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Answering the Big Questions About the Dollar

Few Americans have developed expertise in understanding the implications of fluctuating currency prices. But the dollar's valuation plays a crucial role in the operation of global and domestic financial markets. A working knowledge of the basics can help investors understand what's driving the markets today—as well as what to expect in the future.

by Mark Biller

It's odd, but Americans tend to give less thought to the value of the U.S. dollar than people who live elsewhere. In some countries, citizens are nearly as aware of the dollar's current value and trend as they are about their own currency. Here in the states, in contrast, because we both earn and spend in U.S. dollars, most of us barely notice the ebbs and flows of the dollar's value—except perhaps when they affect us at the gas pump or grocery store. As a result of being largely insulated from the impact of global currency fluctuations, most Americans have little grasp of such things as the dollar's role in the worldwide economy, the factors that influence the dollar's valuation, and the implications of changes to that valuation.

This article is an effort to lay a bit of groundwork regarding the dollar's most important aspects. What is the U.S. dollar's role in the global trade system? How did that system evolve to its present state? How does inflation factor into all this? And, ultimately, what are the implications for investors?

Understanding *currency* markets isn't easy. It doesn't come naturally to most of us to think about these subjects because we rarely need to. But grasping these concepts will help us better understand the *financial* markets.

Global reserve currency

You may have heard the dollar referred to as the global "reserve currency." What does that mean? The answer is complicated. Economists and historians have written entire books about the internatinal financial system leaving the "gold standard" and transitioning to the "dollar standard." Don't worry—this article isn't a deep dive into all that! Instead, we'll offer a short-and-sweet introduction to global reserve currencies.

The reason the world needs a "reserve currency" is to facilitate international trade. For example, if Mexico buys oil from Saudi Arabia, the Saudis would prefer not to be paid in Mexican pesos. Instead, the Saudis want payment in a currency they can quickly turn around and use in their trade with many other countries.

Before 1945, when most of the world was on some version of the "gold standard," currencies were valued relative to gold. This meant that buying and selling in any currency was rather straightforward. All currencies converted to gold based on a simple ratio that everyone could rely on.

Near the end of World War II, the Allied nations held a conference at Bretton Woods, N.H., to deter- *(continued on page 131)*

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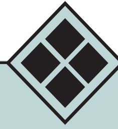
"FOR GOD HAS NOT GIVEN US THE SPIRIT OF FEAR BUT OF POWER, AND OF LOVE, AND OF A SOUND MIND."



EDITORIAL

The 7 Qualities of a Disciplined Investor

When it comes to investing, *learning* what you're supposed to do is relatively easy. But *doing* what you're supposed to do, well, that's surprisingly hard. We can be our own worst enemies, especially when the market becomes unusually volatile, as it has this year.

The one quality that separates the top professionals from the rest of us can take years to develop: emotional self-control. Our emotions interact with news and market events in ways that incline us to act at precisely the wrong time. We all want to "buy low and sell high," but emotionally, it's quite difficult to do either. Experience shows that most investors do the opposite.

For example, few investors are willing to "sell high," even after an extended bull-market run when the caution signs of high valuations are all around. Man's natural greed tends to kick in and investors want to make even more.

Nor is it easy to "buy low." The reason that prices drop is that the economy is weak, the news is bad, and people are pessimistic or uncertain. Investors feel pressured. And under pressure, emotions tend to dictate our actions. As uncertainties increase, so do our anxieties. Rather than buy, we tend to wait for information that is more positive, but it never seems positive enough. We become paralyzed. Why? Emotions.

As you know, SMI's does *not* recommend that you attempt to buy and sell at market lows and highs. The mechanical process built in to Dynamic Asset Allocation and Fund Upgrading 2.0 will tell you if and when to make portfolio changes.

Still, even following a rules-based strategy requires self-discipline if we are to overcome our emotions and trust the system. Here are a few suggestions for how to grow in that area:

● **Be humble.** Accept that "there's nothing new under the sun" (Ecc. 1:9), and that the instructions God has given us in His Word have proven to be practical and effective. There's safety in following the priorities and guidelines He has provided for our protection. Abandoning them can only mean we have more confidence in our own thinking than in His.

● **Be conscientious.** You must see yourself as a caretaker of what God has given you. Acknowledge that taking undue risks jeopardizes His wealth. You're not just in this for yourself, but to responsibly increase your assets so you can provide for your family and give more generously. You want to play your part in taking the gospel of Christ to the millions who have never heard.

● **Be prepared.** Develop a written plan that lays out your investment strategy, one that reflects your personal goals and an appropriate level of risk. Understand how all the parts of your portfolio fit together and the role that each part plays. Then let your buying and selling be dictated *solely* by your plan. You're to be an initiator, not a responder to ever-shifting market news.

● **Be content.** A preoccupation with large profits can be dangerous (1 Tim. 6:9-10), so as you draw up your plan, be reasonable in your financial ambitions. Surely, more money is lost due to greed than any other single factor. Accept the fact that annual gains of 8%-10% over time are most likely.

● **Be diversified.** Make sure your plan divides "your portion to seven, or even to eight, for you do not know what misfortune may occur on the earth" (Ecc. 11:2). To be sure, higher profits can be made by concentrating your money in one or two opportunities, but staggering losses can be incurred as well. By avoiding the temptation to concentrate your holdings, no loss will devastate you.

● **Be patient.** Taking your cue from the Parable of the Talents (where the master was away for "a long time"), make your strategy a long-term one that aspires to build wealth slowly. This will allow you to take up-and-down market cycles in stride. Time is the enemy of the speculator, but the friend of the investor.

● **Be accountable.** Show your plan to your spouse or a trusted Christian friend, and review it with them quarterly to show how you are being faithful in following it. Any thoughts of taking steps outside your strategy will be tempered by your realization that you will have to give an accounting.

Taking these steps will help assure that you are honoring the Lord and His priorities as you strike a wise balance between the risks and rewards of the marketplace. Then, while occasional bear markets and economic storms may threaten, you can be of good cheer, for the Lord has said: "I will instruct you and teach you in the way you should go;
I will counsel you and watch over you....
The LORD's unfailing love surrounds the man who trusts in Him"(Psalm 32:8,10).

AUSTIN PRYOR
FOUNDER/PUBLISHER

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POSTMASTER
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Answering the Big Questions About the Dollar

(continued from front page)

mine the post-war economic system. It was no longer feasible for the world's currencies to be linked to gold because many countries had depleted their gold reserves to pay for the war. Indeed, much of their gold had made its way to the U.S. as payment for war supplies. The new solution: Link their currencies to the U.S. dollar, which in turn was linked to gold.

Thus the global financial system transitioned to a "dollar standard," with the dollar backed by gold. The U.S. dollar became the global reserve currency—the asset held by central banks around the world to back the value of their own currencies. Any country could give dollars back to the U.S. and get gold in exchange at a fixed rate. As such, the dollar became the primary currency the world used for global trade.

In 1971, President Richard Nixon "closed the gold window" and ended that convertibility to gold. The U.S. dollar remained the global reserve currency, but it became a "fiat" currency (along with all the other major currencies). The dollar is not backed by gold nor redeemable in gold, and it lacks intrinsic value. The dollar is money only because the U.S. government has decreed it to be money. So since 1971, the value of most currencies "float." They move up and down relative to all the other currencies, with the market determining the relative value of each.[1]

Returning to our earlier example, the fact that the dollar is the world's reserve currency means that when Mexico buys oil from Saudi Arabia, it pays in dollars. When Spain buys natural gas from Russia, it pays in dollars. And so on. This arrangement isn't universal—some trade is done in local currencies rather than dollars. For example, the 27 nations of the European Union conduct trade between members in Euros. But the latest available data show that more than half of global trade is conducted in dollars. Further, roughly half of the dollars in circulation are outside the U.S.

U.S. imports add liquidity to the global system

Given that so much international trade is settled in dollars, it's obvious why there is a constant demand for dollars around the globe. How does the rest of the world get these dollars? Primarily from U.S. purchases of overseas goods. When the U.S. *imports* goods from the rest of the world, we pay in dollars, making those dollars available to other countries for global trade. When we *export*, the rest of the world pays us in dollars, taking those dollars out of the international trade system. In short, the global dollar system gains liquidity when America imports more than it exports.

Those dollars circulate internationally, and other countries can use any *surplus* dollars to buy U.S. Treasury bonds. Particularly after the gold window closed in 1971, U.S. Treasuries became the primary global reserve *asset*, largely replacing gold as the asset every country wanted to hold for stability and instant liquidity.

This development suited the U.S. well. It meant constant demand for U.S. Treasuries—which meant we could run continual budget deficits and finance them by issuing more Treasuries every year! (The temptation to characterize the U.S. as an immoral overspender is at least lessened when one realizes much of this dynamic benefits the rest of the world and keeps the global dollar trade system running smoothly.)

Problems arise

The global reserve currency system, based on the U.S. dollar, is far from perfect. For one thing, it has led to a fairly unbiblical approach to debt, which has caught up to us in the form of slower economic growth. The U.S. also has gradually awakened to the fact that, by exporting much of our manufacturing and production capacity, we've sent millions of jobs overseas and hollowed out our middle class. Further, we've been left strategically vulnerable as we now rely on other nations to produce many of the goods we need. (The recent COVID crisis has laid bare how problematic it is to rely on a potentially unfriendly trading partner for key strategic needs such as medical supplies, antibiotics and drugs, as well as microchips and rare earth minerals needed for defense and communications gear.)

In recent years, the growth of U.S. energy production has presented a new challenge to the reserve currency system. As America has transitioned from being the world's largest energy *importer* to the largest energy *producer*, the international dollar system we've been discussing has become strained because fewer dollars are flowing out to the rest of the world as payment for U.S. oil imports. There's a deeper story here, but suffice it to say that the worldwide *demand* for dollars is as high as ever, but the *supply* of dollars circulating outside the U.S. has been reduced. That situation is stressing the global financial system. Many of the hard-to-explain dynamics in the financial markets in recent years—the "repo" crisis last fall,[2] the Treasury-market panic in March[3]—ultimately can be traced to this global imbalance in the supply and demand for dollars.

Compared to what?

Investors often hear about the dollar being "strong" or "weak" but may not understand what these terms mean. The key to understanding changes in dollar valuation is grasping the fact that currencies are always gaining or losing ground *compared to something else*.

When the dollar is said to be *weakening*, as it has since March, it is typically being compared to a basket of other currencies. The easiest way to think of this is that a weakening dollar buys less of the other currencies than it used to. In contrast, a *strengthening* dollar buys more of the other currencies.

We can extend this same concept to other measures, such as gold. A rising gold price means that it takes more dollars now to buy an ounce of gold than it used to. Since the amount of gold worldwide is relatively stable, the rising price indicates the dollar is *weakening* relative to gold.

Thinking in these terms helps things to come into focus. The fact that gold recently has set new all-time highs when priced in *virtually all currencies* means that, as a group, paper currencies have *all* been weakening relative to the fixed standard of gold. This weakening makes sense in light of the massive money-creating liquidity measures most governments and central banks have turned to in response to the COVID crisis.

[1]For a more detailed discussion, see *Inflation Report: The Rise and Fall of the U.S. Dollar*. This SMI bonus report was written in 2011, but the historical background is timeless. The report is available online under *Resources*. [2]bit.ly/SMI-Repo [3]April2020:p56

We also can discuss a particular fiat currency strengthening or weakening relative to another currency (for example, the dollar vs. the euro). The long-term dollar chart below communicates several important messages. First and foremost, it shows that relative to a basket of other currencies, the U.S. dollar has been both much stronger (the 1980s and early-2000s) and much weaker (early-1990s and 2008-14) than it is today. That history serves to refute the idea that current policies risk the dollar losing its place as the world's reserve currency. The dollar's value has varied much more in the past than it has lately without jeopardizing that reserve status.

That's not to say that recent changes in the dollar's value aren't significant, however. While Americans may not feel those changes as acutely as people in other nations do, the changes aren't without impact. A past example may be helpful: As the dollar fell from 2002 (center of chart) to its low in 2008, the price of a barrel of oil rose from $28.50 to $165! That type of decline in purchasing power is painful.

Of course, the falling dollar wasn't the *only* reason for soaring oil prices then, but it was a significant factor. The prices of other commodities verify this. For instance, gold tripled from $300/oz. to $1,000 during that same 2002-2008 period. The relationship between the dollar and commodity prices was clear in the other direction too: As the dollar rose from 2011 to 2017, oil declined from $131/barrel to $48, while gold dropped from $1,900/oz. to $1,100.

Which assets are impacted most by changing dollar prices?

As these examples indicate, one of the first places changing dollar valuations tend to show up is commodity prices. Commodity prices aren't the full measure of inflation, but they are an important component in terms of their tangible impact on most households. Since the dollar started declining in March of this year, a broad basket of commodity prices is up +26%. Again, this increase isn't *solely* attributable to the dollar's decline, but the decline has contributed. Gold and oil are often the most visible examples, but the same dynamic influences other commodity prices as well—from food items to copper, lumber, etc. (although each market has its own individual factors).

Another asset class that tends to respond strongly to changes in dollar valuation is foreign stocks, and even more specifically, emerging markets stocks, which tend to be closely tied to commodity exports. Through much of the 1980s and again in the 2000s, the dollar *fell* and foreign stocks outperformed U.S. stocks. In contrast, when the dollar *rose* during the 1990s and 2010s, U.S. stocks handily outperformed foreign.

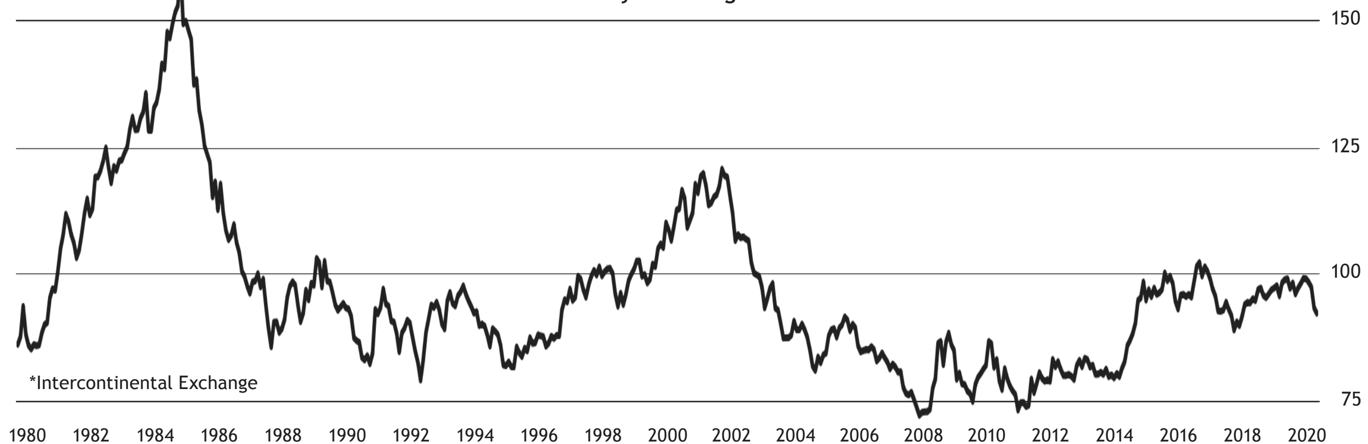
Ben Carlson recently reported in *Fortune*[1] that from 1974-2019—even though S&P 500 performance didn't vary much between years when the dollar strengthened vs. weakened—the gap for certain other asset classes was huge. Foreign stocks earned an average of +2% in years the dollar rose, but +18.6% in years it fell. Emerging markets were even more extreme: +2.7% when the dollar rose vs. +22.5% when it fell. And gold declined an average of -0.8% in years the dollar rose but soared +17.6% on average when the dollar fell.

We've already discussed why this makes sense for gold. Here's why that happens for foreign stocks. In addition to the gain or loss a foreign stock earns as measured in its local currency, an investor in such stocks also earns a gain or incurs a loss when exchanging that local currency to their own. In the case of U.S. investors, when the dollar falls relative to the local currency, they get the stock's gain in the local currency *plus* the currency-conversion gain as the local currency is exchanged back into even more dollars.

How does this factor into inflation?

Nobel Prize-winning economist Milton Friedman famously said that inflation is "always and everywhere a monetary phenomenon." He meant that if the supply of money in a country rises faster than the rate of growth of that country's economy, there will be inflation. Based on what we've discussed so far, this is easy to understand: An increase in the number of dollars chasing the same amount of goods and services is the natural formula for inflation. With current policies vastly increasing the U.S. money supply, it's natural for concerns about inflation to emerge.

However, the aftermath of the Global Financial Crisis in 2008 demonstrated that inflation is a tricky thing to forecast.



[1] bit.ly/3fUH2G3

Significant inflation was a consensus expectation coming out of the GFC, based on fears of exploding debt levels and the relatively new "quantitative easing" (QE) policies pursued by the Fed. But that inflation never materialized. Few understood at the time that banks retained much of the liquidity created to repair their devastated balance sheets. Without that money being passed through to the broader economy in the form of loans, there was no significant increase in the amount of money spent and therefore no inflation. In technical terms, the *velocity* of money slowed even as its *supply* increased.

Furthermore, having now been able to observe the effect of QE policies for more than a decade, both here in the U.S. and even longer in Japan and Europe, it's clear that the impact of such policies has been different than initially expected. Rather than spur higher growth and higher inflation, it's now clear that QE tends to *inhibit* economic growth, which acts as a lid on inflation. As inflation consistently failed to materialize from ever-more global QE, the fear of inflation disappeared. This freed bond yields to move lower.

That said, there are potentially crucial differences between the Financial Crisis response a decade ago and 2020's policy response. One is that the 2020 response has targeted the real economy via *fiscal policy* (government spending) to a greater extent than was the case in 2008. For example, in 2008 it took months for Congress to pass an additional $25/week Federal unemployment benefit. In 2020, an additional $600/week benefit passed with incredible speed. This *24x increase* in the level of support is emblematic of the overall government response targeting households, small businesses, and so on. Much more of this "emergency" money is reaching the real economy than it did a decade ago, potentially making it a more inflationary factor. As a result, inflation concerns are growing as commodity prices rise and broad inflation readings increase.

But before we get too excited about inflation and repeat the errors of a decade ago, it's important to point out that the current economic crisis is deeply *de*flationary. Huge increases in debt, such as we have been accumulating, have always been deflationary. Typically, debt levels decrease during recessions—this is the first recession during which total debt (government, corporate, and household) has increased. All that debt inhibits future growth. Inflation isn't *impossible* in a low-growth environment, but it's less likely.

In terms of the dollar as a specific catalyst to inflation, the long-term chart (previous page) shows that over the past two decades we've experienced dollar valuations both 20% *higher* and 20% *lower* than today, with no significant changes to the disinflationary trend (meaning we've still had inflation, but at declining levels). All of this suggests that while inflation may finally turn higher in the years ahead as growth (hopefully) returns, it's not clear that the recent increase signals a change in the long-term trend.

Short-term expectations require longer-term context

The combination of the dollar falling roughly -10% since March coupled with explosive gains in precious metals and certain other commodities, has given new life to decades-old concerns that our government's unrestrained spending eventually will "crash the dollar." But most of these recent moves have been rather small when looked at in context.

Yes, the dollar has fallen steadily since March. But why was it so high in March to begin with? Because when a crisis hits, the whole world wants to own dollars—the flight-to-safety response is what drove the dollar higher in the first place. As COVID fears have receded, the unwinding of that safe-haven dollar positioning has caused it to fall. Remove the March spike and things look quite different: the U.S. Dollar Index started 2020 around 96.5 and sits at 93.0 today (late August). That's a tiny move when viewed against the longer-term dollar chart.

The commodities story, which has become a driver of the "emerging inflation" narrative, is similar. Yes, a broad basket of commodities is up +26% since March. But that same basket would need to gain *another* +20% just to get back to the level at which it began 2020! Looking back further, even after this year's rise, commodity prices as a whole are still down more than 50% from 2011 levels.

For these reasons, we're not convinced we're on the verge of dramatic dollar or inflation changes. But there is a *longer-term* message here: the breakouts in precious-metal prices across currencies signal widespread concern that governments are debasing their money in the same way that eventually has ruined other fiat currencies. (For current examples of hyperinflation, see Venezuela, Lebanon, and Zimbabwe.) It's also increasingly clear that governments can't support their level of debt without direct support from central banks. That's a new and troubling trend that points to a potentially inflationary future.

But until the U.S. decides it wants another significant change in the global monetary system, as it did in 1944 and again in 1971, there is no viable alternative to the dollar in the global system. While the U.S. dollar's value may continue to decline somewhat, there's an important bias in the current system that exerts steady *upward* pressure on the dollar. Specifically, the U.S. remains the "least dirty shirt in the drawer"—most of the world is *even more* indebted than we are, with worse demographics and slower economic growth. In addition, our interest rates, while low, remain positive—a stark contrast to the $15 trillion of foreign government bonds trading with negative yields today. Those factors explain why the overall trend in the dollar over the past decade has been *higher*, not lower.

There's no question the dollar has been declining while inflation has been increasing in recent months. But it seems premature to declare these new trends have staying power, even if longer-term both a lower dollar and higher inflation seem the most likely outcomes of current Fed and Treasury policy. Should the global economic recovery falter, it's entirely possible we could temporarily see the dollar move higher and inflation decline again.

The good news for investors is that SMI's strategies have built-in mechanisms to respond to changes in dollar valuation and inflation. So rather than needing to *anticipate* when these longer-term trends will take hold, our portfolios will respond to the unfolding trends automatically. Even so, we'll keep a close eye on these themes and explore them further as conditions dictate. ◆

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

INVEST IN YOUR 401(K) OR PAY DOWN YOUR HOME MORTGAGE?

"We'd like to start prepaying our mortgage. But we also want to invest as much as we can for retirement. Which should have the priority?" That's a common question—but there's no one-size-fits-all answer. Considerations include your age, tax bracket, attitude toward debt, and how long you expect to live in a particular house.

Another factor is whether you gain any tax savings from paying mortgage interest. Under a 2017 change in the law, fewer taxpayers are eligible for such a deduction.

Today, a married couple filing jointly needs to have more than $24,800 in deductible items (2020 threshold) to make itemizing worthwhile. (Deductible items include things such as mortgage interest, charitable giving, and property taxes.) Nearly 9 out of 10 of tax-paying households now take the *standard* deduction, according to the Tax Foundation, meaning that the tax deduction for mortgage interest benefits only a relatively small minority of homeowners.

That being the case, our analysis assumes no tax savings related to paying a mortgage.[1]

Two approaches

Let's say two SMI members are wrestling with the prepay-vs-invest decision. Rex is concerned about the long-term health of Social Security, so he focuses on building his retirement savings. In contrast, Mort is more concerned about reducing debt, so he plans to make additional principal payments on his mortgage.

For comparison purposes, let's make Rex and Mort's hypothetical situations identical:

- Both have new $180,000, 15-year, 3% fixed-rate mortgages;
- Both can set aside $1,500 out of each month's paycheck—their mortgage payments are $1,243, leaving each an extra $257 for investing in a retirement account or prepaying principal;
- Both have an opportunity to contribute to a retirement plan at work that will earn 6% year-in and year-out (remember, this is hypothetical).

Rex—the one focused on retirement—contributes his $257 monthly to his 401(k) plan. Mort—the one concerned about getting out of debt—skips his company's retirement plan for now and uses his monthly $257 surplus to make extra principal payments on his mortgage.[2]

Now here's where it can get slightly confusing. Both Rex and Mort are in a 30% tax bracket (federal plus state). Neither gets a tax benefit from paying mortgage interest. However, Rex gets a tax break for putting money in his company's tax-deferred traditional 401(k) retirement plan: He avoids state and federal taxes (until withdrawal) on any income he contributes to the plan.[3]

That means Rex's $257 retirement-account contribution is worth $77 in tax savings, which he also puts into his 401(k). But then that $77 contribution saves him another $23 in taxes, which he'll put into his 401(k). But then that $23...well, you get the idea. Suppose Rex took immediate advantage of all these tax savings. If so, he can afford to put $367 into his retirement plan each month—i.e., his $257 monthly surplus plus $110 in tax savings generated by contributing to the company 401(k). As shown in the nearby table, his $367 monthly contribution works out to $4,404 per year.

While Rex is making the payments on his mortgage ($1,243 a month) and socking away $367 a month in his retirement account, Mort is making his regular mortgage payment (also $1,243) and prepaying an additional $257 each month. Ultimately, those prepayments shave more than three years off Mort's 15-year loan. In just under 12 years, he's paid his mortgage in full! (At that point, Rex still owes more than

(continued on page 140)

REX EMPHASIZES SAVING FOR RETIREMENT

Year	Yearly 401(k) Contribution ($367/mo)	Year-End Mortgage Balance	Year-End Value of 401(k)*
1	$4,404	$170,351	$4,546
2	$4,404	$160,410	$9,364
3	$4,404	$150,165	$14,472
4	$4,404	$139,609	$19,886
5	$4,404	$128,732	$25,265
6	$4,404	$117,524	$31,709
7	$4,404	$105,975	$38,157
8	$4,404	$94,075	$44,992
9	$4,404	$81,813	$52,238
10	$4,404	$69,178	$59,918
11	$4,404	$56,159	$68,059
12	$4,404	$42,744	$76,688
13	$4,404	$28,921	$85,835
14	$4,404	$14,677	$95,531
15	$4,404	$0	$105,809
Totals	**$66,060**	**$0**	**$105,809**

*Assumes 6% annual growth rate.

MORT EMPHASIZES PAYING OFF HIS MORTGAGE

Year	Yearly 401(k) Contribution	Year-End Mortgage Balance	Year-End Value of 401(k)*
1	$0	$167,225	$0
2	$0	$154,061	$0
3	$0	$140,497	$0
4	$0	$126,520	$0
5	$0	$112,118	$0
6	$0	$97,278	$0
7	$0	$81,987	$0
8	$0	$66,230	$0
9	$0	$49,994	$0
10	$0	$33,265	$0
11	$0	$16,027	$0
12	$2,262	$0	$2,275
13	$23,400	$0	$26,565
14	$23,400	$0	$52,313
15	$23,400	$0	$79,605
Totals	**$72,462**	**$0**	**$79,605**

*Assumes 6% annual growth rate.

[1]For an analysis that takes the mortgage-interest deduction into account, see pp. 32-34 of *The Sound Mind Investing Handbook*. [2]We assume neither man's employer offers matching contributions. [3]State tax laws vary. We assume Rex and Mort live in a state that treats traditional 401(k) contributions as "pre-tax."

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

DON'T LOOK! BLISSFUL IGNORANCE CAN BE YOUR INVESTING ALLY

In February, the U.S. stock market ended its remarkable 11-year bull run in stunning fashion—falling 35% in only 16 trading days. Fear filled the headlines as Americans grew concerned about what a fast-spreading pandemic might mean for personal safety, the health of the economy and stock market, and life as we had come to take for granted.

Equally stunning was the market's sudden recovery. By mid-August, the S&P 500 had fully regained its lost ground and reached a new high.

Here is a "thought experiment." Suppose that as stock prices were moving higher in the early weeks of this year, you were checking your investment performance every day. As your portfolio steadily moved higher, you would have been happy and content, knowing that your investments were paying off and that the bull market was continuing. But as the market began plummeting, beginning in February and accelerating in March, the barrage of panicky reporting would have caused your anxiety to shoot higher. Result: High stress!

Now, thought experiment #2: Suppose that while these market gyrations were going on, you were *not* checking your investments regularly (or reading/watching financial news!). Instead, you were enjoying time with family, catching up on some good books, and improving your daily faithfulness to spiritual disciplines. As the market tumbled in February and March, you were blissfully unaware. You had other things to do. If you checked your portfolio balance in mid-August after last checking it in mid-February, you might have thought it had been a dull year in the market! The result: No stress.

Here's the point. Unless you just happen to like high levels of anxiety, it doesn't pay to follow the daily performance of your portfolio. Sure, it may seem like such information is helpful, or at least not harmful. But most of us aren't wired to process significant swings in our investments without a commensurate swing in our emotions.

If your investing time frame is more than five years—which it should be for you to be in the stock market at all—there's a strong likelihood (if history is any guide) that the dollars you invest today will appreciate by the time you need to take them out.

S&P 500 STOCK INDEX
DAILY CLOSE: 1/02/20 - 8/18/20

The longer your time frame, the more the odds are in your favor. As the old saying goes, "It's *time in the market*, not *market timing*, that makes the difference."

Applying this within SMI's framework

SMI's strategies rely on a systematic process of regularly reviewing each model portfolio and taking action based on predetermined criteria as required. So we're not saying everyone should invest by simply "setting it and forgetting it."

But there's a big difference between the periodic review process called for by the SMI strategies—which require attention once per month when strategy updates are issued[1]—and the norm for many investors, which is checking their portfolio every day, or even multiple times throughout the day!

It's crucial to keep in mind that even when using a disciplined framework such as SMI's, not every move will be profitable. At times, as with Upgrading 2.0 this year, we'll look back and think, "Well, that move didn't work!" But even in those times, we're making changes based on a well-researched, predetermined plan that has a strong historical basis for why the moves *should* work more often than not. Although we know in advance that not every move will be a winner, we believe that consistently executing on such a framework will lead to long-term success while minimizing anxiety along the way.

Plan your market exposure in advance

Financial columnist Jason Zweig has drawn attention to the research of Harvard psychologist Paul Andreassen in the late 1990s, which showed that investors who *ignored* the financial news earned more than those who closely followed it. Zweig's conclusion? "Stop checking your watch so often. Investing is a marathon, not a sprint."

Being successful over the long haul requires that you *protect yourself from your emotions*. You must train yourself to think like a long-term investor rather than a short-term trader. That involves establishing a realistic long-term investing plan and sticking with it through thick and thin.

If you're manually implementing SMI's strategies, the only time you *need* to look at your portfolio is once a month when the strategy you're following is updated. (If even monthly exposure tempts you to make unplanned changes, you may want to choose an automated option that implements the SMI strategies on your behalf, removing you from that monthly process.[2])

So if watching your portfolio go up and down has you stressed out, the simple solution is to just look the other way—until your plan tells you it's *time* to look. When that time comes, take whatever action is needed (based on the strategy you're following). Then get on with your life, and no peeking in between updates! ◆

[1]Just-the-Basics investors need to check only once a year. [2]www.smifund.com or www.smiprivateclient.com

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

DIVERSIFICATION: THE ONLY FREE LUNCH IN INVESTING

In celebration of SMI's 30th anniversary, we're highlighting some of the core beliefs and principles that guide our work. This column often highlights specific diversification ideas, but this month we want to pull back and take a broader view: why do we diversify a portfolio in the first place?

Most investors would like to be invested in the top-performing market segment year-after-year. In pursuit of this goal, many chase performance by continually shifting their portfolios toward what's hot. For example, as Large/Growth companies—such as Facebook, Amazon, and Apple—have outperformed recently, investors have piled into the funds and indexes that highlight these stocks.

A common problem with this kind of "performance chasing" is that many investors get into a hot segment just as it is about to cool off! As that segment falls from favor, those investors experience a lot of volatility in their concentrated portfolios and end up with poor relative returns. Disappointed, they jump to the next hot segment and repeat the cycle.

While there's a place for emphasizing what's currently working in the market within your portfolio (all of SMI's active strategies contain an element of this "momentum" approach), it's crucial to do that from within a diversified framework.

Diversification ensures that some of your money will always be in the best-performing segment. Of course, some will be in other segments as well, including those that aren't so hot at the moment. While that may not be as exciting as loading up on the "latest and greatest," diversification provides a less risky and more even-keeled way to make your money grow over time.

Reviewing a decade of performance

The chart below is a variation of the "Periodic Table of Investment Returns." We've modified the table to include only the five major stock-risk categories tracked by SMI's Stock Upgrading strategy. The columns show the year-by-year average returns for all the mutual funds in each of those five categories, with the best-performing category at the top and the worst at the bottom.

The first column is a summary of 2011—not a great year for investors. In the top square, you'll see that the best performer—Large/Value funds—lost -0.8% that year. Each subsequent square below shows the returns for another risk category. The bottom-dweller in 2011 was the Foreign funds category, posting a loss of -14.3%.

The table layout makes it easy to see how each category has fared relative to the others over the past decade (or nearly a decade). The colors help you visually track a particular category from year to year.

As you can see, each market segment has gone through years of strength and years of weakness. Each of the five enjoyed at least one year as the top performer, but three of the five also spent time at the bottom.

Further, the chart illustrates how a segment's relative performance can be volatile from one year to the next. An example is the relative performance of the Small/Value and Foreign categories. In 2015, Small/Value funds were the worst performers, while Foreign funds were second best. In 2016, this reversed strongly, with Small/Value taking the top spot, Foreign the bottom spot, and Small/Value outperforming Foreign by a whopping 25 percentage points! *(continued on page 140)*

PERIODIC TABLE OF INVESTMENT RETURNS

2011	2012	2013	2014	2015	2016	2017	2018	2019	2020 (7 mos)
Large Value -0.8%	Foreign Stocks 18.9%	Small Growth 40.9%	Large Value 10.2%	Large Growth 3.6%	Small Value 26.0%	Foreign Stocks 28.9%	Large Growth -2.1%	Large Growth 31.9%	Large Growth 15.5%
Large Growth -2.3%	Small Value 16.0%	Small Value 36.2%	Large Growth 10.0%	Foreign Stocks 1.5%	Large Value 14.8%	Large Growth 27.7%	Small Growth -5.8%	Small Growth 27.7%	Small Growth 5.5%
Small Growth -3.6%	Large Growth 15.3%	Large Growth 33.9%	Small Value 3.3%	Small Growth -2.4%	Small Growth 11.2%	Small Growth 21.5%	Large Value -8.5%	Large Value 25.0%	Foreign Stocks -6.7%
Small Value -4.5%	Large Value 14.6%	Large Value 31.2%	Small Growth 2.4%	Large Value -4.1%	Large Growth 3.2%	Large Value 15.9%	Small Value -15.5%	Foreign Stocks 22.8%	Large Value -12.2%
Foreign Stocks -14.3%	Small Growth 13.2%	Foreign Stocks 22.4%	Foreign Stocks -5.4%	Small Value -6.7%	Foreign Stocks 0.8%	Small Value 8.5%	Foreign Stocks -16.8%	Small Value 21.4%	Small Value -20.8%

Data source: Morningstar

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

WHICH ASSETS SHOULD YOU WITHDRAW FIRST DURING RETIREMENT?

By Eric J. Reinhold, CFP®, APMA®, MBA[1]

Once you reach retirement and begin drawing from the storehouse of wealth you've worked so hard to accumulate, two questions arise. First, how much can you withdraw each year without running the risk of depleting your reserves prematurely? We looked at that issue last month.[2] Second, which asset accounts should you draw from first? This is an often-overlooked question because banks, brokers, and mutual fund companies are typically more focused on soliciting your business and guiding your investments than helping you develop a strategy for *withdrawing* your retirement savings.

Let's look at four of the most common retirement vehicles: traditional (i.e., tax-deductible) IRAs, Roth IRAs, tax-deferred annuities, and taxable investments. For this discussion, I'll assume any Roth 401(k) assets have been rolled over into a Roth IRA and that any pension plan assets from your place of employment have been rolled into a traditional IRA.

The starting point is to answer this question: "Is my intention to pass a significant portion of these assets to my family, or will I be using them for myself?"

- **To favor your heirs, withdraw from your annuity and IRAs first.** Let's suppose you desire to maximize what you can pass on to your family after your death. This means you'll want to *minimize the tax consequences to your heirs* (even though it may cost you a little more in income taxes in the meantime). With this in mind, you'll want to *avoid generating current retirement income from the sale of assets that will receive a "step-up in basis" at your death.* Suppose, for example, that you purchased Micro Inc. at $5 a share (your basis). On the date of your death, Micro is priced at $50 a share. That means $50 becomes the new tax basis enjoyed by your heirs—and a capital gains tax on the $45-per-share profit is *avoided*. This "step-up" feature is a valuable attribute.

For passing on wealth, therefore, it is best to draw first from your annuities or IRAs because *these have no step-up in basis at your death*. If you do it this way, what are the tax consequences? In the case of an annuity, you will be taxed on a portion (i.e., the amount above what you invested) upon withdrawal. In the case of a traditional IRA, all of the withdrawal will be taxable.

If left to your heirs, however, the money would be taxable to them based on your tax basis. This means an heir in the highest bracket would pay 40% on your previously untaxed gains (or more, depending on state of residence). Further, if you have an estate valued at more than $11.6 million, federal estate taxes will take 40% above that threshold (along with a hefty state bite in certain states).[3] When all is said and done, your children would net only a fraction of your tax-deferred retirement accounts.

- **To favor yourself, withdraw from your taxable investments and Roth IRAs first.** If your priority isn't maximizing inheritance but maximizing retirement income, withdraw first from your taxable investments. This will *prolong the tax-deferral aspects of your annuity and traditional IRAs as long as possible*. For a traditional IRA, you can postpone making withdrawals until age 72 (recently increased from age 70½); in the case of an annuity, required withdrawal varies from company to company.

- **To increase your giving, designate a charitable beneficiary.** If your tax-bracket situation is such that much of your retirement wealth would go to taxes rather than your heirs, consider leaving a considerable portion of your retirement assets to charity. A simple way to do this is to make your spouse the primary beneficiary and a church/charity a secondary beneficiary. Your surviving spouse will be taken care of financially, and then upon his or her death, the charity will get 100% of what remains.

Depending upon your goals, an ideal strategy may be to combine both of the above two concepts. Let your tax-deferred investments continue to grow and designate your spouse as the primary beneficiary and church/charity as the secondary beneficiary, while utilizing your taxable investments and Roth IRA as income sources.

If you would like to do tax-efficient current giving, consider giving some or all of your IRA Required Minimum Distributions (RMDs) directly to charity. While you don't write off this giving on your tax return, you completely avoid any taxes on these distributions.

A word for heirs

- **The SECURE Act changed the rules for distributing assets from an inherited IRA.** A Stretch IRA—which allows the beneficiary to "stretch" receipt of the proceeds out over his or her lifetime—is now limited to spouses and a small class of other beneficiaries.[4] For the most part, if an IRA owner passed away on or after January 1, 2020, the new law requires beneficiaries to withdraw all assets from an inherited IRA *within 10 years* following the death of the account holder. There are tax-avoidance strategies such as declining to inherit or passing the assets to charity if you're eligible. It's wise to get counsel from a CPA or financial planner on all of your options.

Exceptions to the rules

Naturally, being a tax topic, there are exceptions to these general rules! For example, suppose at age 68 you make a major gift or have extremely high medical bills. Because such expenses may result in higher-than-normal tax deductions for that year (assuming you itemize), it may be possible to withdraw tens of thousands of *(continued on page 141)*

[1]Eric Reinhold is a financial advisor at Ameriprise Financial in Orlando, Fla. He is the author of *THE ONE THING to Achieve Life-Long Financial Success* (Academy Institute Press, 2016). [2]Aug2020:p121 [3]The federal tax rate and dollar threshold may be changed by Congress after 2025. [4]Mar2020:p41

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 fund's risk level and portfolio manager's philosophy. 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 7/31/2020	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	11.8%	-7.0%	4.1%	13.8%	-3.8%	1.8%	1.3%	0.97	0.11%/0.08%	20%	16%	12%	8%	VTIAX/VXUS
Extended Market Index	Small company stocks	25.2%	-0.2%	5.7%	19.7%	0.4%	5.2%	8.0%	1.33	0.06%/0.06%	40%	32%	24%	16%	VEXAX/VXF
S&P 500 Index	Large company stocks	27.2%	2.4%	5.6%	12.9%	2.4%	11.9%	12.0%	1.00	0.04%/0.03%	40%	32%	24%	16%	VFIAX/VOO
Total Bond Market Index	Medium-term bonds	19.0%	8.0%	1.6%	2.8%	5.8%	10.4%	5.8%	1.00	0.05%/0.035%	None	20%	40%	60%	VBTLX/BND

JUST-THE-BASICS: JtB 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 far behind. Depending on your particular stock/bond mix, your JtB portfolio should be allocated across either three or four traditional mutual funds/ETFs (see ticker symbols in rightmost column—performance data above is for traditional funds). For more on JtB, see Jan2019:p7-8.

RECOMMENDED FUNDS FOR SMI'S FUND UPGRADING STRATEGY

Risk	Data through 7/31/2020[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. Vanguard Intl Growth Inv	08/20	NTF	Yes	Yes	91.4	22.1%	8.7%	29.9%	24.0%	37.5%	15.2%	1.12	0.43	130	None	VWIGX
	2. Morgan Stnly Intl Opp A - LW[6]	08/20	NTF	NTF	NTF	91.1	22.9%	8.0%	29.3%	27.2%	34.5%	16.8%	1.08	1.30	52	2% 30days	MIOPX
	3. PGIM Jennison Intl Opps Z	08/20	NTF	Yes	NTF	95.1	26.2%	7.7%	30.6%	25.6%	38.9%	19.6%	1.07	0.90	52	None	PWJZX
Category 4 Small/Growth	1. Morgan Stnly Discovery A - LW[6]	08/20	NTF	NTF	NTF	192.6	80.2%	13.3%	55.3%	68.2%	69.2%	45.0%	1.66	1.00	42	None	MACGX
	2. Baron Partners Retail	08/20	NTF	NTF	NTF	128.5	41.1%	19.2%	44.8%	26.7%	57.0%	27.4%	1.72	2.22	29	None	BPTRX
	3. Needham Sm Cap Growth	01/20	NTF	NTF	NTF	94.0	24.8%	9.0%	20.9%	24.6%	48.5%	23.3%	1.31	1.90	43	None	NESGX
Category 3 Small/Value	1. Miller Opportunity A – LW[6]	08/20	NTF	Yes	NTF	44.1	-1.2%	9.7%	30.7%	1.3%	12.1%	7.7%	2.02	1.49	43	None	LGOAX[7]
	2. Janus Henderson Contrarian T	08/20	NTF	NTF	NTF	28.3	0.2%	5.6%	16.4%	2.0%	9.9%	12.6%	1.25	0.81	44	None	JSVAX
	3. Touchstone Mid Cap Z	05/19	NTF	NTF	NTF	7.3	-4.9%	4.2%	10.7%	-6.2%	2.9%	11.5%	1.04	1.21	31	None	TMCTX
Category 2 Large/Growth	1. Morgan Stnly Insight A - LW[6]	08/20	NTF	NTF	NTF	171.3	71.2%	12.2%	47.2%	61.0%	63.1%	42.2%	1.45	1.17	44	None	CPOAX
	2. Touchstone Cap Select Gwth Z	08/20	NTF	NTF	NTF	98.9	34.7%	8.3%	29.3%	29.8%	39.8%	25.4%	1.24	1.19	31	None	PTSGX
	3. Invesco QQQ Trust	02/20	ETF	ETF	ETF	83.6	25.5%	7.4%	21.6%	21.8%	40.2%	23.9%	1.08	0.20	104	None	QQQ
Category 1 Large/Value	1. Invesco S&P 500 Top 50 ETF	02/20	ETF	ETF	ETF	42.6	9.3%	6.3%	14.3%	7.9%	20.4%	15.2%	0.97	0.20	53	None	XLG
	2. JPMorgan Lg Cap Core Pl - LW[6]	08/20	NTF	NTF	NTF	40.7	8.2%	6.9%	16.1%	7.0%	17.7%	12.1%	1.05	1.92	291	None	JLCAX
	3. Centre American Sel Equity Inv	08/20	NTF	NTF	NTF	46.2	15.1%	5.0%	12.3%	14.4%	19.5%	12.0%	0.84	1.45	46	2% 90days	DHAMX
Bond Categories	Carillon Reams Core Plus[8]	5/20	NTF	NTF	NTF	34.6	14.5%	1.8%	5.5%	12.4%	16.7%	7.7%	1.30	0.80	4.9[9]	None	SCPYX[10]
	Permanent: Vanguard I-T Bond	Perm	ETF	ETF	ETF	22.5	9.4%	1.3%	3.8%	6.7%	12.0%	6.5%	1.20	0.05	6.5[9]	None	BIV[11]
	Permanent: Vanguard S-T Bond	Perm	ETF	ETF	ETF	10.5	4.4%	0.4%	1.2%	3.5%	5.9%	3.5%	0.45	0.05	2.8[9]	None	BSV[12]

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 August, rather than on the end-of-July data shown above. The fund ranked third is the one that currently appears most likely to be replaced next **[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 may change, so verify 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 SMI's 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. 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 apply 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 check with your broker for the most current information. **[6]** Normally is a load fund but is available load-waived (LW) through some brokers. Purchase only if available at your broker without paying a load. **[7]** At some brokers, LGOAX isn't load-waived, but you may be able to purchase the no-load share class LMNOX. **[8] Rotating Fund:** This bond recommendation changes periodically based on SMI's Upgrading methodology. The Intermediate-Term (I-T) and Short-Term (S-T) index recommendations shown below that rotating fund are fixed and don't change from month to month. See January2015:p7 for more information. **[9] Duration:** For bond funds, this column shows the average duration (in years) of the bonds in the portfolio. Typically, the longer the duration, the greater the risk/reward. To learn more, see Nov2018:p167. **[10]** Or buy the institutional share class SCPZX. **[11]** Those preferring a traditional mutual-fund option can buy VBILX. **[12]** Those preferring a traditional mutual-fund option can buy VBIRX.

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 and is easy to implement. This page explains 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 Vanguard International Growth, the highest-ranked Cat. 4 fund is Morgan Stanley Discovery, 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%

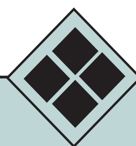
❸ BUY YOUR FUNDS

Example uses an 80/20 mix between stocks and bonds		Dollars	Invest in Funds
Stock Cat. 5: Foreign	16%	$8,000	Vanguard Intl Growth
Stock Cat. 4: Small/Growth	16%	$8,000	Morgan Stanley Discovery A
Stock Cat. 3: Small/Value	16%	$8,000	Miller Opportunity A
Stock Cat. 2: Large/Growth	16%	$8,000	Morgan Stanley Insight A
Stock Cat. 1: Large/Value	16%	$8,000	Invesco S&P 500 Top 50 ETF
"Rotating" Bond Fund	10%	$5,000	Carillon Reams Core Plus
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

LEVEL 1 / CONTINUED FROM PAGE 134

INVEST IN YOUR 401(K) OR PAY DOWN YOUR HOME MORTGAGE?

$42,700 on *his* mortgage.)

With no house payments remaining, Mort shifts the income that formerly would have gone toward mortgage payments into his retirement plan. Like Rex, he takes maximum advantage of the tax savings his contributions create and invests those savings as well. Mort can contribute $1,950 a month—$1,500 from his monthly surplus plus another $450 in tax savings. His annual contribution (in years 13, 14, and 15) totals $23,400.[1]

Now that our 15-year experiment is complete, let's see where things stand. Both Rex and Mort had the same out-of-pocket expenditures—$1,500 per month over 15 years, totaling $270,000. Both accomplished paying off their $180,000 mortgage loans, and both were able to invest for retirement.

By prepaying his mortgage, Mort saved nearly $9,500 in interest and paid off his mortgage more than three years early—giving him peace of mind that his home was free and clear. Rex, in contrast, didn't enjoy any interest savings. Still, by taking full advantage of the tax-deductibility of his 401(k) contributions over 15 years, he did save about $2,300 more in taxes than Mort.

As for their retirement accounts, Rex's 401(k) grew to $105,809, and Mort's to $79,605—a difference of $26,204. Although Rex actually contributed less than Mort ($66,060 to Mort's $72,462), he was able to take greater advantage of the tax-deferred compounding of profits. Mort's retirement account came on strong later, but Rex's head start was too great.

So should you give preference to investing in a 401(k) over prepaying a mortgage? The answer isn't as straightforward as it might seem. Bear in mind a key assumption in our Rex-vs-Mort comparison: Rex enjoyed *steady investment performance*—6% growth per year for 15 years. Real life isn't like that. Investors experience reversals as well as advances—and sometimes reversals can be severe. Depending on when Rex's performance setbacks occurred and how deep they were, Mort may have come out ahead in our comparison.

Now consider the advantages of Mort's approach: Paying ahead on his mortgage enabled Mort and his family to enjoy the financial security of a debt-free home in less than 12 years. Further, while Rex's return on his 401(k) investments could have fallen or even turned negative, Mort's interest savings on his mortgage was guaranteed.

Although each approach—prepaying and investing—has pros and cons, the availability of employer matching funds (which neither Rex nor Mort had) *would make the investing approach much more attractive*. If a match were available, then delaying 401(k) investing—and thereby missing out on the match—would mean forsaking years of compounding of those unclaimed matching funds.

A blended approach

Instead of thinking of the "prepay or invest" question as an "either/or" matter, we suggest you consider a blended approach. You could *split* your surplus and work toward each goal simultaneously. If your company retirement plan offers matching funds, we urge you to contribute at least enough to receive the full match. Then, you can put any additional surplus toward your mortgage.

A 401(k) calculator[2] can estimate your retirement account's growth based on the size of your contributions, any employer match, and a projected rate of return. And a mortgage calculator[3] can show how prepayments will help you save on interest and shorten the term of your loan.

Keep in mind that in our example, Rex and Mort enjoyed 15 years of job stability, had no changes in tax law to deal with, and neither moved. That's a lot to expect over a decade-and-a-half! Any plan you come up with for investing/prepaying will require adjustments from time to time. But at least you'll be steadily advancing toward greater financial stability and strength—as you build up your retirement account and pay down your debt. ◆

LEVEL 3 / CONTINUED FROM PAGE 136

DIVERSIFICATION: THE ONLY FREE LUNCH IN INVESTING

Then in 2017, the script had flipped yet again: Foreign was back on top, Small/Value was the worst, and this time Foreign was winning by about 20 percentage points.

There is such a thing as a free lunch

When a particular market segment is hot, many investors (understandably) are enticed by the performance numbers. Diversification seems dull by comparison and not as lucrative. So they shift their holdings to what's hot, only to later suffer the consequences of being overly concentrated in a particular slice of the market when that slice falls out of favor.

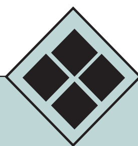
The better path for most investors is to spread their money more broadly across the primary market segments. Yes, this ensures your overall portfolio result won't match the hottest performer's returns in any given year, but it also guarantees you'll never miss out on *participating to some degree* in each year's hot area.

The real beauty of diversification is that it *produces long-term returns similar to the individual risk categories while smoothing out volatility along the way*. This muting of sharp ups and downs is crucial. It helps protect you from the most dangerous obstacle you face as an investor—your own emotions.

So the next time you're tempted to load up on a particular investment type (or wonder if it's really necessary to own funds in all five SMI risk categories), remember the periodic table of investment returns and the diversification lessons it holds.

Diversification is often called "the only free lunch in investing." That's because it costs virtually nothing to diversify, yet diversification yields great benefits—namely, a reduction in portfolio volatility plus a degree of protection from overall losses. At the same time, you get to enjoy having some of your money invested in the market's top-performing segment year-in and year-out. ◆

[1]Under current law, Mort would be allowed to contribute this much annually only if he were age 50 or over. Otherwise, his annual contribution would be capped at $18,000.
[2]bit.ly/bankrate-401k-calculator [3]www.hughcalc.org/mort.php



MONEYTALK

LEVEL 4 / CONTINUED FROM PAGE 137

WHICH ASSETS SHOULD YOU WITHDRAW FIRST DURING RETIREMENT?

dollars from a traditional IRA and owe no income tax on that money. (This differs from the conventional wisdom discussed earlier that might normally cause you to hold off on tapping that account until later.)

Additionally, drawing from your IRAs during years with high tax deductions would produce an added benefit later—at age 72—when Uncle Sam forces you to begin taking "required minimum distributions" from your IRA. Because you would have already withdrawn a significant amount of money, the yearly amount of forced IRA withdrawals would be less.

In some cases, depending on several factors, it can be more tax-efficient to withdraw money from *different types of asset accounts in the same year*, rather than using a distinct sequencing arrangement. For example, you might take a specified amount from an account that receives one type of tax treatment, and then meet the balance of your needs for that year with money from an account that gets a different tax treatment.

It is critical to review your monthly living expenses as you move into retirement, related to both essentials and lifestyle considerations. Likewise, you should prepare for the unexpected, such as long-term care and other health issues that can disrupt your plan.

Determining when to depart from normal asset sequencing in favor of a more finely-tuned withdrawal strategy can be complicated. Figuring out how all the variables work together in the most tax-efficient manner isn't easy, and the tax implications of any particular action may not be immediately apparent. This is a complex area, so it is worth having a CPA or financial planner run the numbers and find the approach that works best given the specific mix of assets in your portfolio. ◆

SIGHTING: S&P 500 HITS RECORD, DEFYING ECONOMIC DEVASTATION

...[A]lmost all the gains in major stock market indexes this year are attributable to the surging share prices of a few giant technology companies, foremost among them Apple, Amazon and Microsoft. These megacompanies...are exerting an enormous influence over major stock market indexes such as the S&P 500. Since such indexes are weighted by the market value of their constituents, the largest companies hold sway over their direction.

Tech giants have fared incredibly well through the crisis as investors bet the stay-at-home economy plays to many of their strengths. Amazon is up about 80 percent this year. Apple is up almost 60 percent, while Microsoft has risen more than 34 percent. Without those three companies, the return on owning S&P 500 stocks—including dividend payments—would have been negative 4.1 percent this year through the end of July. Instead, investors captured an actual return of 2.4 percent, according to data from S&P Dow Jones Indices.

The stock market is also incredibly sensitive to actions by the Federal Reserve, with stocks often soaring when the central bank eases monetary policy, typically in response to an economic slump. That means a weak economy can actually be quite good for Wall Street, if it means that the Fed keeps the river of freshly created money—what's known on Wall Street as liquidity—flowing into financial markets. That could help explain why empirical studies of the relationship between economic growth and stock market performance often show little connection between the two.

"Nothing matters but liquidity," wrote Michael Hartnett, chief investment strategist at Bank of America Global Research, in a recent research note....

The performance of the market in the face of such dire expectations for growth, he wrote, is just the latest example of investors betting that low growth will prompt the Fed to continue pushing money into the financial system, ultimately bolstering stocks. In other words, stocks are going up not because of economic optimism, but because the future looks fairly grim. Mr. Hartnett titled his report, "I'm so bearish, I'm bullish."

– From an 8/18/20 article in *The New York Times*. Read more at nyti.ms/2YvFInk.

SIGHTING: BUFFETT'S BERKSHIRE HATHAWAY HAS INVESTED IN A GOLD MINER—A HUGE DEPARTURE FROM THE PAST

Warren Buffett's Berkshire Hathaway made its first investment in a gold miner last quarter, even though the famed investor has warned against betting on the precious metal for at least two decades. The conglomerate bought 20.9 million shares of Barrick Gold, worth about $564 million at the end of June, according to its latest portfolio update....

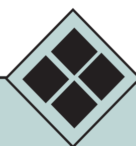
Buffett is clearly a vocal critic of gold, but it's important to note that he has invested in precious metals in the past. The Berkshire boss purchased almost 130 million ounces of silver in the late 1990s as he predicted shrinking stockpiles would drive up the metal's price. He also bought silver in the 1960s in anticipation of its demonetization by the US government.

Moreover, Buffett might not be behind the Barrick investment. One of his two investing deputies, Ted Weschler and Todd Coombs, may have made the call.... However, the investment still represents a significant shift in Berkshire's stance on gold.

– From an 8/17/20 article at BusinessInsider.com. Read more at bit.ly/31uX4CD.

SIGHTING: A RAISE LIKELY FOR SOCIAL SECURITY RECIPIENTS AFTER ALL

Inflation has been on a roller coaster in 2020. First, COVID-19 disruptions cratered prices for gasoline, travel, even car insurance. Summer rebounds in those commodities, as well as increases for in-demand items like used cars, meat and haircuts, have put the consumer price index back on a more normal trajectory, one that will likely mean an increase in the Cost of Living Adjustment (COLA) for 2021.



MONEYTALK

The Kiplinger Letter is now forecasting a 1.2% increase in the 2021 COLA....

The Social Security Administration (SSA) is required by law to prevent inflation from eroding the buying power of the benefits paid out to nearly 69 million Americans. It uses a... COLA formula based on the consumer price index to adjust payouts every January. Since prices typically rise, payouts typically rise also. If prices fall (as they did earlier this year), payouts would remain unchanged until prices catch back up again. But it matters *when* they fall.

The SSA calculates the percent change between average prices in the third quarter of the current year with the third quarter of the previous year.... And it's likely that those figures (the third-quarter comparison) will show an increase.

– From an 8/24/20 "Economic Forecasts" article at Kiplinger.com. Read more at bit.ly/32rchUr.

MARKET NOTES, QUOTES, AND ANECDOTES

Signs point to continued growth

"…the angle and speed of the market's ascent…make it resemble most closely the powerful moves off decisive and sanctified market bottoms of yore, ones that kicked off long bull markets and signaled enduring economic revivals." – CNBC senior markets commentator Michael Santoli, in an 8/15/20 article. For those who worry that the market's rally may have run its course, he wrote, "investors shouldn't dismiss the chance that it's not so late in the grand scheme." Read more at cnb.cx/32s1QAa.

Or not

"Never before have I seen a market so highly valued in the face of overwhelming uncertainty."– James Montier, a member of the investment committee for GMO, writing on the company's blog on 8/12/20. He sees a dangerous mix of overoptimism and overconfidence among today's investors. Read more at bit.ly/3l179io.

The high cost of indecision

"Even if you believe the probability of a correction is high, it's far from certain. And when the correction doesn't happen, the expected opportunity cost of having waited is much greater than the expected benefit."– Larry Swedroe, chief research officer at Buckingham Strategic Wealth, in an 8/21/20 *Evidence-Based Investor* blog post. He said more money is lost anticipating corrections than in them. Read more at bit.ly/3gsb4kJ.

Emotional momentum

"You may have decades of investment experience, but not all of those years are weighted equally. The more recent the fear, the more skewed the appraisal of risk and reward." – Behavioral psychologist Daniel Crosby, in an 8/11/20 *Kiplinger* article about the danger of recency bias—the tendency to be overly influenced by recent events, such as the COVID-19 pandemic. Read more at bit.ly/3j8wDZk.

Are we there yet?

"We have a long way to go and we aren't getting there very fast."– Mark Zandi, chief economist for Moody's Analytics. Moody's helped create a "Back-to-Normal Index," which shows which states are closest to and furthest from their pre-pandemic economies. Overall, the index showed the U.S. economy was operating at about 78% of normal as of August 19. Read more and see where your state stands at cnn.it/32jlIp2.

The Dow gets a makeover

"It shows you how the giants can fall."– Wharton finance professor Jeremy Siegel, commenting to CNBC on 8/25/20 about the decision to replace Exxon, Pfizer, and Raytheon with Salesforce, Amgen, and Honeywell in the Dow Jones Industrial Average. Exxon (formerly Standard Oil), a Dow component for nearly 100 years, has seen its market capitalization plunge nearly 50% since April 2019. Read more at cnb.cx/2QkPGTS.

How low can they go?

"The reality of money-market funds is it's no longer about return on capital. You're not going to make any money until the Fed raises rates."– Keith Berlin, head of fixed income at consulting company Fund Evaluation Group, quoted in an 8/24/20 *Wall Street Journal* article. Low interest rates have prompted many money market funds to cut investor fees to avoid having yields fall below 0%. Read *Seeking Alpha*'s summary at bit.ly/3aUUBnT.

Objectivity takes a holiday

"What gnawed at [Sir Isaac] Newton for years, and what still seems strange, is that his capacity for dispassionate analysis failed him when he needed it most. Here was a man who had calculated logarithms to 50 places. But in the thrill of the moment, he failed to do the math."– Thomas Levenson, in an excerpt from his newly released book, *Money for Nothing*, which ran on 8/23/20 in *The Atlantic*.

Levenson said Newton let emotion govern his investment in the South Sea Company, which led to catastrophic losses—a phenomenon still common among investors today. Newton lost the equivalent of nearly 2 million pounds in today's money ($2.6 million in U.S. dollars). Read more at bit.ly/3gpgOMe.

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

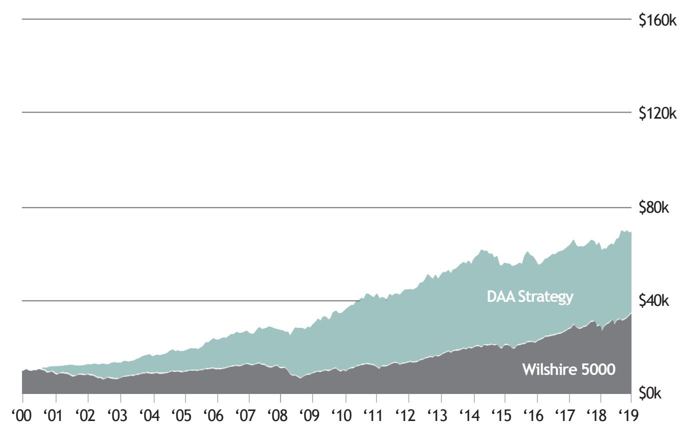
Overview

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

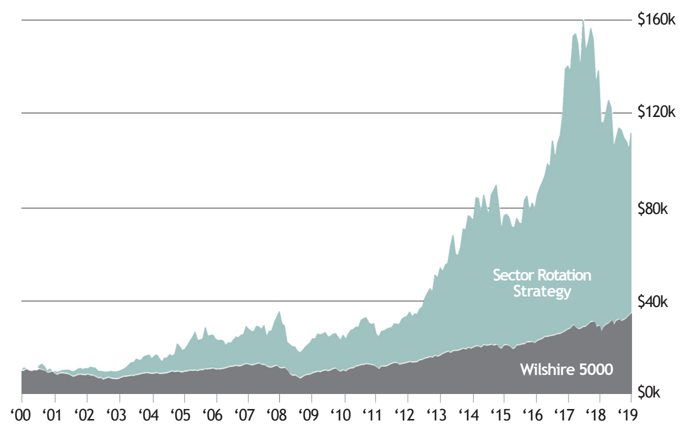
Overview

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.

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PERFORMANCE DATA

SOUND MIND INVESTING MODEL PORTFOLIOS • DATA THROUGH JULY 31, 2020

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]	2.2%	5.7%	13.8%	11.2%	11.5%	11.1%	13.6%	9.0%
Just-the-Basics[2]	-0.5%	5.5%	15.8%	7.2%	8.2%	8.5%	11.4%	8.1%
Stock Upgrading[3]	-7.2%	2.8%	8.2%	-2.5%	3.9%	5.3%	9.3%	7.1%
U.S. Bond Market[4]	8.0%	1.6%	2.8%	10.3%	5.6%	4.4%	3.7%	4.4%
Bond Upgrading[5]	9.0%	1.3%	4.0%	11.4%	5.6%	4.4%	4.7%	6.3%

PREMIUM STRATEGIES

	Year to Date	1 Month	3 Months	12 Months	3 Yrs Annual	5 Yrs Annual	10 Yrs Annual	15 Yrs Annual
DAA[6]	11.8%	7.3%	10.7%	16.4%	8.7%	5.7%	8.4%	9.9%
Sector Rotation	-7.4%	2.4%	9.7%	-6.9%	-0.4%	3.4%	15.7%	11.0%
50-40-10 Blend[7]	2.3%	5.2%	9.7%	6.6%	6.2%	5.6%	9.7%	9.4%

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 7/31/2020	Year to Date	1 Month	3 Months	12 Months	3 Year Annual	5 Year Annual	10 Year Annual
SMIFX	-4.69%	4.71%	11.83%	-0.77%	3.90%	4.22%	8.02%
Wilshire 5000	2.18%	5.66%	13.77%	11.16%	11.47%	11.10%	13.60%
S&P 500	2.38%	5.64%	12.87%	11.96%	12.01%	11.49%	13.84%

Quarterly Returns as of 6/30/2020	Year to Date	1 Month	3 Months	12 Months	3 Year Annual	5 Year Annual	10 Year Annual
SMIFX	-8.98%	2.82%	16.77%	-3.75%	3.13%	3.58%	8.34%
Wilshire 5000	-3.30%	2.34%	21.94%	6.78%	10.13%	10.27%	13.74%
S&P 500	-3.08%	1.99%	20.54%	7.51%	10.73%	10.73%	13.99%

Total/Gross expense ratio: 1.94% as of 2/28/20 (includes expenses of underlying funds)
Adjusted expense ratio: 1.18% as of 2/28/20 (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 Ultimus Fund Distributors, LLC (member FINRA).

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