at their jobs, the more income they can make. And their companies usually impose sales quota pressures (or they do it themselves). They want to constantly sell more and more.

Many jobs seem to have no boundaries on the time that can be spent working. Most vocations that tend to generate the greater incomes also tend to exert the greatest pressure on the person's time. If not handled properly, this pressure can steal the time necessary to raise godly posterity. Vocations that put the least stress on the person's time tend to produce less income and can put more stress on the financial side.

One final comment about overworking. Many persons may overwork, not because of the money, but because their identities and self-images are tied to what they do. We must recognize that our self-image is a function of who we are in Christ. It should not depend on our vocation. We need to keep our egos out of it and realize that God "resists the proud" (1 Peter 5:5).

Practical steps toward balance

Regardless of your vocation, consider the following observations as you struggle to balance your work and your need for time margin for training your posterity.

1. Find a vocation you enjoy and are equipped for, and then live within the income it provides. It's your responsibility to work hard and well at what God has called and equipped you to do (Colossians 3:23), realizing that the income you generate is no surprise to Him. He sovereignly ordains it through your employer or through the clients or sales He allows you to have in your business.

2. If you are in a fixed-time job that has limited income, don't think you would be better off in a vocation that paid more money. It may be easier for you to raise godly posterity because of fewer time pressures than it would be for the person who has the variable time job and greater income. Although less income may result in more financial pressures, lifestyle—not income—is often the reason for financial pressure. Therefore, control your lifestyle, live within your income, and be content in the vocation for which God has equipped you.

3. Be aware of the different time demands at your family's different stages. The needs and time demands are the greatest when the children are young. Those demands usually subside somewhat through the teenage years and into college.

Let's look at how this works out practically. If you're starting a business and you don't have children yet, project what your time commitments will be later in the business as you start a family. If the growth of the business reduces your time commitments, that's good. But if business growth will require more of your time exactly when your children need you, you may want the business to grow more slowly, hire a key assistant, or stay smaller longer. If you're in one vocation and are considering switching to another, be careful to evaluate the impact of the change on your time. Also evaluate where you are in the different stages of your family life. If the children are young, you may be better off waiting a few more years until they're teenagers to make the switch. Or if they are teenagers, you may want to wait until they graduate from high school.

I know this concept of slowly climbing up or even getting off the ladder of success is a difficult one, especially for some men. In such cases, I always try to remind my clients what really counts for eternity.

I must add a comment lest you think I'm leaving God out of this equation. What if God "calls" you to another vocation at what appears to be a wrong time? For example, when a new job would take you away from your children. Using 1 Corinthians 10:13 and 1 Thessalonians 5:24 as cornerstone passages, I'm convinced that God is faithful and will not call you to do something He won't also give you the ability to handle. In this case, He will give you the ability and energy to stay balanced. It's hard, however, to fathom God calling someone to a job that would dilute His ministry in people's (and children's) lives.

4. Don't be in a big hurry to retire and quit working. Extend your work horizon. One of the biggest obstacles to keeping work in balance is the "hurry up and retire" mentality. In our business we've found that regardless of how much money a person has, in most cases, he will continue to work. Work is good, and it brings fulfillment (Genesis 2:5,15). Man was created by God to work, and if he doesn't work he may be quite miserable. Many men grow bored quickly after they retire.

You have your entire lifetime to work, and only 20 years to make the primary impact on your children. Therefore, earn your income slowly. Spread your earnings over a 40- to 50-year period. You don't have to be a millionaire by the time you're 40, nor do you need to retire at 55.

One of the greatest causes of midlife crisis is that many men work so hard and go so fast they accomplish all their goals by the time they're in their 40s. Then they wonder, "What's next?" What's next is what they forgot. They forgot to spend time with their kids and wife, and by then, in many cases, it's too late.

5. Only change vocations to better fulfill your purpose and maximize your time flexibility—not to make more money. As Solomon said, "He who loves silver will not be satisfied with silver; nor he who loves abundance, with increase. This also is vanity" (Ecclesiastes 5:10). A change in vocation will by necessity require a greater time commitment. You must invest time to learn the new job. This may be all right if the investment of additional time doesn't last too long and will result in more time, flexibility, and options later. However, many individuals change vocations in pursuit of more money, only to find that the cost to the family wasn't worth it. Also, making the change often takes so much emotional energy that the additional income isn't worth the effort. We have only so much emotional energy. If we spend it all on job changes, we don't have any left to apply to raising our children.

This is not to say that no one should ever change vocations, but the costs need to be carefully weighed. It may be that you would be better off waiting and earning less income at the old job until your children are at an age where a job change wouldn't be so disruptive to them by taking you away from them.

A friend of mine decided to change jobs. Although his motive wasn't more money, he underestimated the emotional cost. Not only were his financial pressures increased, but his time commitments increased as well. His wife needed to work because he was having trouble financially. This wouldn't have been a significant problem if the children were older, but they needed mom and dad then—not in three to five years when less time and energy was demanded by the new job.

I remember when I was teaching school right out of college and decided to change jobs. One of the teachers commented that I could make a change relatively easily at that point because I had no children, but that it would be harder if I were further down the vocational road. I didn't know what he meant then, but I do now. It would have been difficult to spend the time necessary to start my financial-planning career if I had had young children. If I'd had children at the job change point, I might have been better off staying in the secure, lower-paying teaching job with less emotional and time pressures. This isn't to discount following God's call about changing jobs. It's just that flexibility to meet other objectives needs to be a high consideration.

6. If you are in a variable-time job, set your time parameters and do what you can do. Then trust God to do what you cannot do. If you're a salesperson, specify a reasonable number of hours you're going to devote to your work. Set an amount that will allow you to provide for your family's needs and work hard during those hours. When those hours are up, stop working and spend time with your family.

If you're in an unavoidable situation that requires you to spend a large block of time at work, try to make up for current overtime through future extended and relaxed times with the family. As an example, I once had a really tough week. I had three out-of-town trips in seven days, including four nights away from home. However, since I knew this was coming, I planned to take some relaxed time with my family the week after the trip. I didn't schedule any early-morning meetings so I could have breakfast with the kids and a cup of coffee with Julie. *When work does get out of balance, make plans to bring it back into equilibrium.* Put time with family in your business calendar just as you do your work appointments. Develop the good discipline of planning to build margin by coming home early or going in late a couple days a week.

7. If you're in a vocation that is currently generating sufficient income, be careful to evaluate additional time spent to earn more income, especially if your children are young. If you have the opportunity in your vocation to opt for less income or to freeze your income and get more free time when the demands of your family are the greatest, consider doing it. Don't fall into the trap of thinking, *I'll work really hard now and make a lot of money, and then I'll spend time with the children.* Remember, the children's first 10 years are the most critical. If you're making enough now, the extra time may be more valuable than the extra money.

An article in *Money* magazine illustrated this point quite nicely. The author wrote, "Once you've reached a certain level of comfort, the return on extra earnings begins to diminish—particularly if the extra work erodes your quality of life…. You may be able to improve your life by reducing spending." Here are practical ways to implement this observation:

• Opt for a slower career path, and plan to work until you're 70 or 75. Although some corporations aren't concerned about family and may label you as disloyal if you take this option, there seems to be more and more flexibility on this front. In today's economic environment, many companies are looking for creative ways to compensate employees other than with salary increases. Some of the ways they're doing this are by offering flexible time schedules, alternative work schedules, and more vacation time and personal days. Don't hesitate to negotiate with your employer.

• If you're the boss, consider reducing your income so you can hire someone to free up some of your time. For example, a friend of mine didn't need the six-figure income he was making, so I suggested he use the extra income to hire some help. He did it and had more time with his children at a very strategic time in their development.

• As a trade-off, opt for more vacation time instead of salary increases. Some Fortune 500 companies allow employees to elect "vacation days" as part of their benefits package. The employee "buys" these days through reduced salary.

• Offer to work four-day weeks rather than five for 80 percent of your current salary.

• Offer to work six- or seven-hour days versus the traditional eight- to ten-hour days for less salary.

Of course, to successfully implement this observation, it's important to make good financial decisions and control your lifestyle so you don't need to earn more and more money.

Balance is the key

No good comes from overworking, especially when the cost of the overwork is the family. We Christians should be at the forefront of the movement to balance life and integrate meaning into our lives. We must be prepared to handle the peer pressure of the world and even of some well-meaning Christians who will not understand us. "Why," they will wonder, "are you slowing down your climb up the ladder? Why didn't you take that job with more income? Why do you drive that old car and live in a smaller house?" The answer is that we look to the end of our lives and realize we must make the tough decisions now. ◆

Russ Crosson is Executive Vice President and Chief Mission Officer of Ronald Blue Trust and Executive Vice Chairman of the board of directors for Thrivent Trust Company, the parent company of Ronald Blue Trust. He and his wife, Julie, have three children and five grandchildren.

LEVEL 1 ONE

Strengthening Your Foundation

Wise money management begins with a strong financial foundation. In this column, we cover topics such as how to manage cash flow, apply strategies for getting debt-free, make wise purchasing decisions, build savings, choose appropriate insurance protection, navigate marital financial issues, and many more.

"By wisdom a house is built, and through understanding it is established." Proverbs 24:3

6 STEPS TO BUDGETING SUCCESS

by Austin Pryor

At Sound Mind Investing, we have written before about the importance of agreeing on a cash flow plan (a.k.a., a budget!) and following it faithfully. For several years during the late 1980s, my wife Susie and I applied a rather rigorous approach to control our spending, and it worked pretty well. I didn't keep a diary at the time, but looking back on it now, these are the "keys to success" that come to mind.

1. Be truthful in your communication. I keep track of the money in our family, and so I was the first to realize we were facing a serious financial challenge (see chapter 28 in the *SMI Handbook* for background). Susie knew we were experiencing some financial disappointments, but didn't know how difficult it had become to balance our income and outgo. Even though some of the events that had caused the problem were beyond my control, I felt like a failure in my role as the financial provider in the family. I hated the idea of telling her our situation, but we needed to make some changes and I knew it would take both our best efforts to turn things around.

2. Be thorough in your preparations. As I began working on our spending plan, I listed not only every category of spending I could think of, but also every anticipated item within each category. For example, I didn't just put down $500 for family birthdays—I listed each person on the gift list and how much we typically spent on that person. The more categories you have, the better idea you'll have of where all the money's going and, consequently, the more ideas you'll get on where you can save. Furthermore, I didn't just put down round numbers that "seemed right." I used canceled checks, credit card bills, and old tax returns to see what I'd actually spent in the past.

3. Be willing to change your lifestyle. All of my work only gave us a picture of where our money had gone in the past. Then it was time to go over the spending categories and discuss what we could do to lower (or temporarily eliminate) the spending in each one. Savings are possible in most categories if you're willing to make changes in your lifestyle and shopping habits. Focused on the goal of living on less, and with a little creativity, it doesn't even feel like suffering!

4. Be consistent in monitoring your spending. My goal was to account for 100% of our spending (an almost impossible task, as I was to find out!). It's amazing how much money is spent a few dollars here and a few dollars there. This was more of a burden on Susie than on me because she typically handled the majority of our routine spending. We used "old reliable"—the envelope system—to help us stay within our budget. Here's how we did it.

Each week, I would write a check to Susie for the budgeted amounts in the categories she was most responsible for. She would cash it and carry the money in her purse in a small envelope that was just slightly larger than a dollar bill. If she went to Kroger and spent $48.24, she'd write "Groceries $48.24" on the front of the envelope at the time she withdrew the money. Ditto the drug store, gas, school lunch money…whatever.

There were two advantages to doing it this way. First, it was easier to keep track of her spending because she was pulling the cash from the actual envelope. Second, she could pace herself as the week went along and she saw her cash begin to dwindle. At the end of the week, she'd give me the old envelope so I could track her spending in a spreadsheet. Any unspent money was transferred to a new envelope and the process would start over.

An area of confusion for many couples is how to handle the spending that occurs periodically rather than weekly. The way that worked best for us was to divide those items into two groups. I took responsibility for the expenses that were somewhat automatic with respect to the amount and date due—for example, monthly mortgage, life insurance premiums, utilities, and tuition payments. These were typically paid by check. Susie took those categories where purchasing decisions were involved—birthdays, clothing, household items and repairs—and we set aside an amount in an envelope for each one. These were handled like the weekly envelope system except she didn't need to carry them with her.

5. Be disciplined in staying within your agreed upon limits. The reason you need to closely monitor your spending is so you will know if you're on target or whether mid-course adjustments are needed. This gives you a certain degree of flexibility. If you go over in one area, you can cut back in another.

For example, an unexpected dental bill of $200 may have to come out of your "recreation" envelope if the "medical" envelope is already empty. Or, you might prefer to take $20 out of 10 different envelopes to spread the shortfall around and lessen the impact on any one category.

6. Be mutually supportive. Susie was great! She wasn't critical in any way. In fact, she continually reminded me that God was the source of supply, and we would just need to do the best we could while waiting on Him to send a solution. Her attitude was a tremendous encouragement as we "tightened our belt." If you and your spouse aren't of one mind as to the importance of developing and living out this kind of lifestyle, conflicts will arise frequently. So pray together for unity in your finances. ◆

LEVEL 2 TWO

Developing Your Investing Plan

Investing decisions are best made as part of a comprehensive personalized plan. In this column, we focus on topics that will help you implement an investment strategy that takes into account your personal goals, attitude toward risk-taking, and current season of life. We explain investing essentials, discuss SMI's core investing strategies, and help you decide which strategy is best for your situation.

"The plans of the diligent lead to profit as surely as haste leads to poverty." Proverbs 21:5

WILL THE BEAR'S BITE BE ESPECIALLY PAINFUL FOR PASSIVE INVESTORS?

Managing expectations is a crucial aspect of successful investing. With today's long-running bull market having proven its resilience in the face of political, economic, and virtually every other type of threat over the past eight-plus years, it's become dangerously easy for investors to expect the good times to continue indefinitely. Perhaps more than any other group, index-fund investors are particularly at risk of complacency due to their passive approach to their investments.

The golden age of indexing

Index-fund investing has been all the rage in recent years. According to Morningstar, while there is still more money in actively managed funds than passively managed funds ($9.3 trillion vs. $5.3 trillion, as of the end of 2016), the tide is shifting rapidly. In 2016 alone, total actively managed fund assets declined by $285.2 billion, while passive fund assets increased by $428.7 billion. That trend has been in motion for several years now.

The dramatic shift to index funds has been fueled by a pair of powerful forces. The first is the recent performance of passive index funds relative to actively managed investments. Active management, taken as a whole and after accounting for its typically higher fees, has failed to beat its benchmarks in most cases. This performance shortfall has been especially vivid during the current bull market, which now extends back the better part of a decade. As a result, it's been easy for investors to become convinced that passive investing is the "simple" way to succeed.

Second, the dominant financial advisory model has shifted so as to align advisors with indexing. Over the past 10-15 years, most advisors have shifted away from the old commission-based model in favor of a "1% of assets" wrap-fee approach. While in theory this unties an advisor's hands to recommend whatever he or she thinks is best, in reality the overall fees charged within the portfolio are a significant constraint. With the advisor's fee already at 1% or more, it's difficult for most advisors to recommend adding substantial active-management fees on top of that. Putting a client in a suite of low-cost index funds is much more palatable, as it keeps the overall expense ratio of the portfolio lower.

THE GREAT INVESTING DIVIDE

Passive Management
Investing in a broad cross-section of securities so as to generate investment returns *similar to* those of the market as a whole. This approach is also referred to as "indexing." No attempt is made to gather and analyze economic and financial information. SMI's Just-the-Basics is a passive strategy.

Active Management
The gathering and analysis of economic and financial information for the purpose of buying and selling securities in an attempt to generate investment returns *greater than* those of the market as a whole. SMI's Upgrading, DAA, and Sector Rotation are active strategies.

Not surprisingly, the brokerage house that invented the index fund, Vanguard, has been the biggest beneficiary of index-fund enthusiasm, with nearly $300 billion flowing into its funds in the first nine months of 2017. The firm now has $4.7 trillion under management.

Daniel Wiener, editor of the *Independent Adviser for Vanguard Investors*, a newsletter that follows Vanguard funds, told the *Wall Street Journal* there's only one thing that could stem the tide: "I don't think that there's much that changes these flows until we have a negative market. I can't tell you when that happens, but when it does there will be a lot of very surprised investors."[1]

Caution is advised

And there's the rub for index-fund investors. Having bought into the narrative of index-fund superiority, and having enjoyed a relatively smooth upward ride since 2009, any change of market direction likely will come as a shock. Concerns are growing that index-fund investors in particular may be in for an especially rough ride when the market changes direction.

Josh Brown, CEO of Ritholtz Wealth Management and author of the widely-read blog, *The Reformed Broker*, wrote this in May: "What will happen into the teeth of the next 20% stock market decline? Here's what I would guess: Vanguard loses 10-15% of its AUM [assets under management], an enormous outflow in a very compressed period of time as newly-minted passives realize that they're not quite cut out to be passive after all. The pain will prove too much for many recent indexing dilettantes who thought this was easy."[2]

There are at least two specific reasons to believe index-fund investors may suffer disproportionately during the next bear market:

1. Index funds are always fully invested. By definition, index funds are designed to mimic a particular index, such as the S&P 500. As such, they typically allocate *all* of their assets to the investments that compose their benchmark. Holding no cash gives index funds an advantage over actively managed funds during bull markets, but that can turn into a disadvantage during a bear.

Actively managed funds, on the other hand, typically keep 2%-4% of their assets in cash in order to handle normal customer cash flows without having to disrupt their portfolio to cover redemptions. In addition, some managers like to have some cash on hand to take advantage of buying opportunities that present themselves.

Taking that a step further, some active-fund managers have increased their cash holdings as a defensive position against future market declines, noting the market's (continued on page 172)

[1]on.wsj.com/2yY6PYY [2]bit.ly/2q2yZAs

LEVEL 3 THREE

Broadening Your Portfolio

This column goes beyond the investing essentials taught in Level 2, introducing you to a wider range of investment securities and markets. By further diversifying your holdings, you can create a more efficient, less volatile portfolio. We also comment quarterly on the performance of the various markets, and on how SMI's fund recommendations and strategies have fared.

"Divide your portion to seven, or even to eight, for you do not know what misfortune may occur on the earth." Ecclesiastes 11:2

3RD QUARTER REPORT: LET THE GOOD TIMES ROLL

The financial markets continued their uninterrupted march higher throughout the third quarter, with both stocks and bonds adding healthy gains. Foreign markets were again the strongest performers, but domestic stocks also were strong across all of SMI's risk categories.

The S&P 500 total-return index has now had 11 consecutive winning months (Nov-Sept). That's quite rare, happening for only the second time in the past four decades. As we have noted previously, this is also just the sixth time since 1950 that more than a year has passed without at least a 5% pull-back for the S&P 500 index. This lack of volatility has been highly unusual by historical standards.

Sustained trends like this are great for SMI's trend-following strategies, so it's no surprise they posted excellent performance during the third quarter and sport compelling year-to-date numbers as well. While market storm clouds may be rumbling in the distance, the third quarter was a reminder that cashing out of a richly-valued market while it is still rallying can mean leaving considerable gains on the table.

Just-the-Basics (JtB) & Stock Upgrading

Just-the-Basics rode strong foreign- and smaller-stock performance to a +5.0% gain for the quarter, finishing ahead of the U.S. market's +4.6% gain (as measured by the Wilshire 5000, the broadest U.S. market index). Stock Upgrading performed even better, gaining +5.7%.

On a year-to-date basis, Upgrading pulled into a slight lead over the market, +13.8% vs +13.7%. JtB is the leader among SMI's broadly diversified strategies so far in 2017, having gained +15.0%. It's been a great year to be invested in stocks!

Bond Upgrading

The Federal Reserve held short-term interest rates steady during the third quarter, and longer-term rates remained quiet as well. This led to muted, though positive, returns for most bond investors. The Barclay's U.S. Bond Index gained +3.1% year-to-date, with Bond Upgrading trailing slightly at +2.4%. However, if we go back one more quarter to take in a full year (and include the bond market volatility that occurred immediately following last year's election), Bond Upgrading leads the index by a +0.8% to +0.1% margin.

While the third quarter was quiet for bonds, the fourth quarter may provide some interesting developments. Not only is the Fed expected to raise interest rates one more time this year, it also will begin the process of reducing its balance sheet by letting bonds expire as they mature. In recent years, when a bond owned by the Fed matured, it rolled that money into a new bond, but the Fed is gradually shifting away from this. As with all of the Fed's Quantitative Easing policies, this is uncharted territory, so no one knows how the markets will respond. That said, there's little reason to expect any dramatic immediate impact.

Dynamic Asset Allocation (DAA)

DAA posted another solid quarter, with a +3.0% gain. While that's less than the market's +4.6% gain, it's important to remember that DAA invests a maximum of two-thirds of its portfolio in stocks. That almost always will result in DAA trailing during strong market rallies. In that context, we're thrilled with DAA's +11.1% gain through the first nine months of 2017, despite the broad stock market being up +13.7%. When DAA hangs that close during rising markets, we know its returns will quickly catch up to the market once the next bear market shifts the playing field in DAA's favor.

3RD QUARTER 2017 DAA ETF UNIVERSE

Ticker & Category	3Q Result
SPY U.S. Stocks	+4.4%
EFA Foreign Stocks	+5.0%
VNQ Real Estate	+0.9%
BLV Long-Term Bonds	+1.6%
SHY Money Market	+0.2%
GLD Gold	+3.0%

As Austin detailed in last month's editorial, being insulated against the potential of a market decline is crucial at this point in the stock-market cycle. It's hard to imagine that the next bear market may be looming when stocks have risen uninterrupted for so long. But we know markets are cyclical, and unfortunately the strong gains of recent years don't make stocks *less* risky; they become *more* vulnerable the further valuations get stretched.

Sector Rotation (SR)

We've run out of superlatives to describe SR's superior performance. Up a stunning +19.6% in the third quarter, it now sports a 2017 year-to-date return of +36.1%. Are those facts more or less amazing than the fact that SR is up +28.2% *annualized* over the past five years? We'll let you be the judge.

SMI launched SR as a live strategy nearly 14 years ago in November of 2003. Since then, SR investors have enjoyed annualized gains of +16.4% per year. That dwarfs the market's +9.0% rate of return over the same period. But to really grasp the significance of those annualized numbers, it helps to translate them into actual dollars. A $25,000 initial investment that earned the market's rate of return would have grown to a healthy $83,405 over those nearly 14 years. But that same investment made in SR would have grown to $207,899—two-and-a-half times as much!

Compounding a high rate of return over an extended period like that can yield awesome results. Best of all, those aren't hypothetical numbers—many SMI members have actually earned them, having started with SR when it was first rolled out. The question is whether *your* portfolio is positioned to take advantage of this type of compounding in the future? (continued on page 173)

LEVEL 4 FOUR

Looking Toward Retirement

As you move through your 50s, 60s, and beyond, you face a new set of financial decisions related to reducing your investment risk and generating income from your portfolio. In this column, we address such topics, as well as those pertaining to Social Security, long-term health care, advanced giving strategies, estate planning, and other matters of importance to those nearing and in retirement.

"There is precious treasure and oil in the dwelling of the wise." Proverbs 21:20a

BRIDGING THE GAP: COVERING WHAT MEDICARE DOESN'T PAY

Many people assume Medicare pays for all medical expenses of America's seniors. That isn't the case and never has been. The program—modified only slightly since being launched more than a half-century ago in 1965—was intended to cover only minor medical expenses and short-term care.

As medical costs rose (and treatments expanded) in the 1970s and 80s, the dollar gap between how much Medicare paid toward healthcare bills and what patients had to pay grew larger. To bridge the gap, Congress eventually authorized Medicare Supplemental Insurance or "Medigap"—private insurance plans regulated by the states but with federally standardized benefits. Such plans picked up paying benefits where Medicare left off. Then in 1997, Congress went further. It approved a more flexible approach to additional Medicare-related coverage, leading to what is now known as Medicare Advantage.

Medigap and Medicare Advantage plans give seniors broad coverage options, but broad also can mean confusing—and this is the season when that confusion is strongly felt. Each year at this time, during Medicare's Annual Coordinated Election Period (ACEP), Medicare enrollees can choose their health coverage for the next year. They either can stick with Original Medicare (also known as Medicare Parts A and B) or choose a private Medicare Advantage plan (Part C).[1]

Of Medicare's 58 million enrollees, about a third currently are enrolled in Original Medicare with a Medigap supplement, another third are in Original Medicare without a supplement, and one-third have an Advantage plan. But Advantage plans are surging. Over the past decade, enrollments in Medicare Advantage have nearly doubled, while enrollments in Original Medicare have grown only slightly.

Just to be clear, the choice to be made during the annual Election Period is between Original Medicare and Medicare Advantage. The selection of a companion Medigap plan to go with Original Medicare is a separate decision and can be made at any time, although typically Medigap plans are chosen when a person first signs up for Medicare (see below). Because Medigap plans are designed for use with Original Medicare, switching to an Advantage plan means you'll no longer need Medigap.[2]

Supplementing with Medigap

Choosing between Original Medicare and Medicare Advantage, however, isn't just a matter of looking at those two options. If you want a healthcare plan that covers what Medicare doesn't, Medigap must also be considered as part of your Original-vs.-Advantage decision (even though you can apply for a Medigap plan at any time).

Medigap plans cover certain costs—primarily deductibles, copays, and coinsurance—not paid for by either Part A (hospital insurance) or Part B (medical coverage). These supplemental Medigap policies typically cover the *entire* portion of any hospital charges Medicare doesn't pay plus 20% of medical expenses (Part B covers the other 80%).

Although Medigap policies are sold by private insurance companies, they have federally mandated benefits and are regulated (in varying ways) by the states. In most states, they come in 10 varieties (or 11, depending how you count them), known simply as Plans A, B, C, D, F, High F, G, K, L, M, N (don't confuse Medi*gap* "Plan A" or "Plan B" with Medi*care*'s Part A and Part B!).

Every Medigap "A" plan—regardless of insurance company or the state you live in—has the same *benefits*, each "B" plan is the same, each "C" plan is the same, and on down the line.[3] Even so, Medigap *premiums*—even for the same plan type—can vary widely from company to company, so shop around.

Because most Medigap plans pay "first-dollar" coverage (i.e., they cover all of the "gap" between what Medicare pays and the total obligation), Medigap premiums aren't cheap—typically $200 and $400 a month in addition to the Part B premium that typically ranges from $109-$134. (A few Medigap plans have lower premiums because they have either out-of-pocket limits or a high-deductible before full benefits kick in.)

During the sixth-month Open Enrollment Period (tied to when a person first enrolls in Medicare Part B), all Medigap policies are "guaranteed issue." A person with a health condition who applies during that six-month period can't be refused or made to pay higher rates. Once the sixth-month window has passed, however, an insurance company can refuse a Medigap application or set a higher premium based on a pre-existing condition.

If you buy a Medigap policy, make your initial choice carefully. Although you can switch to another Medigap policy later, switching is a cumbersome process (except in a handful of states that allow switching once a year). In addition, any new policy likely won't be "guaranteed issue," meaning your application could be refused (or you could be made to pay more) if you have a health condition.

Taking Advantage

Medicare Advantage plans are sold by private companies that contract with Medicare. Instead of getting Plan A's hospital coverage and Plan B's medical insurance directly from Medicare, you'll get them from a private company. But Advantage plans go beyond the Medicare-designed A and B benefits. Many include payments for (continued on page 173)

[1]Another decision is whether to sign up for optional prescription-drug coverage (Part D). [2]If you switch then change your mind within a certain period, you can revert to your previous plan. [3]A reduced-cost Medigap plan called Medicare SELECT is available in some areas. It limits choice to specific hospitals/doctors.

SOUND MIND PORTFOLIOS

Basic Strategies

The fund recommendations shown for Upgrading accountholders are based primarily on their most recent "momentum" scores at mid-month (not the earlier end-of-month scores shown on this page), but consistency of performance and the portfolio manager's philosophy and number of years at the helm are also important. Three recommendations are made in each risk category so that you can select the one(s) most in accord with your preferences and broker availability.

"Plans fail for lack of counsel, but with many advisers they succeed." Proverbs 15:22

RECOMMENDED FUNDS FOR SMI'S JUST-THE-BASICS STRATEGY

Data through 9/30/2017	Portfolio Invested In	MOM	Performance YTD	1Mo	3Mo	6Mo	12Mo	3Yr Avg	Rel Risk	Expense Ratio	Stock/Bond Mix 100/0	80/20	60/40	40/60	Ticker Symbol
Total International Stock ETF	Foreign stocks	37.0	21.6%	1.9%	5.9%	12.0%	19.2%	5.3%	1.15	0.11%	20%	16%	12%	8%	VXUS
Extended Market Index ETF	Small company stocks	31.9	12.7%	4.2%	5.0%	7.8%	19.0%	10.5%	1.22	0.08%	40%	32%	24%	16%	VXF
S&P 500 Index ETF	Large company stocks	30.7	14.0%	2.0%	4.5%	7.7%	18.5%	10.8%	1.00	0.04%	40%	32%	24%	16%	VOO
Total Bond Mkt Index ETF	Medium-term bonds	3.0	3.2%	-0.5%	0.8%	2.4%	-0.1%	2.6%	1.02	0.05%	None	20%	40%	60%	BND

VANGUARD JUST-THE-BASICS FOOTNOTES: Just-the-Basics is an indexing strategy that requires just minutes a year to assure that your returns are in line with those of the overall market. You won't "beat the market" using this simple strategy, but neither will you fall badly behind. Your JtB portfolio should be allocated among as many as four Vanguard funds (as shown above) depending on your stock/bond mix. For more on Just-the-Basics, see June2012:p89.

RECOMMENDED FUNDS FOR SMI'S FUND UPGRADING STRATEGY

Risk	Data through 9/30/2017[1]	Date Added	Scottrade Avail[2]	Fidelity Avail[2]	Schwab Avail[2]	MOM[3]	Performance YTD	1Mo	3Mo	6Mo	12Mo	3Yr Avg	Relative Risk[4]	Exp Ratio	Number Holdings	Redemp Fee?[5]	Ticker Symbol
Category 5 Foreign	1. Vanguard Intl Growth	09/17	Yes	Yes	Yes	60.7	37.4%	2.6%	10.6%	22.0%	28.1%	10.4%	1.41	0.46	133	None	VWIGX
	2. Oakmark International	12/16	NTF	NTF	NTF	59.8	26.7%	4.5%	9.1%	15.8%	34.9%	9.4%	1.53	1.00	85	None	OAKIX
	3. Selected International S	06/17	NTF	NTF	NTF	48.7	31.4%	2.6%	8.4%	17.8%	22.6%	8.1%	1.48	1.30	39	2%30days	SLSSX
Category 4 Small/Growth	1. ☎ Conestoga Small Cap	11/17	NTF	NTF	NTF	59.1	24.0%	6.6%	9.8%	19.2%	30.2%	18.8%	1.45	1.10	49	None	CCASX
	2. Oberweis Micro Cap	11/15	NTF	NTF	NTF	58.2	23.6%	7.8%	10.0%	15.1%	33.1%	18.7%	1.36	1.65	90	1%90days	OBMCX
	3. Baron Discovery	04/17	NTF	NTF	NTF	53.8	31.1%	4.2%	5.3%	17.5%	31.0%	15.5%	1.61	1.35	64	None	BDFFX
Category 3 Small/Value	1. ☎ Zack's Small Cap	11/17	NTF	NTF	NTF	50.6	14.0%	7.9%	9.5%	11.8%	29.3%	14.6%	1.40	1.39	107	2%30days	ZSCCX
	2. Royce Opportunity	06/17	NTF	NTF	NTF	51.1	17.5%	8.5%	8.8%	11.7%	30.6%	11.7%	1.65	1.49	247	1%30days	RYOFX
	3. AllianzGI NFJ Mid-Cap Val	06/17	No	NTF	NTF	48.3	20.7%	3.7%	4.2%	13.7%	30.4%	11.8%	1.12	0.99	103	None	PQNAX
Category 2 Large/Growth	1. Guggenheim S&P 500 Tech	04/17	ETF	ETF	ETF	49.7	25.2%	2.6%	8.4%	12.3%	29.0%	18.1%	1.40	0.40	70	None	RYT
	2. Fidelity OTC	06/17	Yes	NTF	Yes	50.6	30.7%	0.7%	5.8%	15.7%	29.1%	16.5%	1.49	0.81	234	None	FOCPX
	3. Baron Partners	05/17	NTF	NTF	NTF	47.6	30.1%	1.4%	1.3%	16.2%	30.1%	11.5%	1.57	1.35	26	None	BPTRX
Category 1 Large/Value	1. Toreador Core	05/17	NTF	NTF	NTF	44.8	17.0%	5.6%	9.1%	8.7%	26.9%	9.7%	1.22	1.20	97	2%60days	TORLX
	2. Dodge & Cox Stock	12/16	Yes	Yes	Yes	35.2	11.9%	4.0%	4.8%	6.6%	23.9%	9.8%	1.27	0.52	68	None	DODGX
	3. Miller Opportunity	06/17	Yes[10]	Yes[10]	NTF	32.7	19.5%	3.7%	-0.4%	11.5%	21.6%	8.7%	2.15	1.36	35	None	LGOAX[10]
Bond Categories	Vanguard I-T Bond Index [6]	07/17	ETF	ETF	ETF	2.9	3.7%	-0.9%	0.8%	2.6%	-0.5%	3.2%	1.31	0.07	6.5[7]	None	BIV[8]
	Vanguard I-T Bond Index	01/15	ETF	ETF	ETF	2.9	3.7%	-0.9%	0.8%	2.6%	-0.5%	3.2%	1.31	0.07	6.5[7]	None	BIV[8]
	Vanguard S-T Bond Index	07/12	ETF	ETF	ETF	1.7	1.5%	-0.3%	0.4%	1.0%	0.3%	1.4%	0.45	0.07	2.8[7]	None	BSV[9]

Upgrading Footnotes: **[1]** The funds in each risk category are selected (and ranked 1 through 3) primarily based on their momentum scores in late-October, not those shown on this report. The fund ranked third is the one that currently appears most likely to be replaced next. A telephone symbol (☎) next to a fund's name indicates that fund is a new recommendation. See the fund writeups in "MoneyTalk" for more information. **[2]** Fund Availability: NTF means the fund can be bought and sold free of transaction fees as long as you stay within the trading limitations imposed by Scottrade (800-619-7283), Fidelity (800-343-3548), and Schwab (800-435-4000). Policies change frequently, so be sure to verify their accuracy. ETFs trade like stocks and are typically available at all brokers for a modest commission. **[3]** Momentum is a measure of a fund's performance over the past year and is our primary performance evaluation tool. For more, see July2014:p103. **[4]** A 1.0 relative risk score indicates the fund has had the same volatility as the market in general over the past three years. For example, a fund with a score of 1.4 would mean the fund was 1.4 times (40%) more volatile than the market. See June2015:p88. **[5]** Depending on how long you hold this fund, a redemption fee may be applicable when selling (for example, a fee of 1% if you sell within 60 days of purchase). Fees change often and vary from broker to broker, so be sure to check with your broker for the most current information. **[6] Rotating Fund:** This bond recommendation changes periodically based on SMI's Upgrading methodology. The Short-Term and Intermediate-Term Index recommendations shown below that fund are fixed and don't change from month to month. See January2015:p7 for more information. **[7] Duration:** For bond funds, this column shows the average duration of the bonds in the portfolio in years. Typically, the longer the duration, the greater the risk/reward. See Jun2012:p88. **[8]** Those preferring a traditional mutual-fund option can buy VBILX where available, otherwise VBIIX. **[9]** Those preferring a traditional mutual-fund option can buy VBIRX where available, otherwise VBISX. **[10]** At some brokers, the load-waived share class is LMNOX. Read the fund writeup (June:p93) before purchasing.

☎ Changes in our fund recommendations are explained in the MoneyTalk column.

Upgrading: Easy as 1-2-3

Fund Upgrading has long been SMI's most popular Basic Strategy. Whether used in isolation or in combination with SMI's Premium Strategies, Upgrading forms a solid foundation for an investing plan. Upgrading has proven itself over time with market-beating returns over the long haul, and it is easy to implement. This page explains exactly how to set up your own Upgrading portfolio.

"The plans of the diligent lead to profit as surely as haste leads to poverty." Proverbs 21:5

WHY UPGRADE?

SMI offers two primary investing strategies for "basic" members. They are different in philosophy, the amount of attention they require, and the rate of return expected from each. Our preferred investing strategy is called Fund Upgrading, and is based on the idea that if you are willing to regularly monitor your mutual-fund holdings and replace laggards periodically, you can improve your returns. While Upgrading is relatively low-maintenance, it does require you to check your fund holdings each month and replace funds occasionally. If you don't wish to do this yourself, a professionally-managed version of Upgrading is available (visit bit.ly/smifx).

SMI also offers an investing strategy based on index funds called Just-the-Basics (JtB). JtB requires attention only once per year. The returns expected from JtB are lower over time than what we expect (and have received) from Upgrading. JtB makes the most sense for those in 401(k) plans that lack a sufficient number of quality fund options to make successful Upgrading within the plan possible. See the top section of the Basic Strategies page at left for the funds and percentage allocations we recommend for our Just-the-Basics indexing strategy.

WHERE TO OPEN YOUR ACCOUNT

Opening an account with a discount broker that offers a large selection of no-load funds greatly simplifies the Upgrading process. This allows you to quickly and easily buy/sell no-load mutual fund shares without having to open separate accounts at all the various fund organizations. There are several good brokerage choices available. We recommend reading our latest Broker Review (August 2015:Cover article, also available online at bit.ly/smibroker) for details regarding the pros and cons of each broker, as your specific investing needs will largely dictate which broker is best suited to your situation.

401(K) INVESTORS

For a detailed explanation of how to Upgrade within your 401(k) plan, see bit.ly/smi401ktracker. That article also contains ideas on Upgrading in any type of account where your available fund choices are limited.

HOW TO BEGIN STOCK UPGRADING

❶ First determine your stock/bond target allocation by working through the investment temperament quiz online in the "Start Here" section (see the link near the top of the home page on the main navigation bar). For example, Table 1 below provides guidelines for those with an "Explorer" temperament. For more on asset allocations, see Jan2017:p8.

❷ Find the column that matches your stock/bond allocation in Table 2. (If your target falls between two listed columns, split the difference.) Multiply each percentage by the value of your total portfolio amount to calculate the dollar amount to invest in each risk category.

❸ Buying your funds is easy. Look at the recommended funds on the opposite page. In each category, start with the #1 listed recommendation. If it's available at your brokerage (indicated by Yes, NTF, or ETF), buy it. If it's not, continue down the list to the next available fund. Then contact your broker—online or via phone—to buy the fund you've picked.

Let's see how a new subscriber 12 years from retirement with $50,000 to invest and an account at Fidelity would proceed. First, he or she selects the proper stock/bond mix for their situation (let's assume 80/20). Then, from Table 2, finds the percentages for each risk category. Multiplying $50,000 by each percentage yields the dollar amount for each category as shown in Table 3.[1] Looking at the Fidelity column on the Recommended Funds page, the highest-rated Cat. 5 fund available is Vanguard International Growth, the highest-rated Cat. 4 fund available is Conestoga Small Cap, and so on. After doing this for each category, the orders are placed and the stock portion of the Upgrading portfolio is complete!

From then on, it's just a matter of checking the Basic Strategies page each month. When an owned fund is *removed* from this page (not when it merely shifts out of the #1 ranking), you should immediately sell that fund and invest the proceeds in the highest-ranked fund in the same risk category that is available at your broker.

❶ PICK YOUR ALLOCATION

Seasons of Life	Stocks	Bonds
15+ years until retirement	100%	0%
10-15 years until retirement	80%	20%
5-10 years until retirement	70%	30%
5 years or less until retirement	60%	40%
Early retirement years	50%	50%
Later retirement years	30%	70%

Note: These are SMI's recommendations for those with an "Explorer" temperament. See Step ❶ in the text for information on our investment temperament quiz. You may want to fine-tune the above percentages to suit your personal approach to risk-taking.

❷ FIND YOUR PORTFOLIO MIX

Portion of Portfolio Allocated to Stocks:	**100%**	**80%**	**60%**	**40%**
Portion of Portfolio Allocated to Bonds:	**None**	**20%**	**40%**	**60%**
Stock Cat. 5: Foreign Stocks	20%	16%	12%	8%
Stock Cat. 4: Small Companies /Growth	20%	16%	12%	8%
Stock Cat. 3: Small Companies /Value Strategy	20%	16%	12%	8%
Stock Cat. 2: Large Companies /Growth	20%	16%	12%	8%
Stock Cat. 1: Large Companies /Value Strategy	20%	16%	12%	8%
Bond Cat. 3: "Rotating" Bond Fund	None	10%	20%	30%
Bond Cat. 2: Intermediate-Term Bond Fund	None	5%	10%	15%
Bond Cat. 1: Short-Term Bond Fund	None	5%	10%	15%

❸ BUY YOUR FUNDS

Example uses an 80/20 mix between stocks and bonds		Dollars	Invest In Funds
Stock Cat. 5: Foreign	16%	$8,000	Vanguard Intl Growth
Stock Cat. 4: Small/Growth	16%	$8,000	Conestoga Small Cap
Stock Cat. 3: Small/Value	16%	$8,000	Zack's Small Cap
Stock Cat. 2: Large/Growth	16%	$8,000	Guggenheim S&P 500 Tech
Stock Cat. 1: Large/Value	16%	$8,000	Toreador Core
"Rotating" Bond Fund	10%	$5,000	Vanguard I.T. Bond Index
Intermediate-Term Bond Fund	5%	$2,500	Vanguard I.T. Bond Index
Short-Term Bond Fund	5%	$2,500	Vanguard S.T. Bond Index
Total	100%	$50,000	

BOND UPGRADING

Your bond allocation is divided among three funds as seen in Table 2. One-half of that is invested in the rotating Upgrading selection, which is reviewed monthly and changes from time to time. The other half is divided evenly between short-term and intermediate-term index bond funds, which are permanent holdings. For more on why SMI approaches bond investing in this way, see "Introducing an Upgrading Approach to Bond Investing that Outperforms the Bond Market" (bit.ly/smibondupgrading).

[1] Rounding off to the nearest hundred is fine. As time goes by, your portfolio will gradually move away from these starting percentages as some funds perform better than others. This will be fixed once a year when you "rebalance" back to your desired portfolio mix (see Jan2017:p8).

MONEYTALK

STOCK UPGRADING — NEW FUND RECOMMENDATIONS

[We choose our recommended funds with the hope they will be held for at least 12 months and therefore qualify for long-term capital gains tax treatment. Nevertheless, we suggest a fund change when a recommended fund's performance falls below the threshold of our mechanical guidelines. Our guidelines provide objective criteria for making the decision as to when to "upgrade" to a better-performing fund. When a fund no longer meets our performance guidelines, we suggest you sell it even if the 12-month holding period hasn't been met. However, a "$" symbol following the name of the fund being sold lets you know that we still think well of the fund and its management and you might elect to continue holding the fund for a month or two to achieve a tax benefit or to save on transaction or redemption fees.]

◆ **In the Small/Growth group, William Blair Small Cap Growth (WBSNX, 5/2017) is being replaced.$** This fund earned +10% in the first five months it was recommended (May-September). That was significantly better than the +7.8% gain of the average fund in our small/growth group. But it has fallen down the rankings in October and is now below the quartile, requiring it to be replaced.

• **Conestoga Small Cap (CCASX) is being added.[1]** Conestoga built its reputation by holding up better than most of its peers in falling markets. That hardly makes it a wallflower—it sizzled in the strong 2013 market and has flourished again this year. But it's reassuring to know that management pays attention to risk and has seen that translate into above-average performance in past downturns.

◆ **In the Small/Value group, Fidelity Low-Priced Stock (FLPSX, 9/2017) is being replaced.$** This recommendation has also performed well, gaining +4.4% in less than two months. But the small-company segment of the stock market has been so hot recently that the fund has fallen on a relative basis within its peer group despite solid absolute gains.

• **Zack's Small Cap Core (ZSCCX) is being added.[1]** This recommendation is as close to being a "growth" fund as one can get while still remaining in our value categories. Morningstar actually categorizes it as a "blend," meaning it falls *between* growth and value, having attributes of both styles. SMI lumps "blend" funds into our value categories, making them a natural go-to when the market is strong and growth stocks are in favor.

Note: These fund write-ups have been condensed due to space constraints. SMI members can view the expanded write-ups online at https://sminow.com/nov17fw. ◆

LEVEL 2 / CONTINUED FROM PAGE 167:

WILL THE BEAR'S BITE BE ESPECIALLY PAINFUL FOR PASSIVE INVESTORS?

rich valuations. For example, among the current recommended funds used in SMI's Stock Upgrading strategy, at the end of June, Baron Discovery had 7.6% of its portfolio in cash, while Selected International had a whopping 22.3% cash allocation!

Keeping some assets in cash, and having the freedom to shift more to cash at times of (or in anticipation of) market stress, can help actively managed funds better navigate declining markets. Of course, how well actively managed funds weather a downturn also depends on the *nature* of the particular bear market.

As the following table shows, Stock Upgrading (the SMI strategy that relies most heavily on actively managed funds) suffered less-severe losses than either the S&P 500 index or SMI's index-fund strategy (Just-the-Basics), in the last two bear markets. Upgrading's performance advantage was far greater in 2000-2002, due to that bear's longer length (which allowed Upgrading more time to align with the longer-term trend) and the fact that some types of stocks held up better than others. In contrast, during the 2008-2009 bear market, virtually all stocks fell in unison, leaving few options (other than cash) for active managers to avoid the devastation.

SMI Strategy	3/2000-9/2002	10/2007-2/2009
S&P 500	-38.3%	-50.2%
Just-Basics	-45.1%	-52.9%
Upgrading	-25.7%	-50.0%
DAA*	+19.6%	-1.4%

* Back tested results; DAA had not yet been introduced during these prior bear markets.

2. The market's narrowing breadth may signal pain for indexers. Breadth refers to how many stocks are participating in the market's gains or losses. This bull market's relentless march higher has been disproportionally driven by a small number of stocks the past few years—specifically Facebook, Apple, Amazon, Netflix, Microsoft, and Google.

The S&P 500 index is the most popular index among passive investors. As of August, FactSet reported that one-seventh of all ETF assets tracked the S&P 500. Because the S&P 500 is a *cap-weighted* index (meaning each stock's influence on the index depends on its *size*, as measured by total market value) this handful of large, yet still rapidly growing, stocks have an outsized influence on the index's performance.

Goldman Sachs reported in June that Facebook, Apple, Amazon, Microsoft, and Google (Alphabet) collectively made up about 13% of the value of the S&P 500. However, their strong performance had driven 40% of the S&P 500 index's growth for the year to that point, adding some $660 billion in value. While most passive investors likely believe their returns come from a large, well-diversified collection of stocks, the reality is their returns have become increasingly driven by a relative handful that have grown disproportionately within that index.

The concern for index-fund investors, then, is simply this: When the market changes direction, those high-flying stocks may experience significant outflows, taking their value and the value of S&P 500 index funds down disproportionately. It's common for the fastest-growing stocks during a bull market to decline the most during the subsequent bear market. The difference this time is millions of new passive investors may exacerbate this "normal" selling as they see the value of their indexed holdings plummet, creating a self-perpetuating, vicious cycle.

What does it mean for SMI investors?

Here are a few thoughts to consider, depending on which of SMI's three core strategies you use.

• **Just-the-Basics.** As the above table shows, JtB fell right along with the market during both bear markets. In fact, its small-company and foreign stock holdings lost a little more than the S&P 500 during those periods, which isn't unusual

[1]For more on this fund, visit www.morningstar.com.

during stock-market declines.

JtB is ideally suited for investors with money in taxable accounts, and market conditions don't change that fact. JtB investors with a long-term perspective may want to continue on that path, but all JtB investors would be wise to periodically consider their risk tolerance and mix of strategies. If nothing else, this will help ensure that their stock/bond allocation within JtB remains appropriate.[1]

• **Stock Upgrading.** As noted earlier, Upgrading helped SMI members weather the past two bear markets, with a substantial performance benefit during 2000-2002. Just as no one knows when the next bear market will arrive, no one knows how severe it will be or the exact shape it will take. Upgraders with a long time horizon may be content to stay the course, understanding that the strategy may spare them *some* of the agony a bear will bring. For those with shorter horizons or weaker stomachs, this would be an appropriate time to consider diversifying strategies, adding an allocation to DAA to build in some downside protection.

• **Dynamic Asset Allocation.** Going all-in with DAA would provide the best protection against a bear market, as the table shows. However, moving money from Upgrading to DAA may also mean missing out on some future gains should the bull market continue for an extended period.

If you *do* decide to focus on DAA, you will still need to manage your expectations. Remember that DAA, like Stock Upgrading, is a trend-following strategy. As such, it won't avoid all losses at the beginning of a bear market. For example, when the market lost -4.2% in November of 2007, DAA investors would still have had two-thirds of their portfolio invested in stocks and would have had losses of -3.1% that month. However, DAA shifted out of U.S. stocks the very next month and stayed out through the remainder of that bear market, saving investors from tremendous losses.[2]

Note that this article isn't meant to suggest that SMI believes a bear market is imminent. We have long held the position that the future direction of the market is unknowable. That said, as we have been reminding readers lately, no bull market lasts forever. Eventually this one will end, as they all do, so manage your expectations accordingly. ◆

LEVEL 3 / CONTINUED FROM PAGE 168:

3RD QUARTER REPORT: LET THE GOOD TIMES ROLL

If not, consider allocating a portion of your portfolio to SMI's high-risk, high-reward Sector Rotation strategy.

50/40/10

This portfolio refers to the specific blend of SMI strategies—50% DAA, 40% Upgrading, 10% Sector Rotation—detailed in our May 2014 cover article, *Higher Returns With Less Risk: The Best Combinations of SMI's Most Popular Strategies*. It's a great example of the type of diversified portfolio we encourage most SMI readers to consider.[3] While the markets have been unusually calm so far in 2017, history vividly illustrates that the stock market can shift suddenly from rewarding those who take greater risks to punishing them, so a blend of higher-risk and lower-risk strategies can help smooth your long-term path.

Given the success of the three individual component strategies during the third quarter, it's no surprise that a 50/40/10 portfolio outperformed the broad market, +5.8% to +4.6%. On a year-to-date basis, 50/40/10 is beating the market +14.7% to +13.7%—*while also providing significant downside risk protection.* Gathering a large percentage of the market's gains during rising markets while avoiding even a portion of its losses during falling markets is a recipe not only for superior long-term returns, but provides the type of emotional stability that is so important to sustained investing success. ◆

LEVEL 4 / CONTINUED FROM PAGE 169:

BRIDGING THE GAP: COVERING WHAT MEDICARE DOESN'T PAY

Medicare deductibles and coinsurance costs (similar to what Medigap policies cover for enrollees of Original Medicare), as well as vision, hearing, and dental benefits. Some Advantage plans also include a Medicare Part D prescription benefit. And you can't be turned down for Medicare Advantage coverage if you have a pre-existing condition.

All this comes at a remarkably low monthly cost. The current average monthly premium for Advantage plans is only $36, according to the Kaiser Family Foundation. In fact, some plans make such efficient use of the subsidies they get from Medicare that they're able to set their monthly premium as low as $0.

ANNUAL STATEMENT OF OWNERSHIP, MANAGEMENT, AND CIRCULATION

(Required by 39 U.S.C. 3685) **1.** Publication title: Sound Mind Investing. **2.** Publication number 006-344 **3.** Filing date: 9/30/2017. **4.** Issue frequency: Monthly. **5.** Number issues published annually: 12. **6.** Annual subscription price: $99.50. **7.** Complete mailing address of known office of publication: Sound Mind Investing, 9700 Park Plaza Avenue, Suite 203, Louisville, Kentucky 40241. Contact person: Todd Pilbean. Telephone: 502-426-6284. **8.** Complete mailing address of headquarters of publisher: Same as #7. **9.** Full names and complete mailing address of: Publisher and Editor Austin C. Pryor, Jr., Managing Editor Mark Biller, address same as #7. **10.** Owner: Austin C. Pryor, Jr., 90%, Same as #7; Susan Pryor, 10%, Same as #7. **11.** Known bondholders, mortgages, and other security holders owning or holding 1% or more of total amount of bonds, mortgages or other securities: None. **12.** Tax status: Has not changed during preceding 12 months. **13.** Publication title: Sound Mind Investing. **14.** Issue date for circulation data below: September 2017. **15.** Extent and nature of circulation: [a] Total number of copies (net press run): Average number copies each issue during preceding 12 months, 7,233; Number copies of single issue published nearest to filing date, 7,200. [b] Paid circulation: (1) Mailed outside county, paid subscriptions: Average number copies, 6,952; Recent issue, 6,958. (2) Mailed in county, paid subscriptions: Average number copies, 26; Recent issue, 26. (3) Paid distribution outside USPS: Average number copies, -0-; Recent issue, -0-. (4) Paid distribution other classes mailed through USPS: Average number copies, 1; Recent issue, 1. [c] Total paid distribution: Average number copies, 6,979; Recent issue, 6,985. [d] Free or nominal rate distribution: (1) Free or nominal rate, outside county: Average number copies, 96; Recent issue, 97. (2) Free or nominal rate, inside county: Average number copies, 19; Recent issue, 19. (3) Free or nominal rate copies mailed at other classes through USPS: Average number copies, -0-; Recent issue, -0-. (4) Free or nominal rate distribution outside the mail: Average number copies, -0-; Recent issue, -0-. [e] Total free or nominal rate distribution: Average number copies, 115; Recent issue, 116. [f] Total distribution: Average number copies, 7,094; Recent issue, 7,101. [g] Copies not distributed: Average number copies, 282; Recent issue, 242. [h] Total: Average number copies each issue during preceding 12 months, 7,376; Recent issue, 7,343. [i] Percent paid: Average number copies, 98.4%; Recent issue, 98.4%. **16.** This statement of ownership will be printed in the November 2017 issue. **17.** Signature and title of business manager: Todd Pilbean / Director of Operations.

[1]Take SMI's risk tolerance assessment at bit.ly/SMIQuiz [2]Read more about DAA's 2007-2009 bear market performance at bit.ly/SMIdaa2007-09. [3]Blending multiple strategies adds complexity. Some members might want to use an automated approach. See bit.ly/SMI504010.

MONEYTALK

About 60% of Advantage users are in zero-premium plans.[1]

But while Medicare Advantage premiums are attractive, Advantage policyholders will likely face out-of-pocket expenses (i.e., expenses not reimbursed by insurance) that are *potentially* higher than those faced by enrollees who choose Original Medicare plus Medigap. That liability is not open-ended, however. Advantage plans are required by law to have an annual out-of-pocket limit—typically $3,000 to $4,000. Once the limit is reached, covered expenses will be paid in full by the plan.

Medicare Advantage users can choose from an array of health-care delivery options, some of which limit certain choices. Most Advantage plans use an HMO (health maintenance organization) approach, while others use a PPO (preferred provider organization) structure (see Table A). Other plans are based on a Private Fee-For-Service model or are centered around the use of a personal Medical Savings Account (MSA). There even are Special Needs Plans (SNP) for people with particular health problems.

Making the Original/Advantage decision

You won't find a simple solution to figuring out whether to go with Medicare Advantage or Original Medicare, nor is there an easy template for selecting a Medigap plan. Your choices depend on your current (and anticipated) health needs, your budget for premiums and out-of-pocket expenses, and how comfortable (or uncomfortable) you are being exposed to the "gaps" in Medicare coverage.

The cheapest approach to Original Medicare—when it comes to premiums—is to forego any Medigap supplement. About half of enrollees in Original Medicare go this route, choosing not to pay a Medigap premium. While Part A premiums are paid for by the Medicare payroll tax, enrollees still must pay Part B premiums (commonly deducted from a user's monthly Social Security retirement benefit).

However, choosing Original Medicare but failing to buy a Medigap policy carries financial risk. You'll be responsible for paying the Part A deductible ($1,316 each time you are hospitalized[2]) plus 20% coinsurance for Part B medical expenses. These costs typically are paid in full by Medigap policies (see Table B).

Further, because Medigap supplemental policies cover extended hospital stays (beyond the 60 days Medicare fully pays for) plus in some cases a limited number of days in a skilled nursing facility, they can help meet the cost of longer-term care, something for which Medicare itself was never designed. (Medigap policies, however, do not pay for assisted living, Alzheimer's care, custodial care, or adult daycare.)

Rather than forego Medigap, a wiser approach for people unwilling to pay a hefty premium for a supplemental policy is to move from Original Medicare to a low- or no-premium Medicare Advantage plan. Doing so could significantly reduce one's financial exposure at little or no additional monthly cost.

Where to turn for help

The Medicare website[3] offers a Plan Finder that lists the plans available in your area, along with price ranges for premiums and estimates of potential out-of-pocket outlays. In addition, the Centers for Medicare and Medicaid Services offers a free 50-page guide online titled "Choosing a Medigap Policy." Other sources of information include PlanPrescriber.com, which offers Medicare Advantage and Medigap policy comparisons. WeissMedigap.com sells detailed information (for $99) that compares Medigap plans available within your ZIP code. ◆

TABLE A: COMPARING YOUR MEDICARE OPTIONS

	Original Medicare + Medigap	Medicare Advantage HMO	Medicare Advantage PPO
What do I pay (per person)?	Part B premium + Medigap premium*	Part B premium + plan premium (if any) + deductibles/copays/coinsurance**	Part B premium + plan premium (if any) + deductibles/copays/coinsurance**
Choice of doctor?	Yes, anyone who accepts Medicare	No, must choose in-network provider	Yes, but may pay more for out-of-network
Referral required for specialist?	No, unless you have Medicare SELECT	In most cases	No, but may pay more for out-of-network
Out-of-pocket limit?	Applicable only for Plans K & L	Yes, varies by plan	Yes, varies by plan

*A few Medigap plans require deductibles, co-pays, and/or coinsurance payments.
**Varies by plan. Average out-of-pocket limit is $3,000 to $4,000. Once limit is reached, services are covered in full.

TABLE B: MEDIGAP PLANS

Medigap Policy Pays For:	A	B	C	D	F*	G	K**	L**	M	N
Part A coinsurance & hospital costs up to 365 days after Medicare benefits are used up	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%
Part A hospice care coinsurance or copayment	100%	100%	100%	100%	100%	100%	50%	75%	100%	100%
Part A skilled nursing facility (SNF) coinsurance	No	No	100%	100%	100%	100%	50%	75%	100%	100%
Part A deductible	No	100%	100%	100%	100%	100%	50%	75%	50%	100%
Part B coinsurance or copayment	100%	100%	100%	100%	100%	100%	50%	75%	100%	Yes***
Part B deductible	No	No	100%	No	100%	No	No	No	No	No
Part B excess (e.g., services exceeding Medicare-approved price)	No	No	No	No	100%	100%	No	No	No	No

*Benefits under high-deductible version of Plan F begin after $2,200 deductible. **Out-of-pocket limits for plans K & L are $5,120& $2,560 respectively. Once limit is reached, services are covered in full. ***Plan N has an up-to-$20 co-pay for office visits and an up-to-$50 co-pay for emergency room visits.

[1]However, enrollees must also pay the monthly Part B premium. [2]Technically, the deductible is for "each benefit period"— begining on the day of admission and continuing through 60 days after release. [3]www.medicare.gov

PREMIUM STRATEGIES

The strategies described below are available to those with an SMI Premium web membership. These strategies can be used in combination with—or in place of—our Just-the Basics and Upgrading portfolios. They have special characteristics that could make them desirable depending upon your individual goals, risk tolerance, and tax bracket. You can learn more about each strategy in the Premium section of the SMI website.

DYNAMIC ASSET ALLOCATION

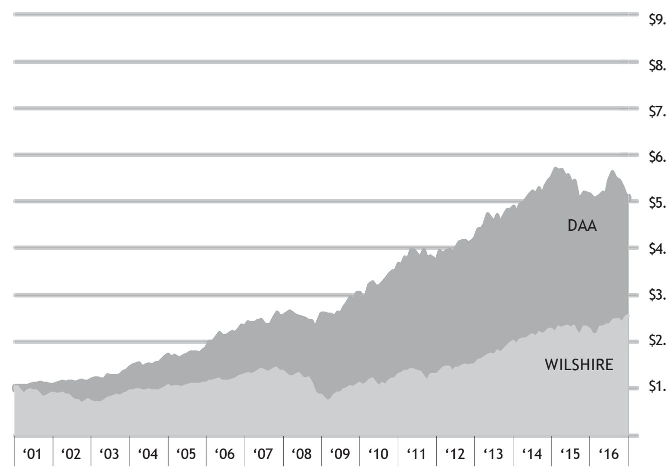
Overview

This is a stand-alone strategy that can be used in combination with (or in place of) SMI's basic strategies. DAA is designed to help you share in some of a bull market's gains, while minimizing or even preventing losses during bear markets. It's a low-volatility strategy that nonetheless has generated impressive back-tested results over the long term. DAA involves rotating among six assets classes—U.S. stocks, foreign stocks, gold, real estate, bonds, and cash. Only three are held at any one time.

Who Should Consider This Strategy

Anyone, but especially investors who are more concerned with avoiding major losses during bear markets than they are with capital growth during bull markets. **Pros:** Excellent downside protection during bear markets, reflected in a very low worst-case result and relative-risk score. Great long-term track record. **Cons:** Subject to short-term whipsaws. Lags the market in up years. Making trades promptly and concentrating entire portfolio in only three asset classes can be emotionally challenging.

Dynamic Asset Allocation vs Wilshire 5000
Growth of $1 Jan 2001 - Dec 2016



Strategy	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	Avg[1]	Worst 12[1]	Rel Risk[1]
Dynamic Asset Allocation	4.0%	10.4%	22.4%	19.3%	8.6%	25.7%	10.1%	1.3%	17.6%	20.3%	1.4%	13.9%	16.2%	13.0%	-6.8%	-0.5%	10.7%	-13.7%	0.64
Wilshire 5000	-11.0%	-20.9%	31.6%	12.5%	6.4%	15.8%	5.6%	-37.2%	28.3%	17.2%	1.0%	16.1%	33.1%	12.7%	0.7%	13.4%	6.1%	-43.3%	1.00

SECTOR ROTATION

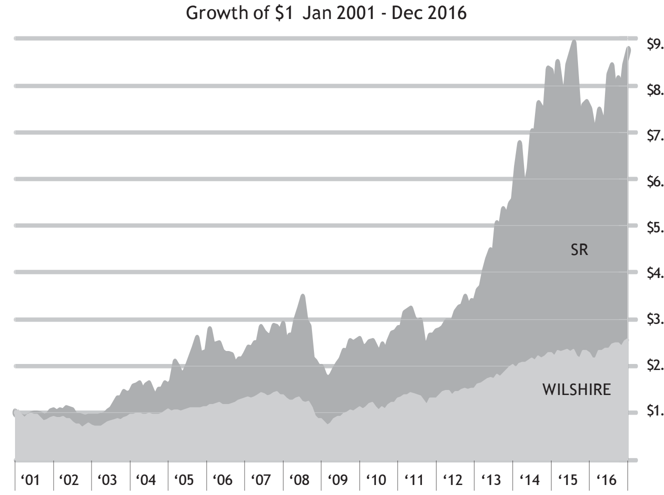
Overview

This high-risk strategy involves investing in a single special-purpose fund that focuses on a specific sector (such as biotech, energy, or financial services). Because these stock funds invest in a narrow slice of the economy, they carry a higher degree of risk. Only one fund, selected based on having superior momentum relative to other sector options, is held at a time. The sector-fund recommendations in this strategy are designed to be used in combination with Just-the-Basics, Fund Upgrading, or DAA (or a combination of these) up to a maximum of 20% of the stock allocation. While the performance peaks and valleys of Sector Rotation have been higher and lower than all other SMI strategies, it's a strategy that has generated especially impressive long-term returns.

Who Should Consider This Strategy

Experienced investors willing to concentrate an investment in a single sector of the economy. **Pros:** Very attractive long-term returns. **Cons:** Much greater month-to-month volatility and relative risk with dramatic short-term loss potential.

Sector Rotation vs Wilshire 5000
Growth of $1 Jan 2001 - Dec 2016



Strategy	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	Avg[1]	Worst 12[1]	Rel Risk[1]
Sector Rotation	3.7%	-13.1%	54.4%	12.6%	46.1%	-1.9%	28.1%	-31.5%	30.5%	9.1%	-3.2%	23.3%	65.7%	49.9%	-9.7%	16.8%	14.5%	-38.6%	1.66
Wilshire 5000	-11.0%	-20.9%	31.6%	12.5%	6.4%	15.8%	5.6%	-37.2%	28.3%	17.2%	1.0%	16.1%	33.1%	12.7%	0.7%	13.4%	6.1%	-43.3%	1.00

[1]The three data points on the far right in each of the two tables are for the Jan2001-Dec2016 period. "Avg" represents the average annualized return from 2001-2016. "Worst12" represents the worst investor experience over 169 rolling 12-month periods from 2001-2016.

PERIODICALS POSTAGE
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Dated Investment Material
Please Do Not Delay!

PERFORMANCE DATA

SOUND MIND INVESTING MODEL PORTFOLIOS • DATA THROUGH SEPTEMBER 30, 2017

BASIC STRATEGIES

	Year to Date	1 Month	3 Months	12 Months	3 Yrs Annual	5 Yrs Annual	10 Yrs Annual	15 Yrs Annual
U.S. Stock Market[1]	13.7%	2.4%	4.6%	18.9%	11.0%	14.3%	7.6%	10.5%
Just-the-Basics[2]	15.0%	2.8%	5.0%	19.0%	9.6%	13.0%	6.8%	10.7%
Stock Upgrading[3]	13.8%	4.0%	5.7%	18.4%	9.1%	12.8%	6.4%	11.5%
U.S. Bond Market[4]	3.1%	-0.5%	0.7%	-0.2%	2.5%	1.9%	4.1%	4.1%
Bond Upgrading[5]	2.4%	-0.7%	0.7%	0.8%	2.6%	3.1%	6.4%	6.5%

PREMIUM STRATEGIES

	Year to Date	1 Month	3 Months	12 Months	3 Yrs Annual	5 Yrs Annual	10 Yrs Annual	15 Yrs Annual
DAA[6]	11.1%	0.5%	3.0%	4.3%	3.7%	6.6%	8.6%	11.4%
Sector Rotation[7]	36.1%	8.5%	19.6%	46.5%	16.8%	28.2%	15.5%	18.9%
50-40-10 Blend[8]	14.7%	2.7%	5.8%	13.9%	7.3%	11.4%	8.9%	12.6%

Notes: Transaction costs and redemption fees—which vary by broker and fund—are not included. • [1] Based on the float-adjusted Wilshire 5000 Total Return index, the broadest measure of the U.S. stock market. • [2] Calculated assuming account rebalancing at the beginning of each year with 40% of the stock allocation invested in the Vanguard S&P 500 (VOO), 40% in Extended Market (VXF), and 20% in Total International Stock (VXUS). • [3] For a 100% stock portfolio, assuming the portfolio allocation for each risk category was divided evenly among all the recommended funds. • [4] Based on Barclay's U.S. Aggregate Bond Index, the broadest measure of the U.S. bond market. • [5] For a 100% bond portfolio, assuming 25% of the portfolio was invested in Vanguard I-T Bond Index (BIV), 25% in Vanguard S-T Bond Index (BSV), and 50% in the rotating recommended bond fund. The results prior to January 2015 are hypothetical, calculated from backtesting the strategy following a mechanical rules-based system. • [6] The results prior to January 2013 are hypothetical, calculated from backtesting the strategy following a mechanical rules-based system. • [7] The results prior to November 2003 are hypothetical, calculated from backtesting the strategy following a mechanical rules-based system. • [8] For a portfolio allocated 50% to DAA, 40% to Stock Upgrading, and 10% to Sector Rotation. See the May 2014 cover article for details. The results prior to January 2013 are hypothetical, calculated from backtesting the strategy following a mechanical rules-based system.

THE SOUND MIND INVESTING MUTUAL FUND (SMIFX)

Current Returns as of 9/30/2017	Year to Date	1 Month	3 Months	12 Months	3 Year Annual	5 Year Annual	10 Year Annual
SMIFX	12.65%	3.19%	6.13%	15.94%	6.75%	11.04%	5.11%
Wilshire 5000	13.73%	2.41%	4.59%	18.89%	10.96%	14.27%	7.61%
S&P 500	14.24%	2.06%	4.48%	18.61%	10.81%	14.22%	7.44%

Quarterly Returns as of 9/30/2017	Year to Date	1 Month	3 Months	12 Months	3 Year Annual	5 Year Annual	10 Year Annual
SMIFX	12.65%	3.19%	6.13%	15.94%	6.75%	11.04%	5.11%
Wilshire 5000	13.73%	2.41%	4.59%	18.89%	10.96%	14.27%	7.61%
S&P 500	14.24%	2.06%	4.48%	18.61%	10.81%	14.22%	7.44%

Total/Gross expense ratio: 1.97% as of 2/28/17 (includes expenses of underlying funds)
Adjusted expense ratio: 1.15% as of 2/28/17 (excludes expenses of underlying funds)

Notes: *The performance data quoted represent past performance, and past performance is not a guarantee of future results. Investment return and principal value of an investment will fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original cost. Current performance may be lower or higher than the performance information quoted.* • ***You should carefully consider the investment objectives, risks, fees, charges and expenses of the Funds before investing. The prospectus contains this and other information about the Funds. To obtain a prospectus or performance information current to the nearest month end, call 1-877-764-3863 or visit www.smifund.com. Read the prospectus carefully before investing.*** • Because the SMI Funds invest in other mutual funds, they will bear their share of the fees and expenses of the underlying funds in addition to the fees and expenses payable directly to the SMI Funds. As a result, you'll pay higher total expenses than you would investing in the underlying funds directly. • Returns shown include reinvestment of dividends and capital gains. The Wilshire 5000 index represents the broadest index for the U.S. equity market. The S&P 500 Index is an unmanaged index commonly used to measure the performance of U.S. stocks. You cannot invest directly in an index. • The Sound Mind Investing Funds are distributed by Unified Financial Securities (member FINRA).

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