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4th Quarter 2018 Market Review

Dig Deeper than the Headlines

Dow Jones Industrial Average 1/2/18 to 12/31/18

Many recent articles have pointed out that 2018 was the worst year since the 2008 crisis. This is true. (There have been two negative years since 2008, with 2015 being the other one at -2.23%.)

However, these types of fear-mongering headlines are misleading because they ignore context. If someone had told me at the beginning of 2018 that we would have four rate hikes, a tax cut, massive deregulation, two new Supreme Court justices, mid-term elections, tariff drama and significant changes to our trade agreements with other countries, I would not have been surprised to see a true bear market decline of 20% or more. Yet the DJIA opened the year at 24,809 and closed at 23,327, a loss of 1482 points or -5.9%.

Growing Pains

A major reason for 2018's volatility was, paradoxically, the fact that the economy was strong enough to withstand rising interest rates. The Federal Reserve raised rates four times, which tends to spark volatility. However, remember the reason for raising rates. After the financial crisis, the Federal Reserve dropped the overnight lending rate near zero to stimulate the economy. Now, the Fed is raising rates again to normal levels because the economy has shown signs of strength and recovery. Unemployment, inflation, and other economic metrics are at strong levels. As savers and investors, higher interest rates are a positive because we can receive better yields, and these higher yields will actually serve as a buffer to future volatility. However, a return to normal monetary policy comes with a return to normal levels of volatility. It has been several years since we experienced this! The factors that caused volatility are factors associated with a period of recovery.

Remember that you are an investor, and investing involves a certain degree of risk. Risk is what allows us to have a return! Unfortunately, it means there will be negative years too. This is the tradeoff we accept as investors. A strategy without risk is a strategy without any chance of growth.

Should I Be More Cautious, or More Aggressive?

Sometimes a rocky year prompts investors to question whether their portfolio allocation is appropriate. In bullish markets, investors wonder if they should be more aggressive, and in bearish ones, investors wonder if they should be more conservative. This is natural—we all want more gains and fewer losses. Rest assured, you are already allocated for YOUR needs. Your allocation should never be determined by factors outside your control, such as what happens with the economy or the market. (Note: these are not the same thing!) Your allocation is dependent on what you need personally—for example, how many years you plan to work, your goals for retirement and cash flow needs. Our philosophy is to control the factors within our control, and to take proactive steps to prepare for or mitigate those factors out of our control.

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How We Optimize Your Portfolio for Good Times and Bad

- **Proper allocations.** Remember that your portfolio is *not* the same as the economy, or the major equity indices like the DJIA. Instead, your portfolio mix is designed to expose you to a level of risk and return suited to your specific situation. While everyone likes the gains equities can bring, a down market shows the value of a more balanced approached built on *your* risk propensity and investment objectives.
- **We use an "open architecture" investment platform.** This means we can select *any* investment available. We are independent from any bank, broker, or insurer, so we have no reason to choose anything other than the proper investments for your situation. As fiduciaries, we implement a rigorous screening process to find the optimal securities in each asset class.
- **No trading fees, commissions, up-front charges or deferred charges.** Transaction fees limit your returns. Our clients avoid all commissions, trading costs and holding costs.
- **Your investments are always liquid.** We do not buy funds that have a surrender period or a penalty for withdrawing before a certain amount of time has passed. Having liquidity is critical for your financial stability!
- **We constantly monitor your investments relative to their peers and benchmark.** Ensuring your securities are always the optimal position to hold is an important investment priority.
- T**ax efficient at all times**. Taxes usually have a far greater drag on your returns than any downturn. The tax on a short-term investment gain is your income tax bracket. Even if you wait after 12 months, your tax on investment gains reduces to 15%, 20% or 23.9%, depending on your income tax bracket.

"Don't drive with the rearview mirror."

Right now, my twins have their learners' permits and we are all going through the challenge of driving practice together. When I'm in the passenger seat, I find myself giving the same advice my parents gave me: "Don't drive with the rearview mirror." It's true for investing too. Sure, you need to use the "rearview mirror," and be aware of what has happened in the past, or potential challenges surrounding you—but if you use the rearview mirror to steer your path, you're going to crash.

Loss aversion (the pain of a loss feeling far worse than a gain feels good) is a real behavioral finance phenomenon that all investors experience. It can be difficult to focus ahead on the long term future in times like this, but remember stocks have recovered after *every single* downturn in history to go on to new highs. Do not wait for markets to settle down to make progress on your personal financial goals. **Markets do not settle down—they settle up.**

We have taken steps to help your portfolio weather this process and succeed long term, and I invite you to call or email anytime if you have a question or concern. As always, we appreciate and value the trust you place in us and it is our pleasure to work with you.

All of us at Halpern Financial wish you a terrific 2019 with plenty of health, wealth and happiness! Make big plans and live them!

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