VOLUME 32 ◆ NUMBER 2

FEBRUARY 2021

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The Psychology of Money

Successful investing may appear to be primarily about choosing the right investments and keeping the math straight. But many less obvious—and more important factors—come into play. Writer Morgan Housel, of venture capital firm The Collaborative Fund, excels at identifying and explaining these often-overlooked but critically important aspects of successful investing. We're pleased to offer this excerpt from his recent book, *The Psychology of Money*, which brilliantly highlights several of the most crucial ones.

by Morgan Housel

More than 2,000 books are dedicated to how Warren Buffett built his fortune. Many of them are wonderful. But few pay enough attention to the simplest fact: Buffett's fortune isn't due to just being a good investor, but being a good investor since he was literally a child.

As I write this Warren Buffett's net worth is $84.5 billion. Of that, 84.2 billion was accumulated after his 50th birthday. $81.5 billion came after he qualified for Social Security, in his mid-60s.

Warren Buffett is a phenomenal investor. But you miss a key point if you attach all of his success to investing acumen. The real key to his success is that he's been a phenomenal investor for three-quarters of a century. Had he started investing in his 30s and retired in his 60s, few people would have ever heard of him.

Consider a little thought experiment.

Buffett began serious investing when he was 10 years old. By the time he was 30 he had a net worth of $1 million, or $9.3 million adjusted for inflation.

What if he was a more normal person, spending his teens and 20s exploring the world and finding his passion, and by age 30 his net worth was, say, $25,000?

And let's say he still went on to earn the extraordinary annual investment returns he's been able to generate (22% annually), but quit investing and retired at age 60 to play golf and spend time with his grandkids.

What would a rough estimate of his net worth be today? Not $84.5 billion.

$11.9 *million*.

99.9% less than his actual net worth.

Effectively all of Warren Buffett's financial success can be tied to the financial base he built in his pubescent years and the longevity he maintained in his geriatric years.

His skill is investing, but his secret is time.

That's how compounding works.

Think of this another way. Buffett is the richest investor of all time. But he's not actually the greatest—at least not when measured by average annual returns. *(continued on page 19)*

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EDITORIAL

The Wisdom to Show Restraint

"Do not wear yourself out to get rich; have the wisdom to show restraint. Cast but a glance at riches, and they are gone, for they will surely sprout wings and fly off to the sky like an eagle." Proverbs 23:4-5

Market sentiment is more euphoric than ever. So notes the Citigroup Panic/Euphoria indicator, which in early 2021 showed a level of elevated investor sentiment surpassing the early-2000 prior all-time high.

Indeed, signs of market excess are everywhere. One of Warren Buffett's favorite market-valuation signals is the ratio of the total U.S. stock market value (market cap) to U.S. Gross Domestic Product (GDP). A year ago, exactly one week before the COVID-19 bear market began, SMI alerted readers that this indicator had just surpassed its March 2000 peak level of 142.9%. Today, following a year of lockdowns and a massive global recession that we're still battling back from, the ratio has soared to 192%! In other words, the stock market has never before been so richly valued relative to the actual economy.

We could go on listing any number of additional signs of market exuberance. Those would include SMI's Sector Rotation strategy, which followed its +39.4% Nov/Dec 2020 gain by soaring another +18%...in the first 12 trading days of 2021.

Trying to attribute market behavior to any single factor is usually a fool's errand. But the uncomfortable truth is today's speculative excess is based on the belief that the world's central bankers and governments are justifying these valuations via low interest rates and massive stimulus injections. Investors have learned the lesson well over the past dozen years: when governments take these actions, a large portion of the stimulus winds up driving the prices of financial assets (such as stocks and bonds) higher. These actions have never been taken at the scale currently underway around the globe.

As a result, markets face two possible forward paths:

1. Eventually, the bubble pops anyway and we get a deflationary/bear-market result similar to most prior episodes of significant financial market excess.

2. The value of money is debased significantly enough that the 40-year inflation cycle reverses. In this scenario, inflating nominal (non-inflation adjusted) asset prices mask the fact that the purchasing power of those assets is being eroded. This could potentially allow escape without asset prices declining significantly (in nominal terms).

Policymakers are targeting outcome number two. Confident they can contain the inflationary beast once awakened, they realize the peril of letting the markets (and likely the broader economy) go down the deflationary path of pain.

Investors are buying into the idea of the inflationary path as well—quite literally, as they flood into "reflation" plays such as commodities, energy stocks, and so forth.

In 1993, John Templeton famously warned that "This time is different" are among the "most costly words in the annals of investing." What most investors don't know is Templeton conceded that 20% of the time the phrase is true. This time really *is* different. There is no historical precedent with which to compare today's unprecedented policies, making it impossible to say for sure which of the two paths markets will follow.

How should we respond in the face of this uncertainty? The Proverb atop of this editorial offers an important key. Regular investors can easily fall into the trap of blowing past restraint en route to imagined future riches. Here are a few tips to help check that impulse.

• **Focus on risk first, returns second.** Your investment choices regarding strategies and the kinds of assets you want to own in your portfolio should be informed by the knowledge that another sharp downturn could happen *at any time*. As you continue to invest, do so soberly. Recognize that high-risk, high-reward strategies (such as Sector Rotation) can be useful in moderation, but dangerous when restraint is abandoned.

• **Don't take more risk than is necessary to meet your goals.** If you've been blessed to be in position to meet your retirement goals with a less-aggressive investment plan than you once anticipated, rejoice—then dial back your risk! The object isn't to build the biggest nest egg possible. It's to be a good steward and be able to provide for your future needs.

• **Set an ultimate "finish line"—and scale back risk when it is reached.** This can protect you from sacrificing things you truly treasure (financial freedom and security) in pursuit of what you will no longer need (more dollars in an investment account).



MARK BILLER
EXECUTIVE EDITOR

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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 368 • Volume 32 Number 2. Mailing date: 2/04/2021.

The Psychology of Money

(continued from front page)

Jim Simons, head of the hedge fund Renaissance Technologies, has compounded money at 66% annually since 1988. No one comes close to this record. As we just saw, Buffett has compounded at roughly 22% annually, a third as much.

Simons' net worth, as I write, is $21 billion. He is—and I know how ridiculous this sounds given the numbers we're dealing with—75% less rich than Buffett.

Why the difference, if Simons is such a better investor? Because Simons did not find his investment stride until he was 50 years old. He's had less than half as many years to compound as Buffett. If James Simons had earned his 66% annual returns for the 70-year span Buffett has built his wealth he would be worth—please hold your breath—sixty-three quintillion nine hundred quadrillion seven hundred eighty-one trillion seven hundred eighty billion seven hundred forty-eight million one hundred sixty thousand dollars.

These are ridiculous, impractical numbers. The point is that what seem like small changes in growth assumptions can lead to ridiculous, impractical numbers. And so when we are studying why something got to become as powerful as it has—why an ice age formed, or why Warren Buffett is so rich—we often overlook the key drivers of success.

I have heard many people say the first time they saw a compound interest table—or one of those stories about how much more you'd have for retirement if you began saving in your 20s versus your 30s—changed their life. But it probably didn't. What it likely did was *surprise* them, because the results intuitively didn't seem right. Linear thinking is so much more intuitive than exponential thinking. If I ask you to calculate 8+8+8+8+8+8+8+8+8 in your head, you can do it in a few seconds (it's 72). If I ask you to calculate 8x8x8x8x8x8x8x8x8, your head will explode (it's 134,217,728).

The danger here is that when compounding isn't intuitive we often ignore its potential and focus on solving problems through other means. Not because we're overthinking, but because we rarely stop to consider compounding potential.

None of the 2,000 books picking apart Buffett's success are titled *This Guy Has Been Investing Consistently for Three-Quarters of a Century*. But we know that's the key to the majority of his success. It's just hard to wrap your head around that math because it's not intuitive.

There are books on economic cycles, trading strategies, and sector bets. But the most powerful and important book should be called *Shut Up And Wait*. It's just one page with a long-term chart of economic growth.

The practical takeaway is that the counterintuitiveness of compounding may be responsible for the majority of disappointing trades, bad strategies, and successful investing attempts.

You can't blame people for devoting all their effort—effort in what they learn and what they do—to trying to earn the highest investment returns. It intuitively seems like the best way to get rich.

But good investing isn't necessarily about earning the highest returns, because the highest returns tend to be one-off hits that can't be repeated. It's about earning pretty good returns that you can stick with and which can be repeated for the longest period of time. That's when compounding runs wild.

Tails win, so diversify!

Steamboat Willie put Walt Disney on the map as an animator. Business success was another story. Disney's first studio went bankrupt. His films were monstrously expensive to produce, and financed at outrageous terms. By the mid-1930s Disney had produced more than 400 cartoons. Most of them were short, most of them were beloved by viewers, and most of them lost a fortune.

Snow White and the Seven Dwarfs changed everything.

The $8 million it earned in the first six months of 1938 was an order of magnitude higher than anything the company earned previously.

It transformed Disney Studios. All company debts were paid off. Key employees got retention bonuses. The company purchased a new state-of-the-art studio in Burbank, where it remains today. An Oscar turned Walt from famous to full-blown celebrity. By 1938 he had produced several hundred hours of film. But in business terms, the 83 minutes of *Snow White* were all that mattered.

Anything that is huge, profitable, famous, or influential is the result of a tail event—an outlying one-in-thousands or millions event. And most of our attention goes to things that are huge, profitable, famous, or influential. When most of what we pay attention to is the result of a tail, it's easy to underestimate how rare and powerful they are.

Some tail-driven industries are obvious. Take venture capital. If a VC makes 50 investments they likely expect half of them to fail, 10 to do pretty well, and one or two to be bonanzas that drive 100% of the fund's returns. Investment firm Correlation Ventures once crunched the numbers. Out of more than 21,000 venture financings from 2004 to 2014:

65% lost money.

Two and a half percent of investments made 10x-20x.

One percent made more than a 10x-20x return.

Half a percent—about 100 companies out of 21,000—earned 50x or more. That's where the majority of the industry's returns come from.

This, you might think, is what makes venture capital so risky. And everyone investing in VC knows it's risky. Most startups fail and the world is only kind enough to allow a few mega successes.

If you want safer, predictable, and more stable returns, you invest in large public companies.

Or so you might think.

Remember, tails drive *everything*.

The distribution of success among large public stocks over time is not much different than it is in venture capital.

Most public companies are duds, a few do well, and a handful become extraordinary winners that account for the majority of the stock market's returns. J.P. Morgan Asset Management once published the distribution of returns for the Russell 3000 Index—a big, broad, collection of public companies—since 1980. Forty percent of all Russell 3000 stock com-

ponents lost at least 70% of their value and never recovered over this period. Effectively all of the index's overall returns came from 7% of component companies that outperformed by at least two standard deviations. That's the kind of thing you'd expect from venture capital. But it's what happened inside a boring, diversified index. This thumping of most public companies spares no industry. More than half of all public technology and telecom companies lose most of their value and never recover. Even among public utilities the failure rate is more than 1 in 10.

The interesting thing here is that you have to have achieved a certain level of success to become a public company and a member of the Russell 3000. These are established corporations, not fly-by-night startups. Even still, most have lifespans measured in years, not generations.

Not only do a few companies account for most of the market's return, but within those companies are even more tail events. In 2018, Amazon drove 6% of the S&P 500's returns. And Amazon's growth is almost entirely due to Prime and Amazon Web Services, which itself are tail events in a company that has experimented with hundreds of products, from the Fire Phone to travel agencies.

Apple was responsible for almost 7% of the index's returns in 2018. And it is driven overwhelmingly by the iPhone, which in the world of tech products is as tail-y as tails get.

The idea that a few things account for most results is not just true for companies in your investment portfolio. It's also an important part of your own behavior as an investor.

Napoleon's definition of a military genius was, "The man who can do the average thing when all those around him are going crazy."

It's the same in investing.

Most financial advice is about *today*. What should you do *right now*, and what stocks look like good buys *today*?

But most of the time *today* is not that important. Over the course of your lifetime as an investor, the decisions that you make today or tomorrow or next week will not matter nearly as much as what you do during the small number of days—likely 1% of the time or less—when everyone else around you is going crazy.

A good definition of an investing genius is the man or woman who can do the average thing when all those around them are going crazy. Tails drive everything. When you accept that tails drive everything in business, investing, and finance you realize that it's normal for lots of things to go wrong, break, fail, and fall.

If you're a good stock picker you'll be right maybe half the time.

If you're a good business leader maybe half of your product and strategy ideas will work.

If you're a good investor most years will be just OK, and plenty will be bad.

If you're a good worker you'll find the right company in the right field after several attempts and trials.

And that's if you're good.

Peter Lynch is one of the best investors of our time. "If you're terrific in this business, you're right six times out of 10," he once said.

There are fields where you must be perfect every time. Flying a plane, for example. Then there are fields where you want to be at least pretty good nearly all the time. A restaurant chef, let's say.

Investing, business, and finance are not like these fields.

Something I've learned from both investors and entrepreneurs is that no one makes good decisions all the time. The most impressive people are packed full of horrendous ideas that are often acted upon.

Take Amazon. It's not intuitive to think a failed product launch at a major company would be normal and fine. Intuitively, you'd think the CEO should apologize to shareholders. But CEO Jeff Bezos said shortly after the disastrous launch of the company's Fire Phone:

If you think that's a big failure, we're working on much bigger failures right now. I am not kidding. Some of them are going to make the Fire Phone look like a tiny little blip.

It's OK for Amazon to lose a lot of money on the Fire Phone because it will be offset by something like Amazon Web Services that earns tens of billions of dollars. Tails to the rescue.

A similar thing happens in investing. It's easy to find Warren Buffett's net worth, or his average annual returns. Or even his best, most notable investments. They're right there in the open, and they're what people talk about.

It's much harder to piece together every investment he's made over his career. No one talks about the dud picks, the ugly businesses, the poor acquisitions. But they're a big part of Buffett's story. They are the other side of tail-driven returns.

At the Berkshire Hathaway shareholder meeting in 2013 Warren Buffett said he's owned 400 to 500 stocks during his life and made most of his money on 10 of them. Charlie Munger followed up: "If you remove just a few of Berkshire's top investments, its long-term track record is pretty average."

Leaving room for error

Benjamin Graham is known for his concept of margin of safety. He wrote about it extensively and in mathematical detail. But my favorite summary of the theory came when he mentioned in an interview that "the purpose of the margin of safety is to render the forecast unnecessary."

It's hard to overstate how much power lies in that simple statement.

Margin of safety—you can also call it room for error or redundancy—is the only effective way to safely navigate a world that is governed by odds, not certainties. And almost everything related to money exists in that kind of world.

Forecasting with precision is hard. This is obvious to the card counter, because no one could possibly know where a particular card lies in a shuffled deck. It's less obvious to someone asking, "What will the average annual return of the stock market be over the next 10 years?" or "On what date will I be able to retire?" But they are fundamentally the same. The best we can do is think about odds.

Graham's margin of safety is a simple suggestion that we don't need to view the world in front of us as black or white, predictable or a crapshoot. The grey area—pursuing things

where a range of potential outcomes are acceptable—is the smart way to proceed.

But people underestimate the need for room for error in almost everything they do that involves money. Stock analysts give their clients price targets, not price ranges. Economic forecasters predict things with precise figures, rarely broad probabilities. The pundit who speaks in unshakable certainties will gain a larger following than the one who says "We can't know for sure," and speaks in probabilities.

We do this in all kinds of financial endeavors, especially those related to our own decisions. Harvard psychologist Max Bazerman once showed that when analyzing other people's home renovation plans, most people estimate the project will run between 25% and 50% over budget. But when it comes to their own projects, people estimate that renovations will be completed on time and at budget.

Two things cause us to avoid room for error. One is the idea that somebody must know what the future holds, driven by the uncomfortable feeling that comes from admitting the opposite. The second is that you're therefore doing yourself harm by not taking actions that fully exploit an accurate view of that future coming true.

But room for error is underappreciated and misunderstood. It's often viewed as a conservative hedge, used by those who don't want to take much risk or aren't confident in their views. But when used appropriately, it's quite the opposite.

Room for error lets you endure a range of potential outcomes, and endurance lets you stick around long enough to let the odds of benefiting from a low-probability outcome fall in your favor. The biggest gains occur infrequently, either because they don't happen often or because they take time to compound. So the person with enough room for error in part of their strategy (cash) to let them endure hardship in another (stocks) has an edge over the person who gets wiped out, game over, insert more tokens, when they're wrong.

Bill Gates understood this well. When Microsoft was a young company, he said he "came up with this incredibly conservative approach that I wanted to have enough money in the bank to pay a year's worth of payroll even if we didn't get any payments coming in." Warren Buffett expressed a similar idea when he told Berkshire Hathaway shareholders in 2008: "I have pledged—to you, the rating agencies and myself—to always run Berkshire with more than ample cash.... When forced to choose, I will not trade even a night's sleep for the chance of extra profits."

There are a few specific places for investors to think about room for error.

One is volatility. Can you survive your assets declining by 30%? On a spreadsheet, maybe yes—in terms of actually paying your bills and staying cash-flow positive. But what about mentally? It is easy to underestimate what a 30% decline does to your psyche. Your confidence may become shot at the very moment opportunity is at its highest. You—or your spouse—may decide it's time for a new plan, or new career. I know several investors who quit after losses because they were exhausted. Physically exhausted. Spreadsheets are good at telling you when the numbers do or don't add up. They're not good at modeling how you'll feel when you tuck your kids in at night wondering if the investment decisions you've made were a mistake that will hurt their future. Having a gap between what you can technically endure versus what's emotionally possible is an overlooked version of room for error.

Another is saving for retirement. We can look at history and see, for example, that the U.S. stock market has returned an annual average of 6.8% after inflation since the 1870s. It's a reasonable first approximation to use that as an estimate of what to expect on your own diversified portfolio when saving for retirement. You can use those return assumptions to back into the amount of money you'll need to save each month to achieve your target nest egg.

But what if future returns are lower? Or what if long-term history is a good estimate of the long-term future, but your target retirement date ends up falling in the middle of a brutal bear market, like 2009? What if a future bear market scares you out of stocks and you end up missing a future bull market, so the returns you actually earn are less than the market average? What if you need to cash out your retirement accounts in your 30s to pay for a medical mishap?

The answer to those what ifs is, "You won't be able to retire like you once predicted." Which can be a disaster.

The solution is simple: Use room for error when estimating your future returns. This is more art than science. For my own investments, I assume the future returns I'll earn in my lifetime will be one-third lower than the historic average. So I save more than I would if I assumed the future will resemble the past. It's my margin of safety. The future may be worse than one-third lower than the past, but no margin of safety offers a 100% guarantee. A one-third buffer is enough to allow me to sleep well at night. And if the future does resemble the past, I'll be pleasantly surprised. "The best way to achieve felicity is to aim low," says Charlie Munger. Wonderful.

A good rule of thumb for a lot of things in life is that everything that can break will eventually break. So if many things rely on one thing working, you are counting the days to catastrophe. That's a single point of failure.

The biggest single point of failure with money is a sole reliance on a paycheck to fund short-term spending needs, with no savings to create a gap between what you think your expenses are and what they might be in the future.

The trick that often goes overlooked is realizing that you don't need a specific reason to save. It's fine to save for a car, or a home, or for retirement. But it's equally important to save for things you can't possibly predict.

Predicting what you'll use your savings for assumes you live in a world where you know exactly what your future expenses will be, which no one does. Few financial plans that only prepare for known risks have enough margin of safety to survive the real world.

In fact, the most important part of every plan is planning on your plan not going according to plan. ◆

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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 SURE YOUR HOUSE DOESN'T OWN YOU

By Matt Bell

During the last recession, many people painfully discovered they had stretched too far in buying a home. Loose application requirements tempted many people to buy who, it turned out, were not in a financially strong enough position to buy. Today, with mortgage rates at historic lows, buying a house once again looks very tempting.

Is it a good time to buy? It could be, as long as you buy in such a way that your house doesn't own you.

Save early and save often

Before applying for a mortgage, save enough to be able to make at least a 20% down payment and fill an emergency fund equal to three-to-six months' worth of essential living expenses. That may sound like a stretch, but a 20% down payment will mean you can avoid the cost of private mortgage insurance, and a healthy emergency fund protects you from the financial and emotional stress of paying for the many things that can go wrong with a house.

Establish a reasonable housing budget

No matter how much a mortgage lender says you can afford, set your sights on a home in which your housing payment (mortgage, taxes and insurance) adds up to no more than 25% of monthly gross income, preferably 20%. As we crunched the numbers to come up with SMI's Recommended Spending Guidelines,[1] 25% was the maximum amount that allowed for generous giving, adequate saving and investing, and financial margin.

Ideally, apply that 25% standard to just one income. For a young couple who want to have children one day and where both spouses work outside the home, basing their largest expense—housing—on one income will make it much easier to eventually have one spouse stay home full-time. Even if kids are not in the picture or if both spouses plan to continue working, taking on housing expenses based on two incomes is unwise.

I once talked with a couple who had built an especially expensive lifestyle: two leased cars, frequent dinners out, and a mortgage that required a large portion of their combined high incomes. Then the woman lost her job. When I met with them, their faces were full of fear. His had a tinge of anger. How could she lose her job and put their lifestyle in such peril? But it wasn't her fault. Together they had chosen that high-risk path. Far better to base housing costs on one income.

"Score" the lowest-rate mortgage

As you prepare to apply for a mortgage, keep in mind that your credit score matters greatly in determining if you will qualify and what interest rate you'll get.

FICO credit scores range from 300-850, with the lowest loan rates going to those with the highest scores. (FICO stands for Fair Isaac Corporation, the company that created the credit score.) To obtain the best rate on a mortgage, you'll need a score in the mid 700s or higher.

If you're already working with a lender or mortgage broker, they may be able to pull your credit scores at no cost to you. However, if you're earlier in the process, it's worth paying to obtain your scores before applying for a mortgage. (As maddening as it may be, your credit *report* is free, but not your *score*.[2]) You have three credit scores, one from each of the three credit reporting bureaus. At MyFICO.com, you can purchase all three for $59.85.

Also go to AnnualCreditReport.com where you can get your free credit *reports* from each of the bureaus. Your three credit scores should be within about 50 points of each other. If not, something may have been misreported to one of the bureaus, so go over your credit reports with a fine-tooth comb.

If your scores are lower than you think they should be, look for indications that you have paid your bills late, which is a factor that weighs especially heavy on your score. If your reports show late payments and you know that information is incorrect, contact the creditors in question and ask them to change how that information was reported to the bureaus.

Next, look at your credit utilization. That's the percentage of available credit you are using (regardless of whether you pay your credit card bills in full each month). The best scores go to those who use 10% or less per line of credit and across all lines of credit. If yours is much higher than that, start using less. For example, if you have a credit card with a $10,000 limit, spend no more than $1,000 per month on that card. (Of course, pay your bill in full each month).

If you and your spouse are applying for a mortgage together, all six of your scores will be reviewed (remember, each of you has three). Lenders typically focus on your middle scores and use the lower of the two.

If you are applying for a mortgage that will require only one income and the person whose income you will use has a score in the mid 700s or higher, you don't need to worry about the other person's score, at least not for the purpose of applying for a mortgage. It is fine to apply in only one spouse's name. In most cases, though, it's best to *title* the house in both spouses' names.

Prepare for other monthly payments

A house has a lot of expensive things that can break. So, after buying your home, be sure to allocate a healthy ongoing budgeted amount for monthly maintenance and repairs.

While the exact amount you'll need depends on the age and condition of your house, $200 per *(continued on page 28)*

[1] soundmindinvesting.com/resources#downloads [2] Some credit card providers and online banks may provide one version of your credit score for free.

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

UPGRADING IN A 401(K) OR 403(B) WITH HELP FROM SMI'S PORTFOLIO TRACKER

If you're new to SMI, you may be wondering if you can implement the Fund Upgrading strategy in your 401(k) or 403(b) workplace retirement plan. The answer is: "Yes"—although doing so likely will require the aid of our online tool, the Personal Portfolio Tracker.

Upgrading involves investing in funds demonstrating strong momentum, and then, when those funds begin to lag, replacing them with better performers. The strategy works best when an investor has access to enough funds to be able to replace laggards with leaders.

Almost all workplace plans present challenges for Upgraders. Most, for example, don't provide access to exchange-traded funds (ETFs), even those plans that offer a wide range of investment options through a "brokerage window." Other plans provide just a minimal menu of investment options, giving investors little to choose from. Fortunately, the Tracker offers help for would-be Upgraders in either situation.

Based on your risk tolerance and season of life, first determine how much of your Upgrading portfolio to allocate to stocks and how much to bonds. For Upgraders, this "asset allocation" decision is crucial. Use the guidelines in the "Start Here" section of the SMI website,[1] along with the Fund Upgrading calculator.[2]

Upgrading in a robust retirement plan

If your workplace plan has a brokerage window (it may be called a "self-directed account"), you should be able to implement Fund Upgrading with only a few alterations.

Our new approach to Upgrading (see the January 2021 cover article) calls for investing the stock-based portion of your portfolio across seven funds—five actively managed funds and two passively managed index funds. An active recommendation is subject to being replaced—i.e., "upgraded"—when its performance lags and it no longer meets our top-quartile guideline. In contrast, the index funds serve as longer-term holdings. (If your asset allocation includes the use of bonds, we suggest one rotating actively managed bond fund and two "permanent" bond index funds.[3])

Assuming your workplace plan doesn't offer ETFs, you'll need to find a *traditional-fund* alternative any time Upgrading recommends an ETF. To help, we try to suggest one or more comparable traditional mutual fund alternatives when an ETF is recommended, or we point you to the appropriate risk category within SMI's monthly *Fund Performance Rankings* report[4] where you can look through a listing of high-momentum alternative funds.

Once you've selected any necessary substitutes, go to the Tracker[5] and click "Create a New Portfolio." Enter the ticker symbols of all of the current Upgrading recommendations available via your plan, along with tickers of any substitute funds you've selected. (If you'd like your index holdings to show up in your Tracker report, enter those as well.)

Next, click "View Portfolio." The Tracker's default Category View will display your retirement-plan portfolio—including the official Upgrading recommendations in which you've invested plus any substitute funds you're using.

Be aware that the risk categories shown in the Tracker differ from those used in the SMI newsletter. Instead of displaying the newsletter's streamlined "Large Company," "Small Company," and "Situational" categories, the Tracker remains more granular, using Large/Growth, Large/Value, Small/Growth, Small/Value, Foreign and Other.

Treat the Small/Value and Small/Growth categories as Upgrading's Small Company category, the Large/Value and Large/Growth categories as Upgrading's Large Company category. Treat Foreign and Other Funds as "Situational" holdings. (Any bond funds you've entered will show up in the Other category too.)

For sell/buy signals for your Upgrading portfolio, watch the newsletter each month for any changes to our official fund recommendations. To decide whether to change any of your *substitute* funds, use the Portfolio Tracker's percentile data. As long as a substitute fund stays ranked in the top 25% of its risk-category peers (a percentile number of 1-25), no change is necessary. When it falls out of the top quartile, look for a better-performing alternative with help from the *Fund Performance Rankings*.[6]

Upgrading within a limited plan

Even if your workplace retirement plan doesn't offer access to a brokerage window, you probably have access to index funds similar to those now used in Upgrading. So start there.

Suppose your optimal asset allocation calls for a 100% stock portfolio. That means putting 10% of your portfolio in a Small Company index fund and 30% in a Large Company index fund. (Your workplace plan may not offer separate Growth and Value versions of these indexes. That's okay—use what is available.) If your optimal asset allocation calls for an 80/20 stock/bond portfolio, put 8% in a Small Company stock index, 24% in a Large Company stock index, and 20% in a broad bond index fund, such as a "total bond market" fund. Changes to those index fund allocations should normally happen just once a year.

Next, get a list of the ticker symbols for each domestic actively managed stock fund in your plan, either from your plan's website or your company's HR office. Do *not* include foreign funds (they tend to be too volatile), target-date funds, bond funds, or money market funds.

Once you have a list of appropriate funds, add *all* of them *(continued on page 28)*

[1]www.soundmindinvesting.com [2]bit.ly/Upgrading-Calculator [3]See fund recommendations on page 26. [4]bit.ly/smi-fpr [5]portfolio.soundmindinvesting.com [6]Tracker and FPR performance data typically are updated on the 8th of the month.

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

4TH QUARTER SURGE PROPELS SMI STRATEGIES TO NEW HIGHS

Certain years stand out in American history: 1776, 1865, and 1929, for example. Historians would include others, but there is no doubt that list has grown now that 2020 is behind us. No one will ever forget it, and it likely will get its own chapter in the history books!

Let's quickly recap the year in markets before covering the SMI strategies. Stocks were at all-time highs in February when COVID burst into public view in the U.S. The resulting bear market was the fastest in history by a wide margin—a stunning -34% drop in less than five weeks. Since bear markets have historically taken an average of 18 months (!) to play out, and a global economic shutdown was just beginning, many feared a *prolonged* bear market was likely.

Of course, that's not how the story unfolded. Central banks and governments around the globe flooded their economies with stimulus in an effort to offset the economic shutdowns. In the U.S., the Federal Reserve pumped as much aid into the economy and markets in just a few *weeks* as they did in five *years* after the 2008 financial crisis.[1]

Much to everyone's surprise, it worked—at least as far as the financial markets were concerned. The rapid rebound in stocks mirrored the unprecedented speed of the downturn. By September, stocks had reclaimed all-time highs and would soar to even more incredible heights following the release of positive vaccine news in November.

As for SMI, the value of our diversified approach was on full display in 2020, helping members realize strong gains for the year, while reducing the emotional strain of the sharpest bear market in history. All of the SMI strategies ended the year at or near all-time highs. Here's a closer look at how our strategies worked together to help us navigate this wild year.

Just-the-Basics (JtB) & Stock Upgrading

From April to August, the stock market recovery focused on the relatively small group of "stay at home" technology stocks. These stocks soared while most "real economy" stocks languished. But the complexion of the market rally changed dramatically in the final weeks of 2020, following positive news about COVID-19 vaccines. In November and December, big tech plateaued while smaller stocks caught fire.

Led by their allocations to small-company stocks, Just-the-Basics and Stock Upgrading finished the year strong, with fourth-quarter gains of +19.2% and +19.9%, respectively. Those returns far exceeded those of the large-company dominated Wilshire 5000 (+14.5%) and S&P 500 (+12.2%) indexes.

Turning to 2020's annual returns, it's important to note that the table below reports the *fully invested* returns of JtB and the Wilshire 5000 index. In contrast, Stock Upgrading's defensive protocols shifted it partially *out* of stocks from April to July. There's a surprisingly small gap between the three figures, given that significant difference. *(continued on page 28)*

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]
2020	20.8%	22.4%	18.2%	10.0%	12.4%	45.8%	18.1%
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]
Past 15 Years (Total Gain)	319.9%	277.6%	242.6%	150.8%	294.6%	625.7%	320.8%
Dollar Profits on $100,000[5]	$319,904	$277,599	$242,598	$150,778	$294,638	$625,746	$320,837
Annualized Rate of Return	10.0%	9.3%	8.6%	6.3%	9.6%	14.1%	10.1%

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 2006. Results for 15 years are shown rather than the typical 10 years to provide better insight into the comparative returns of various strategies over longer market cycles. **[H]** Results are hypothetical from backtesting a strategy following a mechanical rules-based system.

[1] May2020:p66

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

HOW FEDERAL WORKERS CAN MAKE THE MOST OF THE THRIFT SAVINGS PLAN

The Thrift Savings Plan (TSP), the U.S. government's 401(k)-type retirement plan for federal workers, is the world's largest defined-contribution retirement plan, with approximately six million participants and nearly $770 billion in assets. Participation is open to active employees of the Federal Employees Retirement System (FERS), the Civil Service Retirement System (CSRS), the uniformed services, and certain other categories of civilian government service.

The program offers a number of valuable benefits, especially for FERS employees. First, Uncle Sam makes an automatic contribution equal to 1% of the employee's salary each pay period. There is no waiting period and the employee doesn't have to be making any contributions of his or her own. (There is a two- to three-year vesting period, depending on the type of work the employee does.)

In addition, the government matches dollar-for-dollar any contributions an employee makes, up to 3% of salary. And the government contributes 50 cents per dollar for the next 2% of salary after that.

Automated decisions for newer hires

If you're covered under FERS, a great goal is to invest *at least 5%* of your salary. That will enable you to take full advantage of the matching money offers. In the past, those hired between August 2010 and September 2020 were *automatically* enrolled at 3% of gross pay going into one of the plan's age-based Lifecycle Funds (an employee can opt out of participating or choose different funds). Now, all new TSP-eligible employees are automatically enrolled with 5% of their gross pay going into the TSP. While 3-5% is a good start, that amount is unlikely to be enough to meet your retirement savings goals, so make sure you're investing enough either by contributing more to the TSP or an IRA.

For all TSP participants, the maximum annual amount that may be contributed to the plan in 2021 (not counting employer matches) is $19,500, with an additional $6,500 allowed for participants age 50 and older.

Traditional and Roth options

TSP participants may choose the *traditional* TSP (contributions are tax deductible, but taxes are due on money withdrawn in retirement), the *Roth* TSP (no deduction for contributions but also no tax liability on retirement withdrawals), or a *combination*—in which case a participant would spread contributions across the two plans while adhering to the previously mentioned total contribution limits.

Investment options

TSP participants have access to three stock funds (the I, S, and C funds—International, Small Cap, and Common Stock), two conservative funds (F and G—Fixed Income and Government Securities), and 10 blended "Lifecycle Funds" (L funds) that operate like target-date funds.[1] The Lifecycle Funds are offered in five-year increments, ranging from L 2025 to L 2065. There's also an L Income for those already in retirement.

Each L fund is a "fund of funds," with a mix of the five stock and bond funds (I, S, C, F, and G). The more distant the target date of each Lifecycle Fund, the more it allocates to the three stock funds. The closer the target date, the greater the allocation to the two conservative funds.

Don't set it and forget it

Today, newly hired TSP participants have contributions invested automatically in the L with the target date closest to the year the employee will turn 63. Participants can change investments, and because the plan uses such a relatively young assumed retirement age, they might want to. At the very least, double-check how contributions are being invested. The stock/bond mix chosen for you may be more conservative (or aggressive) than you would prefer.

The TSP's Lifecycle Funds offer an interesting contrast to same-date funds offered by Fidelity and Vanguard. For those with a long time horizon, the TSP's 2055-2065 funds are more aggressive than those from Fidelity and Vanguard, with higher allocations to equities. However, from there, the TSP funds quickly become more conservative than the other fund companies' target-date funds.

If you're using a TSP Lifecycle Fund, go through SMI's asset allocation process found in the Start Here section of the SMI website[2] and compare its results with the allocation used by the fund you're considering.

(continued on page 30)

MANAGING THRIFT PLAN ALLOCATIONS

Investment Options for Federal Workers	For Upgrading/JtB Purposes...
The I Fund: Invests in foreign stocks of 21 developed countries. Similar in performance to: Morgan Stanley EAFE Index	Treat as Situational/Foreign
The S Fund: Invests in stocks of small and mid-size U.S. companies. Similar in performance to: Vanguard Extended Market Index	Treat as Small Company
The C Fund: Invests in stocks of larger U.S. companies. Similar in performance to: Vanguard 500 Index	Treat as Large Company
The F Fund: Invests in corporate and govt-backed securities. Similar in performance to: Vanguard Total Bond Market Index	Treat as Bond
The G Fund: Invests in a non-marketable U.S. Treasury securities. Similar in performance to: Government-only money market funds	Treat as Other

The L Funds: These funds invest in the five funds listed above. The percentage of holdings from each of the I, S, C, F and G funds varies based on target date.

[1] Sep2019:p136 [2] soundmindinvesting.com/start-here/

Basic Strategies

The fund recommendations shown below 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 considered as well, along with the fund's risk level and portfolio manager's philosophy. Recommendations are made in each of the three risk categories shown. Select the fund(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 12/31/2020	Portfolio Invested in	Performance MOM	YTD	1Mo	3Mo	6Mo	12Mo	3Yr Avg	Relative Risk	Expense Ratio	Stock/Bond Mix 100/0	80/20	60/40	40/60	Ticker Symbol
Total International Stock	Foreign stocks	52.7	11.3%	5.8%	16.9%	24.5%	11.3%	5.0%	0.99	0.11%/0.08%	20%	16%	12%	8%	VTIAX/VXUS
Extended Market Index	Small company stocks	99.6	32.2%	7.2%	27.4%	40.0%	32.2%	15.3%	1.35	0.06%/0.06%	40%	32%	24%	16%	VEXAX/VXF
S&P 500 Index	Large company stocks	52.7	18.4%	3.9%	12.2%	22.2%	18.4%	14.1%	1.00	0.04%/0.03%	40%	32%	24%	16%	VFIAX/VOO
Total Bond Market Index	Medium-term bonds	9.7	7.7%	0.2%	0.7%	1.3%	7.7%	5.4%	1.00	0.05%/0.035%	None	20%	40%	60%	VBTLX/BND

JUST-THE-BASICS: JtB is a buy-and-hold *indexing* strategy that helps ensure that 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 funds/ETFs (see ticker symbols in rightmost column—performance data above is for traditional funds). JtB requires only once-a-year maintenance. For more, see Jan2019:p7-8.

RECOMMENDED FUNDS FOR SMI'S STOCK FUND UPGRADING STRATEGY

Risk	Data through 12/31/2020[1]	Ticker Symbol	Percentage Allocated	Date Added	E-Trade Avail[2]	Fidelity Avail[2]	Schwab Avail[2]	MOM[3]	Performance YTD	1Mo	3Mo	6Mo	12Mo	Relative Risk[4]	Exp Ratio	Redemp Fee?[5]
Situational	Invesco DB Commodity Tracking	DBC	10%	01/21	ETF	ETF	ETF	24.1	-7.8%	5.5%	12.6%	19.4%	-7.8%	1.03	0.85	None
	Vanguard Russell 2000 Gwth index	VTWG[6]	10%	01/21	ETF	ETF	ETF	103.3	34.7%	9.4%	29.5%	39.1%	34.7%	1.35	0.15	None
	Traditional fund alternatives to DBC include Alps Funds' JCRAX and Eaton Vance's EAPCX. For alternatives to VTWG, see footnote #6.															
Small Company	Baron Partners Retail	BPTRX	15%	08/20	NTF	NTF	NTF	301.3	148.5%	15.8%	42.8%	110.0%	148.5%	2.08	2.22	None
	Renaissance IPO	IPO	15%	11/20	ETF	ETF	ETF	190.7	107.9%	0.0%	23.4%	59.5%	107.9%	1.63	0.60	None
	iShares Russell 2000 Gwth index	IWO[6]	10%	01/21	ETF	ETF	ETF	103.2	34.7%	9.3%	29.6%	39.0%	34.7%	1.35	0.24	None
	For alternative small/growth options, see categories 207-208 on pages 21-22 of the monthly *Fund Performance Rankings*.															
Large Company	Morgan Stanley Insight A - LW[7]	CPOAX	10%	08/20	NTF	NTF	NTF	173.1	116.0%	0.4%	15.5%	41.6%	116.0%	1.44	1.17	None
	iShares Russell 1000 Gwth index	IWF[8]	30%	01/21	ETF	ETF	ETF	75.7	38.3%	4.5%	11.4%	26.1%	38.3%	1.06	0.19	None
	For alternative large/growth options, see categories 203-204 on pages 17-18 of the monthly *Fund Performance Rankings*.															

Footnotes: [1] Fund recommendations are based primarily on momentum scores in late January, rather than on the December-ending data shown. **[2] Fund Availability:** NTF (no transaction fee) means the fund can be bought and sold without a transaction fee if you stay within the trading limitations imposed by E-Trade (800-387-2331), Fidelity (800-343-3548), or Schwab (800-435-4000). Policies may change, so verify accuracy. ETFs (exchange-traded funds) are available at all brokers and typically without a fee if bought/sold online. See Dec2020:p184 for details about trading ETFs. **[3] Momentum**, SMI's primary performance-evaluation tool, is a measure of a fund's performance over the past year. 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 Nov2020:p167. **[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. Check with your broker for the most current information. **[6]** Traditional-fund alternatives to index ETFs VTWG and IWO include Vanguard's VSGAX and Fidelity's FECGX. **[7]** Buy only if available from your broker as *load-waived*. **[8]** Traditional-fund alternatives to the index ETF IWF include Schwab's SWLGX and Fidelity's FSPGX.

RECOMMENDED FUNDS FOR SMI'S BOND FUND UPGRADING STRATEGY

Data through 12/31/2020[1]	Ticker Symbol	Percentage Allocated	Date Added	E-Trade Avail[2]	Fidelity Avail[2]	Schwab Avail[2]	MOM[3]	Performance YTD	1Mo	3Mo	6Mo	12Mo	Duration[9]	Exp Ratio	Redemp Fee?[5]
Carillon Reams Core Plus[10]	SCPYX[11]	50%	05/20	NTF	NTF	NTF	21.0	16.1%	0.3%	1.6%	3.3%	16.1%	4.6	0.80	None
Permanent: Vanguard I-T Bond	BIV[12]	25%	Perm	ETF	ETF	ETF	11.9	9.7%	0.2%	0.7%	1.6%	9.7%	6.5	0.05	None
Permanent: Vanguard S-T Bond	BSV[13]	25%	Perm	ETF	ETF	ETF	5.7	4.7%	0.2%	0.3%	0.7%	4.7%	2.8	0.05	None

Footnotes: [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] 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 the rotating fund) are fixed and don't change from month to month. See Jan2015:p7 for more information. **[11]** Or buy the institutional share class SCPZX. **[12]** Those preferring a traditional mutual fund option can buy Vanguard's VBILX. **[13]** Those preferring a traditional mutual fund option can buy Vanguard's 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 subscribers with a Basic-level membership have access to two investing strategies. These strategies differ in philosophy and the amount of attention required.

Our preferred strategy is **Fund Upgrading**. It's based on the idea that if you are willing to monitor your mutual-fund holdings regularly and replace laggards periodically, you can improve your returns. While Upgrading is relatively low-maintenance, it does require checking your holdings each month and replacing funds occasionally. (If you don't wish to do this yourself, a professionally managed version of Upgrading is available—learn more at bit.ly/smifx.)

As an alternative to Upgrading, we offer **Just-the-Basics** (JtB), a strategy based on investing via index funds. JtB requires attention only once a year. The JtB strategy is helpful to SMI members whose workplace retirement plans lack a sufficient number of fund options to make successful Upgrading possible. On the Basic Strategies page at left, see the top section for the funds and percentage allocations we recommend for JtB.

Past returns for both Upgrading and Just-the-Basics are shown on the back page of this issue.

A BROKERAGE ACCOUNT

Opening an account with a discount broker that offers a large selection of no-load funds simplifies the Upgrading process. Having such an account allows you to easily buy/sell no-load mutual fund shares without having to open separate accounts at various fund organizations. We recommend reading our latest Broker Review (March 2018:Cover article, also available online at bit.ly/smibroker) for the pros and cons of each broker. Your specific investing needs will dictate which broker is best suited to your situation.

401(K) INVESTORS

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

HOW TO BEGIN UPGRADING

❶ Determine your stock/bond target allocation by working through the investment temperament quiz online in the "Start Here" section of the SMI website at soundmindinvesting.com. (Look for the "Start Here" link on the main navigation bar near the top of the page). Table 1 in the center column at left provides guidelines for those with an "Explorer" temperament.

❷ Using Table 2, find the column that matches your suggested stock/bond allocation. For example, an investor whose stock/bond allocation is 80% stocks/20% bonds would use the percentages shown in the second column. (If your allocation target falls between two listed columns, split the difference.)

For each of the seven recommended stock funds and, if applicable, each of the three recommended bond funds, calculate the dollar amount to invest in each fund. Simply multiply the percentage shown for each fund by the overall number of dollars you have to invest.[1]

❸ Now it's time to buy your funds. Look at the fund recommendations on the opposite page. For each category—Situational, Small Company, Large Company, and (if applicable) Bonds—invest in the funds shown. If a recommended fund isn't available via your broker, find an alternative fund from the same category by using SMI's monthly *Fund Performance Rankings* report (bit.ly/smi-fpr).

Once you've made your fund investments and your portfolio is in place, check the Basic Strategies page each month for any new recommendations. When an owned fund is dropped as a recommendation, sell it and invest in a newly recommended fund.

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 Seasons-of-Life recommendations for an investor with an "Explorer" temperament. See Step ❶ in the text for information on our investment temperament quiz. You may want to fine-tune the above percentages to suit your personal approach to risk-taking.

❷ FIND YOUR PORTFOLIO MIX

Portion of Portfolio Allocated to Stocks:	100%	80%	60%	40%
Portion of Portfolio Allocated to Bonds:	**None**	**20%**	**40%**	**60%**
Stock: Situational Fund	10%	8%	6%	4%
Stock: Situational Fund	10%	8%	6%	4%
Stock: Small-Company / Active Fund	15%	12%	9%	6%
Stock: Small-Company / Active Fund	15%	12%	9%	6%
Stock: Small-Company / Index Fund	10%	8%	6%	4%
Stock: Large-Company / Active Fund	10%	8%	6%	4%
Stock: Large-Company / Index Fund	30%	24%	18%	12%
Bond: "Rotating" Bond Fund	None	10%	20%	30%
Bond: Intermediate-Term Bond Fund	None	5%	10%	15%
Bond: Short-Term Bond Fund	None	5%	10%	15%

❸ BUY YOUR FUNDS

Using the dollar amounts calculated for each row in Table 2, invest in the corresponding funds listed in the Fund Upgrading section of the Basic Strategies page.

To purchase a fund, log in to your brokerage account. Click the word "Trade" or "Invest" (account interfaces vary by broker), then choose the type of fund you wish to buy. Some SMI recommendations are traditional mutual funds while others are exchange-traded funds (ETFs).

Enter the fund's ticker symbol along with the dollar amount of your investment. If purchasing an ETF, you may have to convert the dollar amount to "number of shares" using your broker's online calculator.

Review your order and complete your purchase. Trades of traditional mutual funds will be filled after the market closes for the day. ETF trades, if using a "market order," typically will execute right away.[2]

MORE ON BOND UPGRADING

Your bond allocation (if any) is divided among three funds, as seen in Table 2. One-half the bond allocation is invested in a "rotating" Upgrading selection, which is reviewed monthly and changes from time to time. The other half is divided evenly between two permanent holdings: a short-term bond fund and an intermediate-term bond fund (both are index funds).

For more on why SMI approaches bond investing this way, see "Introducing an Upgrading Approach to Bond Investing that Outperforms the Bond Market" (bit.ly/smibondupgrading). ◆

[1]Rounding off to the nearest $100 for each fund is fine. To make the calculation process easier, use SMI's online Fund Upgrading Calculator at bit.ly/upgrading-calc. [2]For more on ETF order types, see Dec2020:p184.

LEVEL 1 / CONTINUED FROM PAGE 22

MAKING SURE YOUR HOUSE DOESN'T OWN YOU

month is a good starting point. Some months you'll only need to replace a light bulb or two. But at some point you may need to replace a roof or furnace. So, when you have a "light-bulb month," put the remaining portion of your monthly maintenance and repairs budget into savings for those more expensive months.

Can you afford your house?

After reading this article, you may realize you're *already* paying too much for housing. If so, consider something radical. Consider selling your house and moving to one that's more affordable. It's a crazy-sounding idea. Completely impractical. *And* it may just be the best move you could make.

That's what Carol and Tim decided to do. They had been living in what Carol described as her dream home. It wasn't that it was so large or lavish. It's just that it reminded her of her childhood home. But after realizing they had stretched too far to buy the house, they made the agonizing decision to sell.

Carol said two aspects of their move deepened their relationship with God. First, the speed with which their home sold seemed miraculous. Even though many houses in their community were sitting on the market for over a year, theirs sold in a month, and for nearly their full asking price. They saw it as God's affirmation of their decision to sell.

Second, they saw that they had unintentionally moved God out from the center of their lives. "Without realizing it, I think we were trying to fit in to the culture," Carol explained. "Our identities were in where we lived and what we did. They weren't where they should be. When we made this move, it stripped away a lot of things for us. I think of it as kind of a time-out. It's been a reminder that we are just as treasured and just as worthy if we live here as if we live somewhere else."

And they are so much freer—free from other debt they were able to pay off because of their lower housing costs, free to spend more time with their daughter, and much freer from financial worry.

Get the housing decision wrong, and your house will own you. Get it right, and your house will truly be a home. ◆

LEVEL 2 / CONTINUED FROM PAGE 23

UPGRADING IN A 401(K) OR 403(B) WITH HELP FROM SMI'S PORTFOLIO TRACKER

to the Tracker. Click "Create a New Portfolio," and enter each fund's ticker symbol. Then, click "View Portfolio" and use the toggle button to choose "Momentum View."

The funds you entered will be displayed by current *momentum scores* (not by risk category), starting with the highest-momentum funds. These top performers are the funds from which you should choose. How many to hold at any given time is based on the number of funds you entered into the Tracker, as shown in the nearby table.

Let's suppose your optimal asset allocation is 100% stocks and you already have 40% of your portfolio allocated to the two stock-based index funds mentioned earlier (10% to a Small Company index fund and 30% to a Large Company index fund). Let's assume you have *fewer than 20* actively managed funds from which to choose. In that case, spread the remaining 60% of your portfolio equally across the top three funds as the nearby table suggests (row 2). Or if your optimal asset allocation is 80% stocks/20% bonds, and you already had 52% of your portfolio allocated to index funds (8% to a Small Company stock index, 24% to a Large Company stock index, and 20% to a bond fund), you would spread the remaining 48% of your Upgrading portfolio equally across three actively managed funds.

UPGRADING IN A LIMITED PLAN

	Number of Active Funds From Which to Choose	How Many You Should Own at Any One Time	Rank That Must Be Maintained to Continue
1	8 to 14	3	Top 5
2	15 to 19	3	Top 6
3	20 to 24	4	Top 8
4	25 to 29	4	Top 10
5	30 to 50	4	Top 12

For selling guidelines, see the figures in the table's right column. Let's assume you entered 18 actively managed funds when you set up the Tracker. You would have money invested in the three highest-momentum active funds. Each month, you would check the Tracker to see whether any changes are needed. As long as a fund *remains in the top 6* of the 18 funds you are tracking, you would stay invested in that fund. If it falls *below the top 6*, you would replace it with the highest-ranked active fund you don't already own.

Worth the work

Upgrading within a company-based retirement plan isn't quite as simple as Upgrading within an Individual Retirement Account. However, with help from SMI's Personal Portfolio Tracker and *Fund Performance Rankings*, it is doable. The Tracker is SMI's most popular web tool, which means that many of our members find Upgrading in a company plan worth the effort.

We update the Tracker and FPR with data from research company Morningstar on the 8th of the month.[1] To get an email each time those resources are updated, go to soundmindinvesting.com and click "Set up my email updates" in the right column. ◆

LEVEL 3 / CONTINUED FROM PAGE 24

4TH QUARTER SURGE PROPELS SMI STRATEGIES TO NEW HIGHS

JtB's 2020 gain of +22.4% slightly exceeded that of the Wilshire 5000 (+20.8%) and S&P 500 (+18.4%). While the performance of JtB's foreign component lagged the return of U.S. stocks, its allocation to small/medium stocks was a huge winner, gaining +32.2% for the year (with +26.8 points of that gain generated in November and December!).

Stock Upgrading's 2020 return of +18.2% isn't quite as impressive. But digging deeper, we find that Stock Upgrading's return was quite close to the widely-followed S&P 500

[1]Except when the 8th falls on a weekend.

index (+18.4%), *despite Upgrading's defensive protocols exposing it to substantially less risk at a time when devastating losses were a distinct possibility*. If the risks hadn't been so serious, the Fed wouldn't have intervened in unprecedented ways to break the market's downward momentum.

A key to successful investing is avoiding the type of losses that permanently impair your ability to meet your long-term goals. Although the Fed's massive intervention let stock investors off the hook this time, relying on that is a dangerous game. One doesn't have to look back very far (2008-09, 2000-02) for examples of much longer and deeper bear markets. In 2020, Stock Upgrading was positioned to protect SMI investors from that type of extended trauma, yet still bounced back and produced competitive returns.

Bond Upgrading

Even though interest rates started the year near historic lows, the Federal Reserve wasted no time cutting them further—to nearly zero—when the market fireworks began. Longer-term interest rates plummeted as well, with the benchmark 10-year Treasury yield falling from 1.88% at the beginning of the year to 0.54% on March 9. Rates stayed low throughout 2020, with the 10-year yield bottoming at an all-time low of 0.52% on August 4. While rates would rise late in the year on vaccine/economic re-opening optimism, even the late-December peak of 0.96% was just half the level at which 10-year rate started the year.

Allocations to Bond Upgrading play an important role in stabilizing portfolios when stocks are falling. We had a perfect example of that in 2020. Not only did Bond Upgrading produce outstanding absolute and relative returns, gaining +10.0% for the year (while its benchmark index earned just +7.5%), but Bond Upgrading delivered when it was needed most. Nearly all of that return came during the first half of the year, helping offset declines in stocks.

Dynamic Asset Allocation (DAA)

DAA also proved its worth during the bear market. Its changes in the weeks prior to the bear market were nearly ideal, selling Foreign Stocks and Real Estate at the end of January 2020 and shifting into Bonds and Gold. At the end of February, just seven trading days after the stock market set a new all-time high, it sold U.S. Stocks and moved into Cash. By the time markets really crashed in March, DAA was already in its most conservative posture.

2020 PERFORMANCE DAA ETF UNIVERSE

Ticker	Category	2020 Result
SPY	U.S. Stocks	+18.4%
EFA	Foreign Stocks	+7.6%
VNQ	Real Estate	-4.7%
BLV	Long-Term Bonds	+15.8%
SHY	Cash	+3.0%
GLD	Gold	+24.8%

This positioning was an emotional bulwark for SMI investors as they observed one of the most dramatic bear-market plunges in history over the following weeks. With the benefit of hindsight, we know the bear market ended quickly and DAA's conservative positioning would dampen returns in the months that followed. But DAA provided sweet relief at a time when stock investments were getting hit hard.

The strategy delivered exactly what we needed: maximum safety at the point of greatest market risk. That fostered the emotional stability for SMI investors to stay the course and not make the types of course-altering selling mistakes to which investors are prone during violent bear markets.

Sector Rotation (SR)

Sector Rotation lived up to its reputation as the high-risk, high-reward element of the SMI portfolio in 2020. SR suffered a brutal drawdown (high point to low point) of -49.2% during the bear market. Yet it recovered powerfully to post the largest gain of all the SMI strategies, earning +45.8% for the year, more than doubling the return of the broad market.

50/40/10

This portfolio refers to the specific blend of SMI strategies—50% DAA, 40% Upgrading, 10% Sector Rotation—discussed 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 benefits of blending these complementary strategies within a portfolio were clear in 2020. Successful investing requires crafting a plan capable not only of earning solid returns when the markets are rising, but keeping you "in the game" when things are at their worst and the emotional heat feels unbearable. 2020 provided investors with the first serious stress test in a dozen years and an SMI blended portfolio passed with flying colors. Early in the year, our conservative strategies played great defense. Then later in the year, they passed the baton to our more aggressive strategies to play superior offense.

A 50/40/10 portfolio (with 100% stock upgrading) would have advanced +18.1% in 2020. That's a bit less than the Wilshire 5000 index, but quite comparable to the S&P 500's gain of +18.4%.

More importantly, the emotional path to those returns was distinctly different. Many investors spent February and March watching their portfolios nosedive without a parachute. SMI investors experienced significantly less stress knowing their DAA holdings were *already* positioned for the worst-case scenario (and their Stock Upgrading holdings were poised to add further protection should the market continue to fall). Ultimately, Stock Upgrading's defensive protocols turned into an "opportunity cost"—we could have earned even more if we hadn't shifted a portion of the portfolio to cash. But the expectation that every piece of our portfolio would respond *perfectly* to a period that was an incredible historical outlier isn't realistic.

SMI's blended portfolios provided great peace of mind while still posting strong absolute results, despite a dramatic market whipsaw. That's no small accomplishment, given that SMI uses trend-following strategies. In 2020, the trends went from "up big" to "straight down" to "straight back up" in the span of three months! Rapid, dramatic transitions are unusual and far from ideal for trend-following strategies, so

[1]Blending multiple strategies adds complexity. Some SMI members may prefer an automated approach. See bit.ly/SMIPrivateClient.

we are quite pleased with the way our overall performance turned out.

While it's easy to overlook with the benefit of hindsight, if the tremendous intervention by central bankers and governments had *not* stopped the bear market, this recap likely would be focused on how the SMI strategies saved members from devastating losses, unlike investors who lacked such protection. We'll never know exactly how that alternate scenario might have unfolded, but we do know our portfolios were well prepared for a prolonged, deeper drop when that risk was the highest it had been in decades. That should be reassuring to SMI investors as they navigate today's richly-valued, rapidly evolving market environment. ◆

LEVEL 4 / CONTINUED FROM PAGE 25

HOW FEDERAL WORKERS CAN MAKE THE MOST OF THE THRIFT SAVINGS PLAN

Then be sure to choose a LifeCycle fund that's in sync with that allocation.

Using SMI to manage your TSP account

All TSP funds can be tracked using SMI's Personal Portfolio Tracker.[1] The table on page 25 will help you understand how the TSP funds can fit into the asset-allocation structures of SMI's Just-the-Basics and Upgrading strategies.

(Note: In the Tracker, the S Fund appears in the Small Company/Growth category even though the fund includes both Small/Growth *and* Small/Value holdings. The C Fund is displayed in the Tracker's Large/Value category, but the fund is a combination of both Large/Value *and* Large/Growth holdings.)

If the TSP is your only retirement account, you may want to manage it with Just-the-Basics, our full indexing strategy. To build an 80% stock/20% bond portfolio, for example, put 16% in the I fund, 32% in the S fund, 32% in the C fund, and 20% in the F fund.[2]

If you have an IRA in addition to your TSP account, treating the two accounts as a *single portfolio* may enable you to implement Fund Upgrading. Use your TSP account to invest in the index funds used in Upgrading—the S fund for the Small Company index fund and the C fund for the Large Company index fund. Then use your IRA to invest in Upgrading's recommended actively managed funds.

For more on the Thrift Savings Plan, visit www.tsp.gov. To get the downloadable 36-page booklet, *Summary of the Thrift Savings Plan*, go to www.tsp.gov/publications/tspbk08.pdf. ◆

MARKET NOTES, QUOTES, AND ANECDOTES

Good times don't last forever

"I don't know why and I don't know when but eventually investors are going to become uncomfortable once again." – *A Wealth of Common Sense* blogger Ben Carlson, commenting on current market euphoria in a 1/24/21 post, "9 Uncomfortable Facts About the U.S. Stock Market." Read more at bit.ly/3pki1JP.

Every market has its challenges

"If you cannot make it through a bear market without losing your wits, you will never have decent returns. But if you can't survive a bull market without jumping off every time we hit a new high, you will have horrible returns!" – *The Irrelevant Investor* blogger Michael Batnick, in a 1/5/21 post in which he put perma-bear Jeremy Grantham's latest bubble call under the microscope. Read more at bit.ly/39ZA9Cw.

The short-term sells

"When is the last time you heard a pundit say, 'Over the next 10-30 years, I expect this to be a good trade'? Never.... Because the media only talks about the short-term, it encourages us to assign a seemingly logical reason why the market is acting irrationally in the short-term. This causes us to feel like we're acting logically by extension when we make a reactive trade to calm our emotions. But the truth is, rational long-term decisions cannot be made based on short-term irrational market movements." – Ashby Daniels, author of the *Retirement Field Guide* blog, writing on 1/12/21. Read more at bit.ly/3izDmfS.

A silver lining

"Before COVID, you couldn't really ask clients to stay at home for a year to see how much less they might spend. Yet by the time you're in your 80s, that is pretty much what you're doing—there's no commute, not many holidays abroad and your day-to-day living expenses vastly decrease." – Michael Martin, an advisor at Seven Investment Management, quoted in a 1/14/21 *Financial Times* article. He said the pandemic has given people a real-world sense as to what their spending needs might be in the later stages of retirement. Read more at on.ft.com/3qQMxeJ.

Access denied

"This whole idea of being your own bank—let me put it this way: Do you make your own shoes? The reason we have banks is that we don't want to deal with all those things that banks do." – Stefan Thomas, explaining in a 1/12/21 *New York Times* article why he has soured on Bitcoin. He's one of many Bitcoin holders who have lost their passwords, without which they can't access their holdings. Thomas owns over 7,000 Bitcoin that were valued at some $220 million at the time he was interviewed. Read more at nyti.ms/3cacGRN.

[1] portfolio.soundmindinvesting.com. Under "Add Fund," type THRIFT for a clickable list of TSP funds. [2] See the stock/bond mix percentages in the JtB section at the top of p. 26.

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

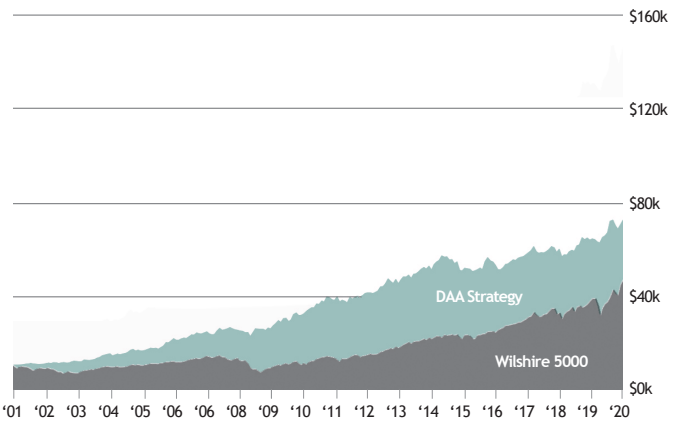
Overview

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 2020



Strategy	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	Avg[1]	Worst12[1]	Rel Risk[1]
DAA	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%	12.4%	10.4%	-13.7%	0.60
Wilshire 5000	-11.0%	-20.9%	31.6%	12.5%	6.4%	15.8%	5.6%	-37.2%	28.3%	17.2%	1.0%	16.1%	33.1%	12.7%	0.7%	13.4%	21.0%	-5.3%	31.0%	20.8%	8.0%	-43.3%	1.00

SECTOR ROTATION

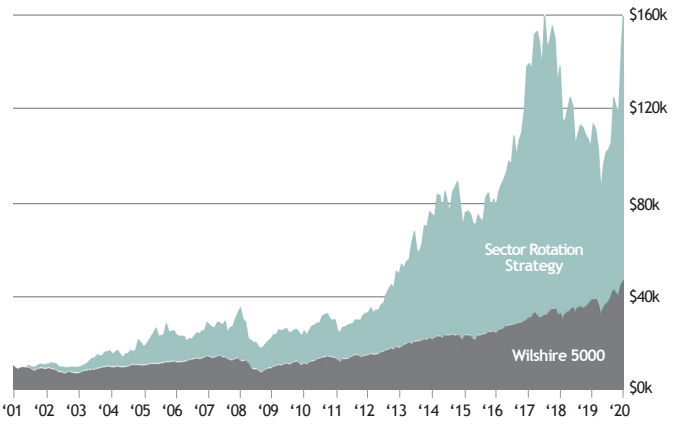
Overview

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 2020



Strategy	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	Avg[1]	Worst12[1]	Rel Risk[1]
SR	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%	45.8%	15.1%	-38.6%	1.69
Wilshire 5000	-11.0%	-20.9%	31.6%	12.5%	6.4%	15.8%	5.6%	-37.2%	28.3%	17.2%	1.0%	16.1%	33.1%	12.7%	0.7%	13.4%	21.0%	-5.3%	31.0%	20.8%	8.0%	-43.3%	1.00

[1]The three data points at the far right in each performance table cover the full 20 years from Jan2001-Dec2020. "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
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Dated Investment Material
Please Do Not Delay!

PERFORMANCE DATA

SOUND MIND INVESTING MODEL PORTFOLIOS • DATA THROUGH DECEMBER 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]	20.8%	4.5%	14.5%	20.8%	14.5%	15.5%	13.8%	10.0%
Just-the-Basics[2]	22.4%	5.7%	19.2%	22.4%	12.8%	14.4%	11.9%	9.3%
Stock Upgrading[3]	18.2%	5.2%	19.9%	18.2%	9.8%	11.6%	10.2%	8.6%
U.S. Bond Market[4]	7.5%	0.1%	0.7%	7.5%	5.3%	4.4%	3.7%	4.4%
Bond Upgrading[5]	10.0%	0.3%	1.1%	10.0%	5.9%	4.7%	4.2%	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]	12.4%	2.8%	3.4%	12.4%	6.8%	7.1%	7.1%	9.6%
Sector Rotation	45.8%	12.6%	37.5%	45.8%	6.5%	17.2%	19.5%	14.1%
50-40-10 Blend[7]	18.1%	4.9%	13.1%	18.1%	8.2%	10.1%	9.8%	10.1%

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 12/31/2020	Year to Date	1 Month	3 Months	12 Months	3 Year Annual	5 Year Annual	10 Year Annual
SMIFX	20.76%	5.31%	18.98%	20.76%	9.56%	10.70%	8.83%
Wilshire 5000	20.82%	4.48%	14.47%	20.82%	14.46%	15.52%	13.79%
S&P 500	18.40%	3.84%	12.15%	18.40%	14.18%	15.22%	13.88%

Quarterly Returns as of 12/31/2020	Year to Date	1 Month	3 Months	12 Months	3 Year Annual	5 Year Annual	10 Year Annual
SMIFX	20.76%	5.31%	18.98%	20.76%	9.56%	10.70%	8.83%
Wilshire 5000	20.82%	4.48%	14.47%	20.82%	14.46%	15.52%	13.79%
S&P 500	18.40%	3.84%	12.15%	18.40%	14.18%	15.22%	13.88%

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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