CELEBRATING 30 YEARS OF OFFERING BIBLICALLY BASED FINANCIAL COUNSEL
30 years

VOLUME 31 ◆ NUMBER 2

FEBRUARY 2020

SoundMindInvesting®
Financial Wisdom for Living Well
WWW.SOUNDMINDINVESTING.COM

The Core Building Blocks of Successful Investing

It's appropriate at times to step back from the details of your investing activities and assess the big picture. Whether you're a market-tested veteran or new reader putting together a plan for the first time, foundational principles are worth reviewing. And, as you get older and navigate changes in your circumstances, it's wise to periodically re-evaluate—and perhaps tweak—your long-term investing approach in light of those principles. We hope this guide will help.

by Austin Pryor and Mark Biller

Investing is not for the faint of heart. Because it always involves an element of risk, it's an uncertain activity that often feels uncomfortable. Just think back on recent history.

After reaching a new high in September 2018, the market sold off, falling nearly 20% to end the year in the red. If investors thought the carnage would continue into the new year, they could be forgiven. After all, many market watchers believed the bull market had gotten a little long in the tooth, and everyone knows good times don't last forever. But the market quickly found its footing, hitting fresh highs by the spring of 2019 and ending the year with huge gains.

Now think back even further, to 2016. At first glance, that looks like a wonderful year to have had money in the market. The S&P 500 tallied a 12% gain. However, as is often the case, the path leading to that result was far from smooth.

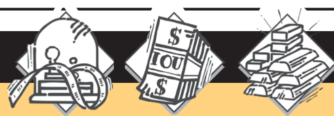
In late June of that year, UK voters surprised the world by opting to leave the European Union ("Brexit"), sending markets reeling. That turmoil was followed by Donald Trump's surprise election in November, which took Dow futures down nearly 800 points. While the market quickly recovered from both surprises, the temporary downward moves they created took a toll on many investors' emotions.

The field of behavioral economics suggests that investors suffer the pain of losses *twice* as acutely as they feel the joy of gains. So, while the market's ups and downs may offset each other financially, they don't necessarily offset each other *emotionally*. Instead, the sharp down days do "double damage"—the corresponding up days only offset half the effect. The market may go sideways, but investor sentiment falls nonetheless.

Unfortunately, you can't control the stock market. But there are many aspects of investing you *can* control. Focusing on the things you can control is an effective counter-weight to concerns about the market (or the economy, or the Middle East, or the next election, etc.).

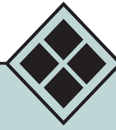
We thought it would be helpful to step back and review the core building blocks of successful investing. Newer readers will surely benefit from a quick survey of these core principles. Seasoned investors should benefit as well—it's all too easy to get bogged down by increasing layers of complexity as the years pass. Even if you've been at this *(continued on page 19)*

IN THIS ISSUE



18 Editorial / How To Keep Dancing With One Eye on the Door
22 Level 1 / Making Ends Meet: Essentials for Successful Budgeting
23 Level 2 / Investing as a Couple
24 Level 3 / 2019 Year In Review: Strong Markets Lead to New Portfolio Highs
25 Level 4 / The New Law of the Land on RMDs, IRA Contributions, and More
26 Basic Strategies **27 Upgrading: Easy as 1-2-3**
28 New Stock Fund Recommendations **31 Premium Strategies** **32 Performance Data**

"FOR GOD HAS NOT GIVEN US THE SPIRIT OF FEAR BUT OF POWER, AND OF LOVE, AND OF A SOUND MIND."



EDITORIAL

How To Keep Dancing With One Eye On The Door

"When the music stops, in terms of liquidity, things will be complicated. But as long as the music is playing, you've got to get up and dance. We're still dancing." – Chuck Prince, ex-CEO of Citigroup, July 2007

There seems to be something about market highs that makes people want to dance. Or at least talk about dancing.

Twenty years ago, near the end of the dot-com stock market bubble, Warren Buffett likened the state of the market to Cinderella's Ball in his annual shareholder letter. He wrote that investors—despite knowing that "overstaying the festivities...will eventually bring on pumpkins and mice"—nonetheless refused to leave the party until just seconds before midnight. He concluded, "There's a problem, though: They are dancing in a room in which the clocks have no hands."

Fast forward to the period just prior to the housing bubble bursting in 2007 and we find the quote atop this article. In words that sound eerily familiar to today's Fed-liquidity driven market, then-Citigroup CEO Chuck Prince uttered his infamous explanation of why his bank continued to lend aggressively despite obviously risky conditions. It didn't age well: just four months later, Prince was forced to resign because of massive losses from the bank's mortgage holdings. Within a year, the whole global financial system would be engulfed in the flames of the subprime mortgage crisis.

More recently, the head of the world's largest hedge fund started feeling that familiar beat. Here's Ray Dalio, July 2017:

> "For the last nine years, central banks drove interest rates to nil and pumped money into the system creating favorable carries and abundant cash.... That era is ending.
>
> "[The central bankers will now] try to tighten at paces that are exactly right in order to keep growth and inflation neither too hot nor too cold, until they don't get it right and we have our next downturn. Recognizing that, our responsibility now is to *keep dancing but closer to the exit* and with a sharp eye on the tea leaves."

Dalio was exactly right. As 2018 drew to a close, the Fed had taken eight baby steps toward higher, normalized interest rates. The ninth hike, in December 2018, would prove too much, sparking an immediate stock market correction of nearly –20% and intensifying concern over a global economic recession that has only recently begun to abate—as a direct result of the Fed reverting to spiking the punchbowl!

These quotes illustrate how market risks can rise to a point where it becomes uncomfortable to continue investing, even for top professionals. A few, like Buffett, simply refuse to play in that environment and wait it out. That's easier to do when you're already a billionaire; it's not a practical option for most investors. Others, like Prince in 2007, ignore the growing risks and carry on unphased. While history looks unkindly on Prince, this is exactly what many index-fund investors are doing today, whether they realize it or not.

The last option is to follow Dalio's approach: continue to invest, but make adjustments to account for the higher-risk environment. Sounds great, but how should a person actually go about doing that?

SMI's approach to "dancing with one eye on the door" begins with the underlying construction of our strategies. All of them, other than Just-the-Basics, are *trend-following* strategies.[1] This means we can have confidence they will never stay on the wrong side of the market's dominant trend for long. When the market is moving sharply higher, as it did last year, SMI's strategies will keep us dancing. But when the market weakens, they will force us to become more conservative (and in some cases, exit stocks altogether).

The past 18 months provide an extreme illustration of this concept in action. When the market dropped sharply at the end of 2018, our strategies responded by rapidly becoming more conservative. As we discuss on page 24, that shift "cost" us additional gains last year, because the correction didn't morph into a full-blown bear market—this time. If it had, our strategies were already positioned to stop the bleeding. When the market trend abruptly shifted higher, our strategies followed suit and still managed to post strong gains in 2019.

The most important step to take as market risk increases is to make sure your blend of SMI's strategies (and overall portfolio stock/bond allocations) are appropriate. If they are, you can continue investing with confidence, knowing your portfolio won't stay on the wrong side of the market's trend for long. Given that no one ever knows what the market will do next, that's reassuring. ◆

MARK BILLER
EXECUTIVE EDITOR

NECESSARY CAUTIONS
It should not be assumed that all investment recommendations will necessarily be profitable. The information published in SMI is compiled from sources believed to be correct, but no warranty as to accuracy is made. SMI is not responsible for any errors or omissions. The counsel given herein is not a substitute for personalized legal or financial planning advice.

CONTACTING US
Correspondence can be emailed to SMI at help@soundmindinvesting.com. Our toll-free Reader Services line (877-736-3764) is available for handling clerical matters such as subscriptions, billings, newsletters not received, and changes of address. Please be advised, however, that the SMI staff is not trained in matters of personal counseling and it is our policy that they not attempt to do so over the phone. If our staff is busy when you call, you may leave your information on our secure answering system.

COPYRIGHT
No part of this newsletter may be reproduced in any fashion without the prior written consent of SMI. © February 2020 by SMI, LLC. All rights are reserved.

POSTMASTER
Sound Mind Investing is published monthly by Sound Mind Investing, 9700 Park Plaza Ave Ste 202, Louisville, KY 40241-2287. Periodicals postage paid at Louisville, Kentucky USPS (006344). POSTMASTER: Address changes to: SMI, 9700 Park Plaza Ave, Unit 202, Louisville, KY 40241-2287. This is Issue 356 • Volume 31 Number 2. Mailing date: 2/05/2020.

[1]The same defensive trend-following protocols SMI uses within Upgrading can be applied to a Just-the-Basics or other indexed portfolio. See January2019:p8 for details.

The Core Building Blocks of Successful Investing

(continued from front page)

investing thing for a while, consider this an opportunity to review your past big-picture decisions and decide if they still make sense given your current season of life and the progress you've made toward your goals.

We could include a great many items in a list of "core" principles. But to focus this discussion more firmly on the investing process itself, we've made a few assumptions up front. We're assuming you're already utilizing a spending plan (aka a budget).[1] Creating a budget and living by it likely will make a more significant impact on your financial life than anything else you can do. It will enable you to have a monthly surplus that makes financial progress possible. Without a budget, you're likely trying to harness the wind.

While on the subject of tilting at financial windmills, if you're not giving generously, make this the year you begin. Scripture makes clear that we were designed to live generously, and it is full of promises for generous, cheerful givers.[2] Though counter-intuitive, giving generously is a key component of building financial security because it invites the Lord's blessing.

We're also assuming you're rid of most, if not all, consumer debt. (If you still have debt other than your mortgage, focus your efforts there first.[3]) Likewise, we're assuming you have a reasonable savings reserve. Building a reserve is your next priority before beginning to invest.[4]

Living on a budget, giving generously, living debt-free, and having a reasonable emergency savings reserve comprise the bedrock we're building on. From there, you're ready to begin your *investing* journey. Here are five foundational principles to help get you where you want to go.

1. Write it down! The importance of your long-term plan

Many people think they have a long-term investing plan. And they do—sort of. At least until the market drops -10% in two weeks. Then they realize they really only have a collection of ideas about how they might want to invest. Guess how much those vague ideas are worth at 3 p.m. on Friday when the market is down –4.5% for the day with no bottom in sight?

In contrast, SMI is built around the idea of creating a personalized, long-term investing plan and *putting it in writing*.[5] Don't neglect this last part. Putting pen to paper (or pixels to screen) forces you to become much more precise, concise, and specific. These are the qualities your plan will need to be truly helpful at 3 p.m. on the aforementioned Friday when the market is tumbling and your emotions are screaming at you to end the pain.

What needs to be included in your long-term plan? A good place to start is with a few brief financial goals. Prayerfully set, and agreed upon with your spouse if you're married, these written goals can motivate you to *stick* to your plan.

Your application of the remaining four steps (i.e., core principles) discussed in this article will constitute a significant portion of your long-term plan. Before moving on to those, here are four *keys* that will help ensure that your plan is effective.

Key #1: Success in investing comes not in hoping for the best, but in knowing how you will handle the worst. No one knows what is going to happen next year, next month, or even next week. Your plan must allow for the fact that the investment markets will experience unexpected rough sledding now and then. That's where diversification comes in. The idea is to pick investments that "march to different drummers." Your strategy should involve owning a mix of investments that are affected differently by economic events. For example, your portfolio might include both a bond fund and a gold fund. When inflation heats up, bonds go down (due to rising interest rates); at the same time, gold goes up (because investors want a secure "store of value"). To the extent that the price changes in the two funds offset one another, you have added stability to your overall portfolio.

Key #2: Your investing plan must have clear-cut, easy-to-understand rules. You must be able to make investing decisions quickly and with confidence. This means reducing your decision-making to numerical guidelines as much as possible. A strategy that calls for a "significant investment" in small-company stocks is not as helpful as one that calls for "30% of your portfolio" to be invested in small-company stocks. Insofar as possible, your strategy should not only tell you *what* to invest in but also offer precise guidance in telling you *how much* to invest and *when* to buy and *when* to sell.

Key #3: Your investing plan must reflect your current financial limitations. Your plan should effectively prevent you from taking risks you can't afford. The words "higher risk" mean there's a greater likelihood you can lose part or all of your money. Every day, people who mistakenly thought "it will never happen to me" find just how wrong they were. Money is not an abstract commodity. For most of us, it represents years of work, hopes, and dreams. Its unexpected loss can be devastating. Only when you are out of debt and have an emergency reserve are you financially strong enough to bear the risk of loss that is ever-present in the stock market.

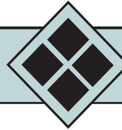
Key #4: Your investing plan should reflect a balance between your emotional "comfort zone" and your need for capital growth. Your plan should prevent you from taking risks that rob you of your peace. That is why, as part of our "getting started" process, we help you identify and understand your tolerance for risk (see next section). We don't want you to embrace a strategy that takes you past your "good-night's sleep" level. If you do, you'll tend to bail out at the worst possible time. On the other hand, you can't set your risk level so low that you have no chance of meeting your long-term goals.

The process of thinking through and writing out your long-term plan will help create the "inside-out" perspective that SMI believes is so important.[6] And the process of periodically referring back to your plan helps maintain that focus as the years pass and you're tempted to add complexity to your investing efforts.

2. Carefully consider your most important investing decision

What determines the performance of your investment portfolio more than any other single factor? Many investors think it's the *specific investments* they choose. Those choices can make a big difference. But this is more crucial: *How much*

[1]Feb2019:p22 [2]Jul2018:p98 [3]Jan2018:p6 [4]Mar2015:p38 [5]Nov2019:p167 [6]June2017:p87



of your portfolio is allocated to stock-type investments and how much to fixed-income securities such as bonds. Academic studies suggest that as much as 90% of your long-term results will be traceable to this fundamental allocation decision.

A portfolio's stock-to-bond mix does more than dramatically influence future returns. It also tells you how those results are likely to be obtained. Generally speaking, the more bonds in your portfolio, the smoother the ride. By contrast, the higher your stock allocation, the more you can expect returns to come in a "two steps forward, one step back" fashion.

If owning stocks subjects you to larger swings in performance *and* produces losses more frequently, why use them at all? Because that's where the biggest long-term gains are! The net effect of all those stock market ups and downs is greater overall returns. So, on the one hand, we have stocks, which are volatile but produce high returns. On the other, we have bonds, which are relatively stable but generate lower returns. How should you go about combining them in a portfolio?

The key ingredient in this recipe is *time*. Over shorter periods, stock returns are more variable. Maybe you'll do great; maybe you'll do poorly. Given a long time frame, however, you can be confident that stocks will provide higher returns than bonds.

Here's an example to illustrate this point. Think about tossing a coin. You know that the probability of getting heads on any single toss is 50%. So if your goal is to get 50% heads, then what matters most to you is *having a lot of tosses*. If there are only going to be two tosses, you should be much less confident of getting 50% heads than if there are going to be ten tosses. With 100 or 1,000 tosses, your confidence should grow correspondingly that the long-term averages will emerge.

So it is with investing. The more years ("tosses") you have ahead of you to invest, the more confident you can be that you'll benefit from the higher average returns stocks have historically provided. The fewer years you have to invest, the more you need to protect against the possibility that the results over your shorter time period may not match the long-term averages.

That's why it's generally recommended that younger investors take advantage of the many "tosses" in their future by investing heavily in stocks. They can afford to ignore the short-term ups and downs, while focusing on the highest long-term returns possible. Later, as you move closer to retirement and the number of future tosses declines, it's prudent to scale back the short-term risk of loss by gradually increasing the percentage of bonds held in the portfolio.

The allocation of a portfolio is the primary driver of both its expected returns and volatility. If you're nearing the end of your investing time frame (whether for retirement, college, etc.), this information should give you confidence that you can keep growing your money at a reasonable rate even if you decrease your stock holdings to reduce the chance of short-term losses. Conversely, if you still have many years to invest, understanding this should liberate you from worrying too much about short-term stock market losses and help you focus on the higher long-term returns stocks have historically provided.

SMI provides tools to help you determine the optimal stock/bond allocation given your risk tolerance and current season of life. See the "Start Here" section of the SMI website for these tools.[1] (Note that our Dynamic Asset Allocation strategy does not require you to predetermine your optimal asset allocation. So, if you plan to use that strategy exclusively, you don't need to go through this process. However, if you are using any other SMI strategy, solely or *in addition to* DAA, you should go through the process to determine your optimal asset allocation.)

3. Maximize tax-advantaged opportunities

Taking maximum advantage of the opportunities provided by the government to delay or avoid taxation of your investment earnings is a crucial component to building long-term wealth. Yes, you can invest in a regular taxable brokerage account, but you'll advance much more quickly—and likely wind up keeping much more of your earnings overall—if you take full advantage of the retirement savings plans provided by employers (401k, 403b, etc.) and/or IRAs.

Describing all the account types and how to decide between them is too detailed a discussion for this article, but here's a broad overview. 401(k) plans and IRAs come in two types—"traditional" and "Roth." Traditional 401(k) plans and IRAs allow savers to defer taxes now and pay them later. Retirement savers get an up-front tax deduction when they deposit into the account. Their earnings then grow tax-deferred, and they pay tax on all of the withdrawals (both their original principal and all earnings) in retirement. The Roth versions of these plans flip the tax equation: pay taxes now, make tax-free withdrawals later. *After*-tax money is deposited initially, which makes all later withdrawals (principal and earnings) tax-free in retirement. Which approach is better largely depends on whether you end up in a higher or lower tax bracket in retirement.[2]

Roth accounts would seem to be more advantageous, but that isn't always the case. With "traditional" accounts, it may appear that you're merely postponing your taxation day of reckoning. But keep in mind that most people are likely to be in higher tax brackets now (while working and saving) than during retirement (when their employment income has stopped). This means they may pay significantly less taxes on investment gains later, as opposed to paying them each year while earning employment income.

Granted, non-taxable accounts have more strings attached than taxable brokerage accounts, so you lose some flexibility. But that's a reasonable tradeoff for most people.

It's also worth noting that these tax-advantaged accounts have income and contribution limits, so it's wise to start utilizing them sooner rather than later. If you delay making these deposits until you achieve other financial goals, you may find yourself unable to take maximum advantage. If you forgo making a contribution one year, it's gone forever—you can't make a double contribution the next year.

4. Choosing the right investment strategy

What makes an investment strategy the "right" choice? It's not always an easy decision. The most important point is that you believe in your chosen strategy enough to stick with it during the inevitable downturns. Every strategy will

[1]www.soundmindinvesting.com/start-here [2]See April2019:Cover and chapters 20 and 21 of *The Sound Mind Investing Handbook*.

falter occasionally. Bailing out at those times in search of a better-performing approach isn't a formula for building long-term wealth.

Sound Mind Investing offers two "Basic" investment strategies: Just-the-Basics (JtB) and Upgrading. Our two "Premium" strategies are Dynamic Asset Allocation and Sector Rotation. Here's a brief overview.

- **Just-the-Basics** is the epitome of simplicity. Using just three or four Vanguard index funds (depending on your chosen portfolio mix), JtB seeks to match the return of the overall market. Research repeatedly shows that the average investor typically trails the market's rate of return, usually by a significant margin. JtB ensures this won't happen to you by delivering returns roughly equal to that of the market. As a bonus, it's an easy, low-maintenance way to invest, requiring attention only once a year.
- **Upgrading** is a trend-following strategy that attempts to beat the market by continually adjusting to the types of investments the market is currently favoring. In Upgrading, we rank more than 1,600 mutual funds by type each month and determine which ones have been delivering the best recent performance. We recommend the purchase of the highest-momentum[1] funds in each of five SMI stock risk categories. These funds are held until they stop outperforming. At that point, we recommend replacement funds showing stronger recent performance.[2]
- **Dynamic Asset Allocation (DAA)** is also a trend-following strategy. However, instead of rotating into the highest-momentum *funds* within different stock risk categories, DAA rotates among entire *asset classes*—U.S. Stocks, Foreign Stocks, Real Estate, Gold, Bonds, and Cash—keeping those following the strategy invested in the three best-performing classes. As a somewhat defensive strategy, DAA enables investors to participate in *some* of the gains of a growing market while providing strong protection against loss during market downturns.
- **Sector Rotation (SR)** is SMI's highest-risk, highest potential reward strategy. By investing in a single highest-momentum fund among a universe of focused, industry-specific "sector" funds, SR has generated a remarkable +13% average annual return since the strategy launched in 2003. Because of its high-risk profile, investors are encouraged to put no more than 20% of their portfolio's optimal stock allocation into SR.
- **50/40/10** refers to a way of blending SMI strategies that involves putting 50% of your portfolio in Dynamic Asset Allocation, 40% in Fund Upgrading, and 10% in Sector Rotation. While it requires a little more work to manage your portfolio this way, the benefits can be substantial. SMI research suggests this approach should reduce portfolio volatility while increasing returns.[3]

5. Run your retirement numbers and make adjustments

This step may seem a bit tricky, but it doesn't need to be. First, you need to periodically revisit the first four steps on this list (as well as revisiting your budget). Your budget won't likely be the same at age 30 as at age 50—and neither will your asset allocation. Life happens—an illness, job change, unexpected blessings that cry and need their diapers changed—these and a thousand other factors may cause you to adjust your plan as you go. That's okay. Just *don't abandon your old plan without putting a new plan in place*.

On the purely investment side, things are a little more rigid—you shouldn't make changes to your plan just because the market is down –25% and you're feeling queasy. But if you come across new information or a new strategy that makes you honestly (and unemotionally) believe that a change is warranted, there's flexibility to build it into your plan. Circling back to where we started, however, make sure any changes are *inside-out* (based on your needs and goals), not *outside-in* (based on the news of the day).

In addition, we recommend running your retirement-savings numbers periodically. Every few years may be enough for some; others may prefer more often, perhaps annually. SMI offers two ways to do this. First, you could use the MoneyGuidePro® software, to which SMI Premium-level members can gain access for a one-time $50 fee.[4] This powerful tool allows you to do thorough retirement-related investment planning and to store your information for easy updates in the future.

The second method is to use an old-fashioned pencil-and-paper approach. Chapter 19 of *The Sound Mind Investing Handbook* includes retirement worksheets for this purpose.

The challenging thing, of course, is knowing what to do when reviewing your numbers reveals a shortfall. If you find you're behind schedule on your retirement-savings goals, the safest approach is to increase your savings while keeping your portfolio allocation and strategy selection unaltered. While it's not easy, it is safe because you aren't asking too much of yourself emotionally, as can be the case when you step beyond your ideal allocation or strategy selection.

If you absolutely can't find the extra savings to plug the hole, either you need to scale back your retirement assumptions (when you will retire or how much income you hope to have in retirement), or you need to *add more risk* in pursuit of higher investment returns. We write it that way intentionally to drive home the riskiness of this approach. Boosting your stock allocation from 60% to 80% may not seem like a big deal—until the next bear market rolls around and you're outside your emotional comfort level. Similarly, adding a higher-risk strategy, such as SMI's Sector Rotation strategy, may seem like an easy way to boost returns. Just be aware that with those higher returns comes higher risk and volatility.[5]

Higher risk always accompanies higher-return strategies. Attempting to recover from investment declines by pursuing higher-risk approaches has been the downfall of many investors throughout the ages. Better to make realistic adjustments to your retirement plans by delaying retirement an extra year than risk blowing up your portfolio in pursuit of higher "make-up for lost ground" returns.

The five steps described above aren't comprehensive in terms of taxes, estate planning, insurance, and so forth, but they do provide a helpful guide for gauging your fundamental investing needs and getting started. The primary obstacle for most people as they travel down the road to financial freedom is not a lack of a "perfect" plan—it is inertia. Get going with these bases covered and you'll find there's plenty of time to fine-tune things as you go. ◆

[1]Jan2019:Cover [2]See page 27. [3]Apr2018:Cover [4]Jan2020:Cover [5]Dec2019:p184

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

MAKING ENDS MEET: ESSENTIALS FOR SUCCESSFUL BUDGETING

By Russ Crosson[1]

The foundational Scripture on budgeting is found in Proverbs 27:23-24: "Know well the condition of your flocks, and pay attention to your herds; for riches are not forever, nor does a crown endure to all generations." In today's vernacular, this verse confirms that we should *know where our money is going* versus *wondering where it went*.

Any system is an "envelope" system

Once you have established your living expenses [i.e., you know your actual cost of living], it's time to develop a system to ensure you stay within your spending targets.

A traditional "envelope" system is when you store cash in separate envelopes to meet different categories of expenses. It doesn't matter if you use sophisticated software, a simple spreadsheet, or actual envelopes; the principle is the same. You decide what goes into each budget category—such as utilities, gasoline, vacation savings, clothing, gifts, allowances, or insurance—and you put that dollar amount into each "envelope." After establishing your categories, you spend against what you have allocated in each area.

Tracking is not the same as budgeting

Be careful not to simply *track* what you have spent. That is not budgeting but rather record keeping.

What do I mean by that? Occasionally, when I ask people if they are on a budget they reply, "Yes, we track our expenses through an app." It's fine that they track their spending in an app, but that's not a budget system. It may help them set their budget amounts more realistically, but it doesn't help them stay within their planned budget.

For a budget system to function, you must be able to answer the question, "How much do I have left to spend in each category?" At any time during the month or year, you should be able to review your finances and know how you are doing against what you planned to spend. It's important to say no to items that are not in the budget or that would increase your expenses beyond your income level—for example, a bigger house, a new car, or the latest technology.

Common budget-related questions

● **Can I start using a budgeting system anytime during the year?** Although it's easiest to start a budget at the beginning of a calendar year, you can start anytime. Regardless of when you start, you will go through the same process to determine the calendar-year spending amounts and then allocate them monthly.

● **What if I don't have a set salary because I work on commission or do freelance work?** If you have a variable income, you can begin by putting more money into your savings. You can then deposit your variable checks into your savings account and, in essence, "salary yourself" out of the savings account each month. In other words, you put yourself on a set salary each month, thus removing the monthly variability. You still have to earn a certain total income annually to cover your expenses (living, giving, taxes, and debt payments), but paying yourself a fixed salary should make budgeting easier and less stressful.

● **How do I handle items deducted from my paycheck, such as insurance premiums?** Make sure you include these items in your budget as living expenses. A common mistake people make is to forget to include these categories because they are withheld from the gross paycheck. [Your budget should be based on your gross income, so] these deducted amounts must be accounted for.

● **What if I'm running out of money before the end of the month?** There are only two possibilities: Either you don't have realistic amounts allocated for expenses and need to increase them, or you have set realistic amounts and just aren't following them. In either case, you need to track the details to see exactly where your money is going so that you can either adjust the funds allocated or cut back on your spending.

● **What are major budget breakers to watch for?** Budget breakers are generally found among discretionary, non-monthly budget items. These items are primarily gifts, clothing, vacations, and house furnishings.

It's interesting to note that the non-discretionary items (fixed expenses such as utilities, mortgage, and gas for vehicles) seldom are the culprits. It's also interesting that most expenses in the budget are fixed. So the key to avoiding budget breakers is to control the few unfixed expenses that tend to blow the budget. However, if your fixed expenses are too high—perhaps you live in a house that is too much for your income or have car payments that are too high—they will contribute to your budget problems.

● **Is there an amount that is too much for Christians to spend on living expenses?** As with many areas of the Christian life, it would be much easier if there were definitive answers, but there is no clear answer to this question. God allows us a great deal of freedom in the lifestyle area. He only gives us these definitive boundaries: Spend less than you make and be content (1 Timothy 6:8), give to the Lord (Luke 6:38), pay the lender (Proverbs 22:7), and pay your taxes (Romans 13:7).

Once we do these things, the amount left over is ours to do with as the Lord leads. Maybe we should give more. Maybe we should take more family vacations. These decisions are between God and you. As long as you seek His direction and *(continued on page 29)*

[1]Russ Crosson is Executive Vice President and Chief Mission Officer of Ronald Blue Trust. This article is excerpted from his book *Your Money Made Simple*. Copyright © 2019 by Russ Crosson. Published 2019 by Harvest House Publishers. Used by permission. All rights reserved.

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

INVESTING AS A COUPLE

Investing is arguably the most complicated aspect of managing money. Add to that the challenge of investing as husband and wife and you have a recipe for all kinds of trouble.

Often that trouble manifests itself as one spouse handling all of the investment decisions, leaving the other out of the loop and ill-prepared to invest on their own should that need arise. In other cases, both spouses just do their own thing with their individual investment accounts, which may not be good for their marriage or their investment results.

Two main factors divide couples in this area.

1) Men and women approach investing differently. Various studies show men and women tend to think about investing differently and, therefore, actually invest differently. While there are exceptions to all that follows, generally speaking, women make fewer trades than men; are more likely to use mutual funds than individual stocks; are more likely to choose target-date funds in their retirement plan accounts; are less comfortable with financial risk and therefore tend to choose less risky investments; feel less confident about their investing capabilities; and… wait for it… usually generate *higher* returns than men.

2) Husbands and wives aren't working together. While some of the investing-related challenges couples face can be traced to genetic differences, others are self-inflicted. According to a 2015 Fidelity study,[1] couples aren't on the same page in many areas. Some of this comes down to a lack of communication. For example, 50% of married people are not in agreement about when they will retire, 43% aren't clear about how much income their partner earns, and 36% disagree on the value of their household's investable assets.

As is common with other aspects of money management, one spouse often takes the lead in managing their household's investment accounts. However, in 70% of such couples, the spouses disagree as to *which one* is primarily responsible!

Some challenges couples face with investing can be attributed to a lack of planning. For example, 48% of married people have "no idea" how much money they will need to save for retirement to maintain their current lifestyle. Of those who think they *do* know, 47% disagree with their spouse on how much will be needed (this disagreement is especially prevalent among those closest to retirement age). And only 21% of married couples have developed a detailed retirement plan. What's a couple to do?

Getting on the same page

Here are ways husbands and wives can work on their investments as a team.

● **Goals.** First, talk about why you are investing. If retirement is a major goal, when would you like to retire and how do you envision spending your time in that season of life? If you're investing for your kids' college expenses, what percentage of the expenses would you like to cover? Is that based on an in-state or out-of-state school? Public or private?

● **Risk.** An ideal next step is for you and your spouse to take a risk-assessment questionnaire, such as the one available on SMI's website.[2] Each of you should take it separately and then compare notes. If your investment temperaments differ, try to meet in the middle. For example, if you have 5-10 years until retirement and your temperament is that of a Daredevil, which would point you to an 80/20 stock/bond allocation, but your spouse is a Researcher, which would call for a 60/40 allocation, use a 70/30 allocation.

● **How much to invest.** Run numbers on how much you should invest to accomplish your goals.[3] (Most calculators will require information about how much risk you're willing to take, so it's important to have taken the previous step before this one.) Once you know how much you need to invest each month to meet your goals, discuss and decide whether you're willing and able to invest that much and what, if any, tradeoffs may be needed to do so.

● **How to invest.** It's fine for one spouse to take the lead with the various investment-related *tasks*, such as making trades and tracking returns. However, both should be involved in the investment *decisions*, such as which strategy to use and how much to invest. Both of you should be able to explain how the strategy works, how it is expected to perform under various market conditions, and why the approach is appropriate for you, given your goals and risk tolerance.

This conversation should also lead to an agreement about what to do—or *not do*—at times of market stress.

● **Information access.** Both of you should have easy access to the status of your investments, knowing how much money you have in your portfolio, in which accounts, and how your portfolio is performing. (Do you both have the passwords to your accounts?)

● **What if?** One more step to talk through is how your investments will be managed in the event of a spouse's death. We know numerous SMI newsletter subscribers who have encouraged their spouses to utilize SMI Private Client in the event of their death so that the strategies they are following manually could then be automated.[4]

As you have these conversations, put your decisions on paper. A written investment plan will serve as a guiding document that reminds both of you about your agreed-upon approach to investing while helping you navigate market downturns.[5] Plus, it will make it easier for the spouse who is less involved in the day-to-day management of your household's portfolio to carry on if the other spouse passes away. ◆

[1]bit.ly/2uqBReQ [2]sminow.com/risk-tolerance [3]See SMI's recommended retirement planning calculators here: sminow.com/retirement-calc. For college funding, use this calculator: sminow.com/college-calc. [4]March2018:p40 [5]Nov2019:p167

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

2019 YEAR IN REVIEW: STRONG MARKETS LEAD TO NEW PORTFOLIO HIGHS

As the calendar flipped from 2018 to 2019, few imagined the dramatic turn the financial markets were about to take. The stock market had fallen nearly -20% during the last quarter of 2018 and fear was palpable as 2019 began. But a dramatic shift in Fed policy—from nine interest rate *hikes* in 2016-2018 to three rate *cuts* in 2019, coupled with massive Fed stimulus late in the year that re-inflated the central bank's balance sheet at a breathtaking pace—provided a steady dose of rocket fuel that propelled financial markets to new all-time highs.

JFK famously said, "A rising tide lifts all boats," and that was certainly true of financial markets in 2019. Asset prices rose sharply across the board.

SMI's model portfolios reflected these strong gains as well. Despite starting 2019 with very conservative allocations and fund selections (the result of following the rapidly falling market trend during the dismal fourth quarter of 2018), all of SMI's model portfolios except one still managed to produce new all-time highs during the year. Ironically the one that did not, Sector Rotation, has been the standout performer throughout this long bull market—reinforcing the idea that little is predictable when it comes to investing. Hence, the best course is to diversify and maintain a long-term perspective!

Just-the-Basics (JtB) & Stock Upgrading

When the books closed on 2019, the Wilshire 5000 index was up a breathtaking +31.0%, the strongest year for stocks since 2013, and the third-best year of the past two decades. Of course, much of that shine comes off when the results of 2018's fourth-quarter are included: the 15-month return falls to +12.3%. That's still a solid return, but hardly the remarkable story 2019 appears to be without the context of the steep market correction that immediately preceded it.

As has often been the case in recent years, stocks of large domestic companies led the way higher in 2019. Within JtB, this is reflected in the fact that S&P 500 component (VFIAX) gained +31.5%, extended market component (VEXAX) gained +28.0%, and foreign component (VTIAX) gained +21.5%. Altogether, JtB gained +28.1% for the year.

Stock Upgrading's returns were lower, though its gain of +21.7% was still fantastic in absolute terms. The first and last quarters of the year weighed on Upgrading's performance relative to the market. The first quarter of 2019 saw Upgrading's "2.0 defensive protocols" trigger in response to the rapid market breakdown at the end of 2018. Those first-quarter cash allocations, when the stock market was rebounding strongly, accounted for roughly half of the performance gap. The rest was mostly attributable to being positioned in relatively conservative funds when the Fed dramatically ramped up its liquidity push late in the year. The market spiked +9.1% during the fourth quarter of 2019, while Stock *(continued on page 29)*

A HISTORICAL LOOK AT THE PERFORMANCE OF SMI MODEL PORTFOLIOS

	U.S. Stocks	SMI Basic Strategies			SMI Premium Strategies		
	Wilshire 5000	Just-the Basics[1]	Stock Fund Upgrading[2]	Bond Fund Upgrading[3]	DAA	Sector Rotation	50-40-10 Portfolio[4]
2019	31.0%	28.1%	21.7%	8.5%	13.7%	-1.6%	15.4%
2018	-5.3%	-8.4%	-7.9%	-0.5%	-4.5%	-15.8%	-7.0%
2017	21.0%	21.4%	18.1%	2.3%	16.0%	56.7%	20.9%
2016	13.4%	12.3%	10.4%	3.6%	-0.5%	16.8%	5.6%
2015	0.7%	-1.6%	0.6%	-1.7%	-6.8%	-9.7%	-4.1%
2014	12.7%	7.5%	5.1%	8.4%H	13.0%	49.9%	13.6%
2013	33.1%	31.2%	34.5%	1.1%H	16.2%	65.7%	28.4%
2012	16.1%	17.6%	14.1%	4.6%H	13.9%H	23.3%	14.9%H
2011	1.0%	-3.4%	-5.4%	6.5%H	1.4%H	-3.2%	-1.8%H
2010	17.2%	20.0%	17.8%	17.9%H	20.3%H	9.1%	18.2%H
2009	28.3%	33.9%	33.6%	13.5%H	17.6%H	30.5%	25.3%H
2008	-37.2%	-39.3%	-38.8%	6.6%H	1.3%H	-31.5%	-18.0%H
2007	5.6%	7.1%	14.3%	8.4%H	10.1%H	28.1%	13.5%H
2006	15.8%	17.2%	17.4%	7.6%H	25.7%H	-1.9%	19.6%H
2005	6.4%	9.0%	12.0%	2.0%H	8.6%H	46.1%	13.7%H
Past 15 Years (Total Gain)	269.7%	236.3%	224.6%	132.6%	281.4%	627.0%	305.4%
Dollar Profits on $100,000[5]	$269,710	$236,261	$224,593	$132,615	$281,440	$627,036	$305,372
Annualized Rate of Return	9.1%	8.4%	8.2%	5.8%	9.3%	14.1%	9.8%

Footnotes

Results for all SMI strategies assume all transactions were made on the last trading day of the month. Transaction costs are not included because they vary from broker to broker. **[1]** Results assume the account was rebalanced at the beginning of each year with 40% of the stock allocation invested in the S&P 500 (VFIAX), 40% in Extended Market (VEXAX), and 20% in Total International Stock (VTIAX). **[2]** For a 100% stock portfolio. **[3]** For a 100% bond portfolio. **[4]** For a portfolio allocated 50% to DAA, 40% to Stock Fund Upgrading, and 10% to Sector Rotation. See the April 2018 cover article for details. **[5]** The dollar results show the amount of profits in an account with a $100,000 balance at the beginning of 2005. Results for 15 years are shown rather than the typical 10 years to provide better insight into the return comparisons of various strategies in the years leading up to the last bear market. These seem particularly relevant in view of the present market action. **[H]** Results are hypothetical from back-testing a strategy following a mechanical rules-based system.

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

THE NEW LAW OF THE LAND ON RMDS, IRA CONTRIBUTIONS, AND MORE

The retirement-planning landscape in the USA is different now than it was just a few weeks ago. A federal law took effect January 1 that affects required minimum distributions (RMDs), IRA contributions, inherited retirement accounts, retirement-account investment options, and more.

The SECURE Act[1] has 29 provisions in all (although not all are retirement-related). Here are the most notable:

● **Delayed Required Minimum Distributions:** As of Jan. 1, 2020, the age that triggers RMDs from traditional IRAs and other retirement accounts is no longer 70½ but 72. That means account holders have another year-and-a-half for their nest eggs to grow before being required to start taking money out. (Account holders who turned 70½ *before* Jan. 1, 2020, remain under the old rules.)

Important: Even though the starting age for RMDs has been pushed back to 72, 70½ remains the age at which a taxpayer can start making tax-advantaged Qualified Charitable Donations[2] directly from an IRA, thus avoiding taxes on those distributions (but see the "QCD caveat" below).

● **No Age Limit for "Traditional" IRA Contributions:** Until now, contributions to traditional (i.e., non-Roth) accounts weren't allowed after age 70½. The new law removes that prohibition. As long as an IRA holder has earned income, he or she can continue to contribute to a traditional IRA.

Here's the "QCD caveat": Contributions made to a non-Roth IRA after age 70½ affect how much of a charitable gift made from the IRA can be characterized as a Qualified Charitable Donation. The new law says post-70½ contributions will offset charitable donations dollar-for-dollar. Example: You contribute $7,000 to a traditional IRA at age 71, then make a $20,000 charitable gift directly from the IRA. Only $13,000 of the donated amount ($20,000 minus $7,000) could be claimed as a QCD.

● **Fewer Inherited Accounts Are "Stretchable":** The SECURE Act has changed the "stretch" provisions related to funds inherited from a retirement account (either a traditional or Roth IRA or a defined-contribution plan). Formerly, distributions from an inherited account could be stretched out over a beneficiary's expected lifetime, thus allowing many years for the account to continue to grow while also spreading out the tax burden the beneficiary would incur as the money was withdrawn bit by bit.

Under the new law, a lifelong stretch remains available to certain beneficiaries only: a surviving spouse, a beneficiary less than 10 years younger than the original account owner (a younger brother or sister, for example), or a beneficiary with a disability or a chronic illness (as defined in the Internal Revenue Code).

The SECURE Act bans the lifetime stretch approach for all others who inherit retirement money, if the account owner died after Dec. 31, 2019.[3] Such beneficiaries must now receive the entire proceeds—and pay the taxes on distributions—*within 10 years*. (If a minor child inherits an account from a *parent*, not from a grandparent or other relative, the 10-year payout clock won't start until the child reaches the age of majority.)

Because of the new law, any retirement-account holder who was planning to bequeath an account to an adult child or a grandchild—relying on the stretch rules to create lifetime income while minimizing the tax burden—needs to come up with an alternative plan. One tax-easing option is to convert as much traditional IRA money as possible to a Roth IRA. Such an approach will incur taxes for the account owner in the near-term, but later, the 10-year beneficiary withdrawals from an inherited Roth account would be tax-free.

● **Annuity Options Now More Likely in Employer-Sponsored Plans**: Annuities are insurance contracts that provide a steady income in retirement, either for a pre-determined period or for the rest of the annuity owner's lifetime.

Few employers that sponsor 401(k)s or similar plans have offered annuities because of concerns that an employer could be held liable if an insurance company was unable to meet its obligation to pay out. The SECURE Act provides employers with increased legal protection, clearing the way for annuity contracts to be included as retirement-plan investment options. Whether to offer such options, however, will remain at the employer's discretion.

● **Small-Company 401(k)s**: Because of the cost of setting up and administering a company retirement plan, many smaller employers have been reluctant to provide such plans. Under the SECURE Act, it will be easier for small companies to band together to form "group" 401(k) plans, thus reducing the cost burden.

● **401(k)s for Part-Time Workers**: Starting in 2024, a part-time employee who works for a company with a 401(k) plan will be able to participate if the part-timer meets certain requirements. Employers won't be required to provide matching contributions for part-time employees, however.

● **Penalty-Free Early Withdrawals for Childbirth and Adoption**: The SECURE Act allows up to $5,000 in penalty-free (but not tax-free) early withdrawals from a retirement plan to cover costs of childbirth or adoption. Caveats: To qualify, the money must be withdrawn *after* the birth has occurred or the adoption finalized. A $5,000 withdrawal may be made for each child born or adopted, but any withdrawal(s) must occur within one year of the related birth/adoption. *(continued on page 30)*

[1]Setting Every Community Up for Retirement Enhancement Act [2]July2019:p105
[3]For Thrift Savings Plan accounts and some other government-sponsored plans, the new stretch rules don't take effect until 2022.

Basic Strategies

The fund recommendations shown for Upgrading account holders are based primarily on "momentum" scores calculated just before this issue was published (not the earlier end-of-month scores shown on this page). Consistency of performance is also considered, along with the portfolio manager's philosophy and number of years at the helm. Three recommendations are made in each risk category. 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 12/31/2019	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	Foreign stocks	37.8	21.5%	4.2%	9.0%	7.3%	21.5%	9.9	0.96	0.11%/0.09%	20%	16%	12%	8%	VTIAX/VXUS
Extended Market Index	Small company stocks	44.1	28.0%	2.2%	8.9%	7.2%	28.0%	11.1	1.21	0.07%/0.07%	40%	32%	24%	16%	VEXAX/VXF
S&P 500 Index	Large company stocks	51.4	31.5%	3.0%	9.1%	10.9%	31.5%	15.2	1.00	0.04%/0.03%	40%	32%	24%	16%	VFIAX/VOO
Total Bond Market Index	Medium-term bonds	11.2	8.7%	-0.1%	0.0%	2.5%	8.7%	4.0	1.00	0.05%/0.035%	None	20%	40%	60%	VBTLX/BND

JUST-THE-BASICS FOOTNOTES: Just-the-Basics is an *indexing* strategy that requires just minutes a year to assure your returns are in line with those of the overall market. You won't "beat the market," but neither will you fall badly behind. Depending on your particular stock and bond mix, your JtB portfolio should be allocated among either three or four traditional mutual funds/ETFs (see ticker symbols in rightmost column). For more on JtB, see Jan2019:p7-8.

RECOMMENDED FUNDS FOR SMI'S FUND UPGRADING STRATEGY

Risk	Data through 12/31/2019[1]	Date Added	E-Trade Avail[2]	Fidelity Avail[2]	Schwab Avail[2]	MOM[3]	---------------- Performance ---------------- YTD	1Mo	3Mo	6Mo	12Mo	3Yr Avg	Rel Risk[4]	Exp Ratio	Number Holdings	Redemp Fee?[5]	Ticker Symbol
Category 5 Foreign	1. Fidelity Intl Growth	12/19	Yes	NTF	Yes	55.6	34.0%	3.4%	10.7%	11.0%	34.0%	15.4%	0.95	0.99	90	None	FIGFX
	2. WisdomTree Intl Hedged ETF	12/19	ETF	ETF	ETF	54.2	33.4%	2.6%	8.6%	12.2%	33.4%	12.7%	0.87	0.58	282	None	IHDG
	3. Fidelity Intl Capital Apprec	09/19	Yes	NTF	Yes	49.3	33.0%	3.5%	8.2%	8.1%	33.0%	16.5%	0.95	1.01	99	None	FIVFX
Category 4 Small/Growth	1. Needham Sm Cap Growth	01/20	NTF	NTF	NTF	90.2	54.5%	4.8%	16.1%	19.7%	54.5%	17.9%	1.37	1.93	37	None	NESGX
	2. DF Dent Midcap Growth Inv	09/19	NTF	Yes	NTF	52.5	40.1%	0.4%	5.7%	6.7%	40.1%	22.4%	1.10	0.98	33	2%60days	DFDMX
	3. Janus Henderson Contrar T	10/19	NTF	NTF	NTF	65.5	43.0%	1.4%	10.0%	12.5%	43.0%	13.0%	1.28	0.74	43	None	JSVAX
Category 3 Small/Value	1. Touchstone Mid Cap Z	05/19	NTF	NTF	NTF	52.3	35.9%	1.4%	5.0%	11.4%	35.9%	16.3%	0.99	1.21	32	None	TMCTX
	2. Weitz Hickory	06/19	NTF	NTF	NTF	51.1	36.1%	1.6%	6.6%	8.4%	36.1%	8.3%	1.11	1.09	37	None	WEHIX
	3. Invesco S&P MidCap Mtm ETF	12/19	ETF	ETF	ETF	49.1	30.4%	3.2%	9.4%	9.3%	30.4%	6.6%	1.10	0.39	82	None	XMVM
Category 2 Large/Growth	1. Polen Growth Investor	10/18	NTF	NTF	NTF	58.0	36.8%	2.6%	10.2%	10.9%	36.8%	22.9%	1.01	1.25	25	2%60days	POLRX
	2. ☎ Invesco QQQ Trust	02/20	ETF	ETF	ETF	66.1	39.0%	3.9%	12.9%	14.3%	39.0%	22.6%	1.24	0.20	104	None	QQQ
	3. YCG Enhanced Fund	01/20	NTF	NTF	NTF	61.8	41.2%	2.6%	9.1%	11.5%	41.2%	18.8%	0.92	1.19	73	2%30days	YCGEX
Category 1 Large/Value	1. ☎ Invesco S&P 500 Top 50 ETF	02/20	ETF	ETF	ETF	54.5	32.0%	2.9%	10.3%	12.2%	32.0%	16.1%	1.01	0.20	53	None	XLG
	2. Vulcan Value Partners	12/19	NTF	NTF	NTF	80.6	44.4%	4.1%	16.5%	19.7%	44.4%	15.9%	1.23	1.08	29	2%90days	VVPLX
	3. First Trust Dvd Achievers ETF	12/19	ETF	ETF	ETF	67.6	37.7%	3.9%	13.3%	16.6%	37.7%	15.1%	1.28	0.50	51	None	RDVY
Bond Categories	Vanguard I-T Bond[6]	2/19	ETF	ETF	ETF	12.8	10.3%	-0.1%	0.0%	2.4%	10.3%	4.5%	1.17	0.07	6.3[7]	None	BIV[8]
	Permanent: Vanguard I-T Bond	Perm	ETF	ETF	ETF	12.8	10.3%	-0.1%	0.0%	2.4%	10.3%	4.5%	1.17	0.07	6.3[7]	None	BIV[8]
	Permanent: Vanguard S-T Bond	Perm	ETF	ETF	ETF	7.0	5.0%	0.2%	0.5%	1.4%	5.0%	2.5%	0.46	0.07	2.7[7]	None	BSV[9]

Upgrading Footnotes: [1] The funds in each risk category have been selected and ranked (1 through 3) based primarily on their momentum scores in late January, rather than on the end-of-December data shown above. The fund ranked third is the one that currently appears most likely to be replaced next. If there is a telephone symbol (☎) next to a fund's name, that fund is a new recommendation. **[2]** Fund Availability: NTF (no transaction fee) means the fund can be bought and sold without a transaction fee as long as you stay within the trading limitations imposed by E-Trade (800-387-2331), Fidelity (800-343-3548), and Schwab (800-435-4000). Policies change frequently, so be sure to verify their accuracy. ETFs (exchange-traded funds) are available at all brokers and typically trade free if bought/sold online. **[3]** Momentum is a measure of a fund's performance over the past year and is our primary performance evaluation tool. For more, see Jan2019:Cover. **[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. To learn more, see Nov2018:p167. **[8]** Those preferring a traditional mutual-fund option can buy VBILX. **[9]** Those preferring a traditional mutual-fund option can buy VBIRX.

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

SOUND MIND PORTFOLIOS

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 (March 2018: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 Jan2020:p7.

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 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, the investor selects the stock/bond mix for his or her 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 Basic Strategies page, the highest-ranked Cat. 5 fund is Fidelity Intl. Growth, the highest-ranked Cat. 4 fund is Needham Small Cap Growth, and so on. After making decisions 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 position in the same risk category that is available at your broker.

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%

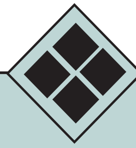
❸ BUY YOUR FUNDS

Example uses an 80/20 mix between stocks and bonds		Dollars	Invest in Funds
Stock Cat. 5: Foreign	16%	$8,000	Fidelity Intl Growth
Stock Cat. 4: Small/Growth	16%	$8,000	Needham Sm Cap Growth
Stock Cat. 3: Small/Value	16%	$8,000	Touchstone Mid Cap Z
Stock Cat. 2: Large/Growth	16%	$8,000	Polen Growth Investor
Stock Cat. 1: Large/Value	16%	$8,000	Invesco S&P 500 Top 50 ETF
"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 Jan2020:p7).



MONEYTALK

STOCK UPGRADING — NEW FUND RECOMMENDATIONS

[When more than one fund in the same risk category is replaced, you should evaluate which of the newly recommended funds is the best fit for your portfolio. The simplest method for picking new funds is to refer to our 1-3 rankings on the "Basic Strategies" page and invest in the highest-ranked fund in each risk category that is available through your broker. • 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 (applies to taxable accounts only). Nevertheless, we suggest a change when a 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 tax-related 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). Be aware, however, that from 2006-2010, the average performance "cost" of retaining such funds was roughly 0.5% per month. For more details, see Oct2011:p153.]

◆ **In the Large/Growth group, Invesco S&P GARP ETF (SPGP, 12/2019) is being replaced.** We're replacing two ETFs this month after holding them each just two months. That's quicker than usual for Upgrading, but with ETFs now trading commission-free and without broker-imposed holding periods, we can take advantage of this flexibility to move quickly when conditions warrant.

When we recommended SPGP at the end of November, the stock market had been accelerating for about six weeks—a short period in terms of our momentum formula, which focuses on longer-term trends. It's not surprising that the first wave of slightly more aggressive fund choices was relatively tame, an apt description of this ETF focused on "growth at a reasonable price" (GARP). However, as the market's strength has continued through December and the first few weeks of January, many of those milder funds have been bypassed by more aggressive fare, especially within the growth risk categories.

After slightly outpacing the average fund in Morningstar's Large/Growth group in December, SPGP couldn't keep up in January. Overall, the ETF gained +1.6% for us over the two months it was recommended (through January 27). That's lower than the average Large/Growth fund's gain of +4.6%, however, so we're moving on.

● **Invesco QQQ Trust ETF (QQQ) is being added.**[1] Unlike SPGP, there's no way anyone would confuse QQQ for a "mild" option. Known as the "Triple Q," this ETF has long been synonymous with the tech-heavy Nasdaq index. When tech is hot—and it has been sizzling since Fed liquidity lit a fire under the market in October—it's difficult for anything else to keep up with the gains in QQQ. Not surprisingly then, the Triple Q is currently at the very top of our Large/Growth rankings.

That's the positive spin—here's the rest of the story. Returns such as QQQ has generated (+11.7% over the past three months, +33.1% over the past year) don't come without a lot of risk. QQQ's relative-risk score of 1.24 isn't excessive for the Large/Growth group at a time when many of the other highly ranked funds are even higher. But that score signifies QQQ has been roughly 24% more volatile than the S&P 500 index over the past three years. Consider that the other two currently recommended funds in our Large/Growth risk category have relative-risk scores of just 1.01 (1% more volatile than the S&P 500 index) and 0.92 (8% *less* volatile), and it becomes clear that QQQ is the high-risk choice among the three current recommendations.

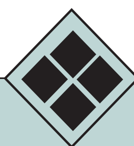
That type of aggression isn't inappropriate given the strong market trend of 2019, and especially the October-January period. But there are significant concerns about the market's valuation combined with relatively weak economic conditions. This ETF will continue to prosper if the Fed keeps pushing liquidity into the market. But with that inflow of fresh Fed liquidity slowing markedly throughout January, it remains to be seen whether stocks can continue to levitate without it.

◆ **In the Large/Value group, Invesco Dynamic Large Cap Value ETF (PWV, 12/2019) is being replaced.** The performance of this ETF has been puzzling. PWV had outperformed the average fund in Morningstar's Large/Value group for eight consecutive months when we recommended it at the beginning of December. It promptly flipped and underperformed both months we owned it. The gap hasn't been particularly large (–0.6% vs. +1.0%), but it's still disappointing. Thankfully, as noted in the write-up (at left) about SPGP, ETFs now offer us the flexibility to move on quickly when a recommendation falters, so we're taking advantage of that here.

● **Invesco S&P 500 Top 50 ETF (XLG) is being added.**[1] Admittedly, this is a somewhat "boring" choice, as this ETF simply owns the 50 largest stocks in the S&P 500 index. That puts this ETF squarely in the "blend" territory between the traditional "Growth" and "Value" camps, owning some stocks from each group. In SMI's risk category system, most "blend" funds are grouped into our value categories. That helps explain why this ETF is near the front of our Large/Value rankings: it has enjoyed the benefit of owning a number of large growth stocks within its portfolio, while most of its competitors within the Large/Value group don't own those stocks. Its largest holdings include Apple, Microsoft, Amazon, Facebook, and Alphabet (Google)—not the traditional fare of value funds.

Although we've seen this risk-category flexibility work out favorably for Upgrading many times in the past, it's important to consider the risks. This fund currently is excelling relative to other value funds because it pushes right up to the line where we might consider moving a fund to the growth camp. That's great when the market is rising and growth stocks are excelling. But that dynamic likely would reverse in a market downturn, causing greater losses here than would be the case with more traditionally conservative value funds. For now though, the market's trend is higher, so we'll continue to follow it. ◆

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



MONEYTALK

LEVEL 1 / CONTINUED FROM PAGE 22

MAKING ENDS MEET: ESSENTIALS FOR SUCCESSFUL BUDGETING

wisdom and are tuned in to His desires, you have freedom in this area.

It is important to make the lifestyle decisions that work best for you, your family, and your current station in life, and know that they may need to be adjusted. You may strive for a simpler lifestyle, but someone in the world will probably always have a simpler one. You may strive to elevate your lifestyle, but someone in the world likely has a higher standard of living. The best answer and choice is simply to walk with God daily and seek contentment.

Accountability in this area will also help make sure you're on track. What do I mean by accountability? Having someone in your life who will be honest regarding your budget may provide extra insight. On our own, we can justify any amount as "needed" in an expense category. It can be helpful to have someone periodically check our thinking for realism and balance. ◆

LEVEL 3 / CONTINUED FROM PAGE 24

2019 YEAR IN REVIEW: STRONG MARKETS LEAD TO NEW PORTFOLIO HIGHS

Upgrading was up "just" +5.9%.

While it's always tempting to simply compare final strategy returns to the market benchmarks, the context of 2019's Upgrading results is important. Following a decade-long bull market, in late 2018 Upgrading recognized the market's trend was breaking down to a degree only witnessed a handful of other times in the past two decades—two of which led directly to market declines of -50%. As a result, Upgrading took defensive measures that would have dramatically limited our losses had a bear market ensued. Due to Fed intervention, that bear market was thwarted and the market rebounded strongly. Stock Upgrading was able to pivot quickly enough to still participate in the bulk of the market's rise, gaining over +21% for the year—despite starting the year from an extremely defensive posture.

Naturally, we'd prefer not to have had Stock Upgrading start 2019 on the wrong foot. But we're encouraged that the system was nimble enough to rebound so quickly given the market's rapid about-face. As our past reporting on Upgrading 2.0's defensive protocols has shown,[1] eventually those measures are likely to save us a lot of money. This year they "cost" us in terms of additional gains we might have otherwise earned, but over the long-term we still believe they will add significant value to our portfolios.

Bond Upgrading

Interest rates were a huge driver of the financial market story in 2019. With investors increasingly concerned about a slowing economy, the Fed disappointed markets in December of 2018 by delivering the ninth interest rate hike of the cycle that began in late-2015. This was the immediate catalyst for the December 2018 stock market correction.

As signs of an economic slowdown around the globe became more evident, longer-term interest rates (which are determined by the bond markets) fell sharply. Eventually, the Fed joined in, making three cuts to the shorter-term Fed Funds rate.

Bond Investing 101 states that when interest rates fall, bond prices rise. So it was in 2019, as bonds of all types soared. Bond Upgrading gained +8.5% in 2019, a remarkable turnaround from the three years prior (2016-2018) when its total return was just +5.4%!

Dynamic Asset Allocation (DAA)

DAA started the year in its most conservative possible allocation. Despite the slow start, DAA still managed a gain of +13.7% for the year.

While the first quarter found most of SMI's trend-following strategies conservatively positioned while the markets quickly reversed course and climbed higher, the one place where this helped rather than hurt our relative returns was DAA's move into long-term bonds at the beginning of 2019. Long-term bonds would remain a DAA holding all year, paying off with a +19% gain. While bonds primarily are used to provide ballast and safety within SMI's other model portfolios, this is an example of DAA opportunistically using these more volatile long-term bonds as a contributor of significant gains.

2019 PERFORMANCE DAA ETF UNIVERSE

Ticker & Category		2019 Result
SPY	U.S. Stocks	+31.2%
EFA	Foreign Stocks	+22.0%
VNQ	Real Estate	+28.9%
BLV	Long-Term Bonds	+19.0%
SHY	Money Market	+3.4%
GLD	Gold	+17.9%

Ultimately, we don't expect DAA to keep pace with the stock market during huge up years like 2019. Participating in a strong portion of the market's gains—as DAA did this year—while providing the kind of protection the strategy was poised to deliver at the outset of the year, is what we're looking for from this strategy.

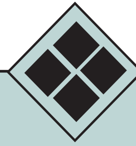
Sector Rotation (SR)

The biggest surprise of 2019 was the significant underperformance of SR, which typically flourishes in environments such as 2019 provided. While SR finished the year with a strong +9.6% December gain to nearly even its books, it ultimately finished with an overall loss of -1.6%. Most of that was attributable to a particularly tough May, when it fell -14.3% as SR pivoted back into tech stocks just as the market took a dive. Despite the off year in 2019, the table on page 24 clearly shows that SR has been the strongest performer among SMI's strategies for many years. Last year served as a reminder of SR's volatility and the unpredictability of its year-to-year returns.

50/40/10

This portfolio refers to the specific blend of SMI strategies—50% DAA, 40% Upgrading, 10% Sector Rotation—dis-

[1] January2018:Cover



MONEYTALK

cussed in our April 2018 cover article, *Higher Returns With Less Risk, Re-Examined*. It's a great example of the type of diversified portfolio we encourage most SMI readers to consider.[1]

The conservative nature of this portfolio was on full display early in 2019. Had the market continued to fall into a bear market, this portfolio's defensive properties would have limited losses dramatically. That's obviously not how 2019's story turned out, but we know bear markets are inevitable, so at some point that *will* be the story. Knowing 90% of this portfolio should outperform an indexed portfolio during a deep market decline likely played a role in helping many investors stay invested in stocks in recent years—perhaps making possible 2019's substantial gains for those who otherwise might not have been willing to stay invested in stocks to as significant a degree.

Gathering a significant portion of the market's gains during rising markets while avoiding the worst of its losses during falling markets is a recipe for superior long-term returns—plus it provides the type of emotional stability so crucial to sustained investing success. ◆

LEVEL 4 / CONTINUED FROM PAGE 25

THE NEW LAW OF THE LAND ON RMDS, IRA CONTRIBUTIONS, AND MORE

Here is a SECURE Act provision *not* related to retirement:

- **Expanded Use of 529 Plan Money:** Up to $10,000 from a 529 education-savings account can now be used to pay down student loans (federal or private), including for a sibling of the named beneficiary. Of course, one goal of 529 plans is to avoid loans in the first place, but if debt already has been incurred, the law now allows 529 money to be paid against that debt.[2]

The new "sibling" provision could be helpful in a situation in which one child goes to a less expensive school, leaving unspent 529 funds in an account for which that child was the beneficiary. Now, money from that account can be applied to school debt incurred by another child in the family. (Note: The $10,000 limit is per child. It is not an overall family limit.)

The SECURE Act also expands "Qualified Education Expenses" allowed under 529 plans to include spending related to participating in a "registered" apprenticeship program, i.e., one certified by the U.S. Department of Labor. ◆

MARKET NOTES, QUOTES, AND ANECDOTES

The market isn't "due" for anything

"...with the stellar performance in U.S. markets over the previous decade, it feels like a correction is warranted. However, if you examine the data you will realize that this thinking is just as flawed as the person expecting a tails after seeing five heads in a row. There is little to no relationship between prior 10-year returns and growth over the next 10 years." – Nick Maggiulli, in a 1/14/20 post on his *Of Dollars and Data* blog about what he called "the investor's fallacy." Read more at bit.ly/2tGTtTP.

Never forget

"If your memory minimizes how much you lost in the last bear market, you can easily overestimate how brave you will be in the next one." – *Wall Street Journal* columnist Jason Zweig, writing on 12/17/19 about how easy it is to forget the damage done by the financial crisis of 2008. While looking at the past through rose colored classes might be good for your mental well-being, he said it could be hazardous to the health of your portfolio. Read more at on.wsj.com/2NLfjMP (paywall).

The investor's edge

"This is easier said than done, but this is the low hanging fruit in the investment world. You can never control the outcome, but you must control your process." – Michael Batnick, in a 12/18/19 post on his blog, *The Irrelevant Investor*. He said an important key to successful investing is maintaining your sanity when the markets get a little crazy. Read more at bit.ly/37k9WMk.

The uncomfortable truth about risk

"The biggest economic risk is what no one's talking about, because if no one's talking about it no one's prepared for it, and if no one's prepared for it its damage will be amplified when it arrives." – Morgan Housel, in a 1/14/20 post on the Collaborative Fund blog about the complicated nature of risk. Read more at bit.ly/2GcgSz6.

What retirees need to know

"...at a bare minimum, anyone embarking on retirement should understand the basics of spending rates: how to calculate them, how to make sure their spending passes the sniff test of sustainability given their time horizon and asset allocation, and why it can be valuable to adjust spending rates over time." – Christine Benz, Morningstar's director of personal finance, reacting in a 11/7/19 article to a study in which 70% of people ages 60 to 75 said they were unfamiliar with the often-mentioned advice that retirees can safely withdraw 4% of their portfolio each year. Many thought it would be safe to withdraw 6% to 8%. Read more at bit.ly/2RzxAiA.

A bias for bias

"People are now talking about behavioral finance so much, and a lot of them are relatively new to it, they almost want to start looking as if there's definitely going to be a bias here. You're biased to find a bias." – Drew Dickson, founder of Albert Bridge Capital, quoted in a 1/13/20 Bloomberg article about the possibility that there may be too much concern over investor bias. Read more at bit.ly/37jkXNV.

[1]Blending multiple strategies adds complexity. Some members may prefer an automated approach.See bit.ly/SMIPrivateClient. [2]For federal tax purposes, the provisions related to paying school loans with 529 funds are retroactive to Jan. 1, 2019. Check with your 529 plan to determine state tax rules.

PREMIUM STRATEGIES

The strategies described below are available to SMI Premium-level members. They have 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

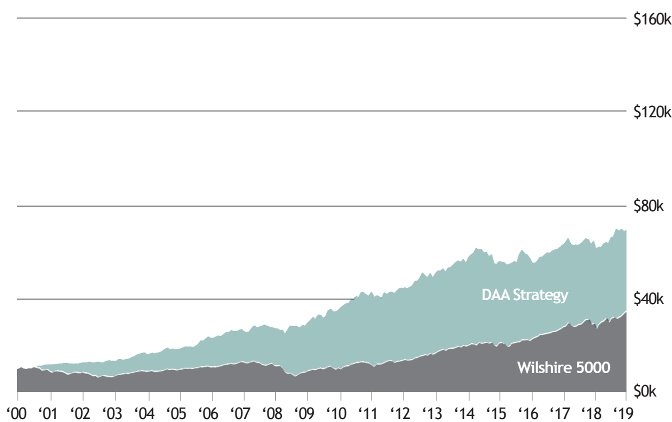
Overview

An investor can use Dynamic Asset Allocation (DAA) in combination with or in place of SMI's Basic Strategies. DAA is designed to help investors 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—by using exchange-traded funds (ETFs). Only three ETFs are held at any one time.

Who Should Consider This Strategy

Anyone—but especially those more concerned with avoiding major losses during bear markets than with capital growth during bull markets. **Pros:** Excellent downside protection during bear markets, as reflected in both a comparatively small worst-case result and a low relative-risk score (see performance table below). Great long-term track record. **Cons:** Subject to short-term whipsaws. Lags the market in "up" years. Making trades promptly and concentrating one's entire portfolio in only three asset classes can be emotionally challenging.

Dynamic Asset Allocation vs Wilshire 5000
Growth of $10,000 January 2001-December 2019



Strategy	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Avg[1]	Worst12[1]	Rel Risk[1]
DAA	7.1%	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%	16.0%	-4.5%	13.7%	10.1%	-13.7%	0.62
Wilshire 5000	-10.9%	-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%	21.0%	-5.3%	31.0%	6.4%	-43.3%	1.00

SECTOR ROTATION

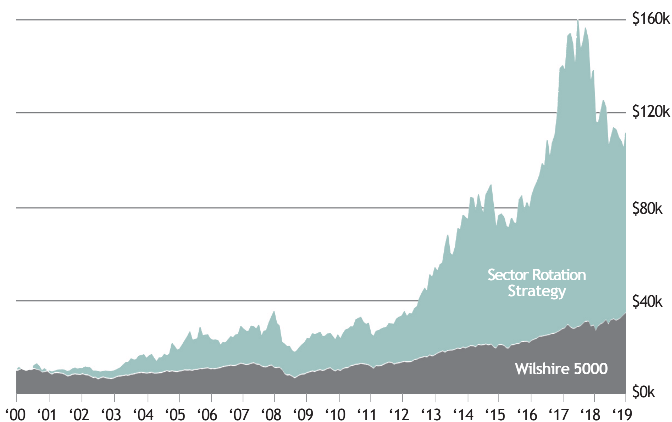
Overview

Sector Rotation (SR) is intended to be used in combination with Just-the-Basics, Fund Upgrading, or DAA (or a mix of these). SR is a high-risk strategy that invests in a single special-purpose stock fund focused on a specific sector (such as biotech, energy, or financial services). Such funds carry a higher degree of risk because they invest in a narrow slice of the economy. In making our fund recommendation, we choose a fund demonstrating especially strong momentum relative to other sector options. Sector Rotation has generated especially impressive long-term returns but with the performance peaks and valleys higher and lower than SMI's other strategies. We suggest that an SR investment account for no more than 20% of one's *total stock allocation*—or, if using SR in combination with DAA, no more than 20% of one's *overall* portfolio.

Who Should Consider This Strategy

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

Sector Rotation vs Wilshire 5000
Growth of $10,000 January 2001-December 2019



Strategy	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Avg[1]	Worst12[1]	Rel Risk[1]
SR	0.7%	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%	16.9%	56.7%	-15.8%	-1.6%	13.0%	-38.6%	1.90
Wilshire 5000	-10.9%	-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%	21.0%	-5.3%	31.0%	6.4%	-43.3%	1.00

[1]The three data points at the far right in each performance table cover the full 20 years from Jan2000-Dec2019. "Avg" shows the average annualized return over those 20 years. "Worst12" represents the worst investor experience over 217 rolling 12-month periods during those 20 years.

PERIODICALS POSTAGE
PAID AT LOUISVILLE, KENTUCKY

Dated Investment Material
Please Do Not Delay!

PERFORMANCE DATA

SOUND MIND INVESTING MODEL PORTFOLIOS • DATA THROUGH DECEMBER 31, 2019

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]	31.0%	2.9%	9.1%	31.0%	14.5%	11.4%	13.4%	9.1%
Just-the-Basics[2]	28.1%	2.9%	9.0%	28.1%	12.5%	9.5%	11.7%	8.4%
Stock Upgrading[3]	21.7%	2.3%	5.9%	21.7%	9.8%	8.0%	10.2%	8.2%
U.S. Bond Market[4]	8.6%	-0.2%	0.0%	8.6%	3.9%	2.9%	3.6%	4.0%
Bond Upgrading[5]	8.5%	0.0%	0.1%	8.5%	3.4%	2.4%	4.9%	5.8%

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]	13.7%	0.8%	0.5%	13.7%	8.0%	3.1%	7.9%	9.3%
Sector Rotation	-1.6%	9.6%	4.4%	-1.6%	9.1%	6.5%	16.1%	14.1%
50-40-10 Blend[7]	15.4%	2.2%	3.1%	15.4%	9.1%	5.6%	9.8%	9.8%

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 recommended funds. • [4] Based on Bloomberg 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] For a portfolio allocated 50% to DAA, 40% to Stock Upgrading, and 10% to Sector Rotation. See the April 2018 cover article for details. 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 12/31/2019	Year to Date	1 Month	3 Months	12 Months	3 Year Annual	5 Year Annual	10 Year Annual
SMIFX	19.29%	2.21%	5.98%	19.29%	8.56%	5.99%	8.65%
Wilshire 5000	31.02%	2.93%	9.08%	31.02%	14.52%	11.38%	13.44%
S&P 500	31.49%	3.02%	9.07%	31.49%	15.27%	11.70%	13.56%

Quarterly Returns as of 12/31/2019	Year to Date	1 Month	3 Months	12 Months	3 Year Annual	5 Year Annual	10 Year Annual
SMIFX	19.29%	2.21%	5.98%	19.29%	8.56%	5.99%	8.65%
Wilshire 5000	31.02%	2.93%	9.08%	31.02%	14.52%	11.38%	13.44%
S&P 500	31.49%	3.02%	9.07%	31.49%	15.27%	11.70%	13.56%

Total/Gross expense ratio: 2.04% as of 2/28/19 (includes expenses of underlying funds)
Adjusted expense ratio: 1.16% as of 2/28/19 (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).

DATA COPYRIGHTS AND NECESSARY CAUTIONS

Copyright © 2020 by Morningstar, Inc. All Rights Reserved. The mutual fund data contained herein: (1) is proprietary to Morningstar and/or its content providers; (2) may not be copied or distributed; and (3) is not warranted to be accurate, complete or timely. Neither Morningstar nor its content providers are responsible for any damages or losses arising from any use of this information. Past performance is no guarantee of future results.

Copyright © 2020 by Sound Mind Investing. All rights reserved. No part of these rankings may be reproduced in any fashion without the prior written consent of Sound Mind Investing. SMI is not responsible for any errors and/or omissions. You are encouraged to review a fund's prospectus for additional important information. Other than the SMI Funds, SMI has absolutely no financial incentive to favor or recommend one broker or mutual fund over another.