nVEST nSIGHTS

December 31, 2018

IN THIS ISSUE:

nvest WEALTH STRATEGIES

Delivering financial peace of mind.

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CONFUSED? UNDERSTANDABLE

Bill Henderly, CFA, Nvest Wealth Strategies, Inc.

Investing in 2018 did not conclude according to investor wishes. The year was chaotic, volatile, and disappointing. The end of year and the full year were primarily influenced by the Fed and tariffs. Either subject provided sufficient uncertainty to ramp up market volatility and investor worry about the future. It seems fitting to quote famed business management author Tom Peters, from his book "Thriving on Chaos" (published the same day as October 19, 1987 stock market crash), "If you are not confused, you're not paying attention." I remember those two days in 1987 – it was two really bad 30% down days for the stock market. Market declines always leave investors with much uncertainty. Anxiety often moves one to draw conclusions – like recent events will end badly - which is incorrectly based for the future. The sky is <u>not</u> falling as Chicken Little would try to have one believe.

Let's quickly look at key facts to answer current questions – What is the state of the US economy? What are the chances of a recession? And what represents value at current prices? First, the US economy is likely to slow some in 2019 from its fast pace in 2018. But it is still the envy of the world – unemployment rate at 3.9% (near a 50-year low) with wages rising at about 3% while core inflation is +2.2% (with oil prices falling again); worth noting that a *slowing* economy is very different than *contracting;* and a recession is very unlikely with these economic facts. Recessions normally start when the Fed tightens too much, or there is some other policy error – fiscal, regulatory, or trade; or there is some other external big event. Important to know, that while the Fed is tightening, the real (after inflation) Fed Funds rate is only +0.25% higher than the current inflation rate. Prior to the last 8 recessions (back to 1960), the real Fed Funds rate was at least +2.0% higher than inflation. Even though the markets are telling the Fed to stop, slow down, wait and watch, the Fed is a long way from the type of higher rates that are in critical full-blown error territory. We know the Fed is monitoring financial conditions closely, and we expect Fed policy to be better for the markets in 2019. Fiscal policy is still pursuing stimulation, as is regulatory policy. Trade is obviously an issue impacting a global economy which is soft. China is slowing a lot; and Europe is working through many big political and economic issues at a time when the ECB plans to start tightening monetary policy. We suspect the Administration follows the stock market's performance closely (barometer of success). Aware of recent tough market action, the Administration should be strongly incentivized to pursue a tariff resolution with China. Finally, stocks are cheaper than bonds, and selling at levels that support attractive 12-month returns. Someone said, "If you liked it at $50, you love it at $25." These facts should be remembered…

When confusion abounds to cloud perspective, it is appropriate to step back to review correct and historical facts. This action helps remove emotional-based thinking/decisions that can dramatically alter plans for success. We believe 2019 will be a successful investing year. The Fed understands the risks; the Administration understands the tariff impact on the US and global economy. Recent market damage will take time to repair and recover. In the near term, we could likely see more investor fear because of up/down market volatility. Thus the current drawdown process may not be complete. Fear & volatility together, will require additional time to pass for the market to complete its basing process. If the Fed evolves and tariffs resolve, 2019 should reprice on positive fundamentals toward higher levels achieved in September 2018.

SHILLY-SHALLY PRONE

The financial markets are prone to "shilly-shallying" these days. If you blink, you'll miss it. If you take a stroll, you could miss it. If you take a nap, you may be glad you did miss it. The recent volatility of the stock market could be classified as "shilly-shally" prone – moving up/down so quickly that it is difficult to understand what is happening. The first recorded use of the term was from Sir Richard Steele's 1703 comedy, "The Tender Husband, or the Accomplish'd Fools." It includes "I'm for marrying her at once – Why should I stand shilly-shally, like a Country Bumpkin?" Meaning "shall I, shall I not?" Today, the verb means "failing to act resolutely or decisively; or "the government shilly-shallied about the matter."

Despite stock, bond and portfolio performance for 2018, we are not "shily-shally" about investing. We are resolute in managing client portfolios for long term results. We understand that long term

(continued on pg. 2)

"the US economy is likely to slow some in 2019 from its fast pace in 2018. But it is still the envy of the world – unemployment rate at 3.9% with wages rising at about 3% while core inflation is +2.2%; worth noting that a slowing economy is very different than contracting; and a recession is very unlikely with these economic facts."

investing involves up/down movements, with some years being one that is not desired. That was how 2018 ended. The economy performed better than the stock market. Of course, the economy is not the market and the market is not the economy. The market is a discounting mechanism, or sometimes called a "voting machine" that weighs the collective investor buy/sell activity each day based upon often too short-sighted "news." At this time, the fear is that some policy mistake – monetary or trade – is possible (some would argue, even likely).

Entering 2019 the stock market is more attractive at this point, being cheaper by about 15% on a valuation basis (past valuation discounts ranged from 15% to 18%), when a recession and bear market did not occur. We expect the year ahead will provide a positive full-year return experience, and the economy is not likely to slide into recession.

Allow me to share facts about 2 prior time intervals, wherein the market declined -15% or more and a recession did not result. The first looks back to the significant market drop in **1962** where no recession occurred. The market peaked in late 1961 after a virtually uninterrupted run of almost 10 years. In the spring of '62, President Kennedy battled a standoff with the CEO of US Steel, which heightened market selling. Ultimately, the Kennedy Slide of -28% was short lived (138 trading days), with the market indexes hitting new highs just 14 months after bottoming. The economy did not enter a recession. More recent and perhaps relevant, the current environment appears very similar to the winter of early **2016**. In 2015, the US dollar rallied (as it did in 2018); stocks were under pressure in early 2016 declining -15%; oil prices tumbled going into yearend (pushing inflation expectations sharply lower); and the Fed ended 2015 hiking rates despite rapidly tightening financial conditions (like 2018). Then, remember that stocks rallied from February 2016 for the next 2 years without so much as even a 5% pullback as those concerns were resolved or faded. It is very possible that resolution of present-day concerns will occur in early 2019 and lead to attractive and swift relief from recent market volatility.

nvest WEALTH STRATEGIES

Following many bad market historical situations, strong accumulation of stocks quickly emerge coming off the lows. Strong accumulation will be a benchmark for judging the strategic duration of any rally that develops in 2019. We know investment success accrues to long-term investors who endure "shilly-shally" volatility. History is repeat with numerous examples that reward investor endurance.

"Strong accumulation will be a benchmark for judging the strategic duration of any rally that develops in 2019."

WE WORK WITH ROCK STARS

Client portfolios own a diversified mix of no-load mutual funds and ETFs (exchanged traded funds). Our ongoing efforts seek to utilize funds that employ repeatable proven investment processes, with no two funds investing the same way. Funds included in client portfolios are "rock stars", as their strong repeatable investment processes are proven - their historical performance experience is attractive relative to peers. We seek to use funds with reasonable operating expense ratios (as expenses do weigh on investment returns), attractive tax efficiency (for personal accounts), and that are experiencing net money inflows. It is also appealing when the managers of the fund invest a significant amount of their own monies in the fund they manage; they "eat their own cooking".

At year-end, the stock market drawdown afforded us the opportunity to swap from a couple of funds (that distributed large capital gains) into other funds and ETFs that meet various important criteria. We also worked to reduce the capital gains tax impact of these distributions by capturing some losses that developed from the distributions themselves and negative market action. These distributions also increased the level of cash. As we begin 2019, our reinvestment efforts are focused on continuing to own lower risk funds and ETFs as the current bull market is 118 months old (since March 2009). We are attracted to new funds that should assist portfolio management with good tax control. Our modifications also attempt to rebalance the portfolio strategy with small changes, to focus on funds that reside in less risky and/or undervalued market areas, like value-style stock funds. We still own growth-style stock funds; but our tactical strategy is rebalancing toward undervalued market areas.

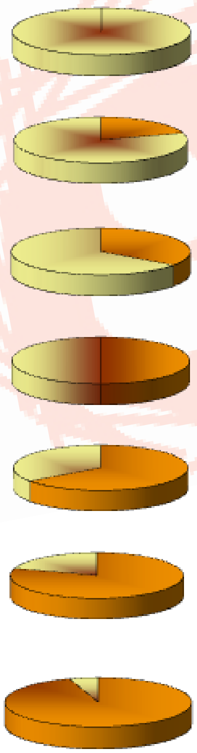
Clients observed changes in their portfolios near year-end. They will also see some continuation of those adjustments during early 2019 as we complete reinvesting cash distributions and new deposits. Please know that our activity is oriented toward managing (minimizing) risk for the expected return opportunity. At this time, we are trying to utilize funds oriented toward providing portfolio safety. Portfolios are managed for the long term, with a close eye on current events and market valuation. If we (clients and us) established portfolio investment objectives correctly, and we utilized "rock star" funds in the portfolios, then clients should be in position to remain a long term investor.

ANNOUNCEMENTS:

- Early January - 1Q 2019 fees collected. 4Q'18 performance reporting delivered
- January 21 - Martin Luther King, Jr Day; markets and banks closed
- Mid-February - Tax Reports delivered by Schwab for the 2018 tax year; Nvest can provide unofficial realized gain/loss and income summaries if desired. See pg. 5 for more detail:
- February 18 - Presidents' Day; markets and banks closed
- March 31 - Last Day of 1Q
- April 15 - Deadline to file personal income taxes; Traditional and Roth IRA contributions for 2018 tax year not accepted after this date.
- Our ADV Part 2A & B as required by the SEC & Ohio (and other states) is available to you anytime upon request.

BENCHMARKING AS OF DECEMBER 31, 2018

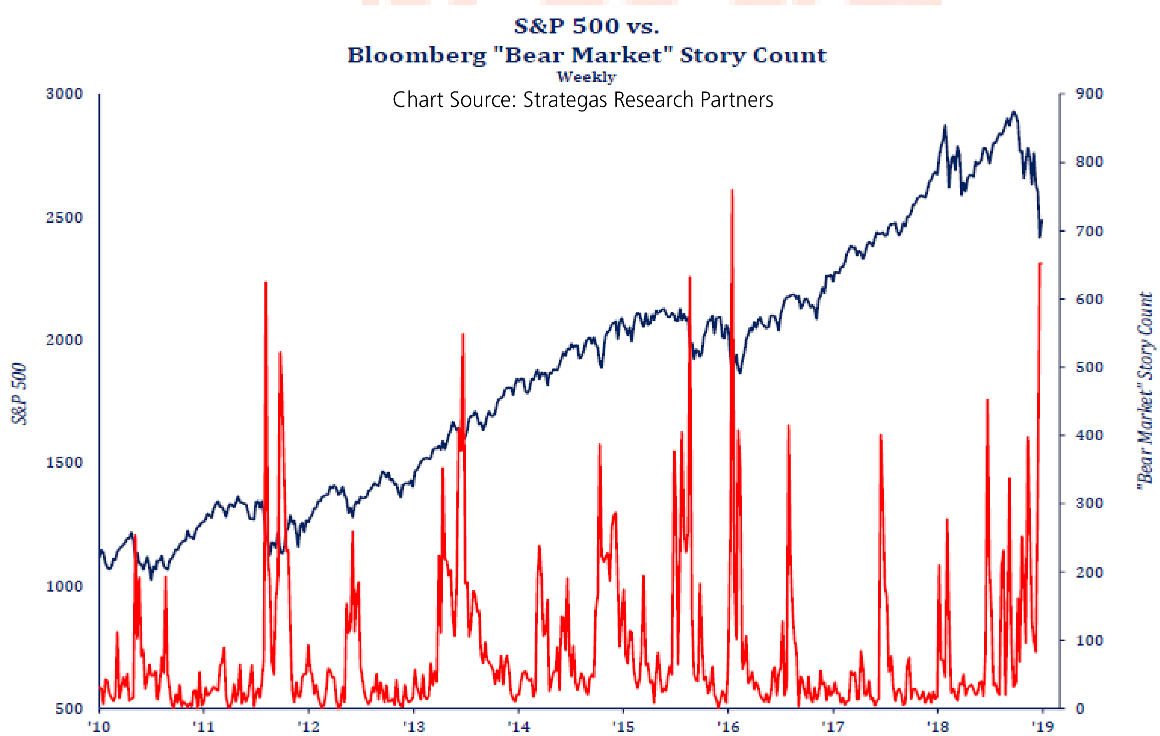
Summary of index portfolio returns compiled by Nvest Wealth Strategies, Inc.



INDEX PORTFOLIO	STOCK/BOND ALLOCATION		TOTAL RETURN THROUGH 12/31/2018			
			4TH QTR	12 MTHS	3 YEARS	5 YEARS
Capital Preservation	0% / 100%	*Cumulative*	0.5%	1.1%	5.0%	6.3%
		Annualized		1.1%	1.6%	1.2%
Income	20% / 80%	*Cumulative*	-2.6%	-1.0%	7.8%	9.7%
		Annualized		-1.0%	2.5%	1.9%
Balanced Conservative	35% / 65%	*Cumulative*	-4.1%	-2.0%	9.3%	11.5%
		Annualized		-2.0%	3.0%	2.2%
Balanced	50% / 50%	*Cumulative*	-6.3%	-3.4%	11.6%	14.6%
		Annualized		-3.4%	3.7%	2.8%
Balanced Growth	65% / 35%	*Cumulative*	-8.6%	-5.0%	13.6%	16.7%
		Annualized		-5.0%	4.3%	3.1%
Growth	80% / 20%	*Cumulative*	-11.0%	-6.3%	16.1%	20.0%
		Annualized		-6.3%	5.1%	3.7%
Aggressive Growth	95% / 5%	*Cumulative*	-12.6%	-7.5%	17.4%	21.2%
		Annualized		-7.5%	5.5%	3.9%

The index returns reflect returns of various mutual fund averages compiled by Morningstar and allocated as follows: Capital Preservation: 90% Bond Average, 10% Treasury Bill Index; Income: 80% Bond, 10% Large Cap, 3% Mid Cap, 2% Small Cap, 5% International; Balanced Conservative: 65% Bond, 15% Large Cap, 5% Mid Cap, 3% Small Cap, 7% International; Balanced: 50% Bond, 24% Large Cap, 7% Mid Cap, 4% Small Cap, 10% International; Balanced Growth: 35% Bond, 30% Large Cap, 9% Mid Cap, 6% Small Cap, 15% International; Growth: 20% Bond, 38% Large Cap, 12% Mid Cap, 8% Small Cap, 17% International; Aggressive Growth: 10% Bond, 40% Large Cap, 15% Mid Cap, 10% Small Cap, 20% International. You cannot invest in these indexes or averages and all above indexes/averages include a 5% allocation to the Treasury Bill Index, reflecting a nominal level of cash. The level of diversification represented by these benchmark averages may be materially different than actual client accounts; therefore, clients may experienced different levels of performance volatility. Past performance is no guarantee of future results.

"Bear Market" word search. A word search for how many times "Bear Market" appears in investment stories provides a different look at investor sentiment. As the chart (right) shows, the word count jumps as the market undergoes big downward movements. Look at the red line "Bear Market" word count in 2015-2016, or 2011 compared to the stock market blue line. It jumps at market lows. It's close again in 2019.



Selected Mutual Funds - Total Return Performance Summary

As of December 31, 2018

Bond Funds - Taxable	Style	4th Qtr	12 Mths	3 Years	5 Years
Taxable Short-Term Bond Average		*0.5%*	*1.0%*	*1.7%*	*1.3%*
Taxable Intermediate Bond Average		*0.9%*	*-0.5%*	*2.2%*	*2.3%*
Wells Fargo Ultra Short	AS	0.2%	1.5%	1.3%	0.9%
AC Alternatives Market Neutral Value	AS	0.0%	-2.7%	0.8%	1.5%
Vanguard Short Federal	HS	1.3%	1.3%	1.0%	1.0%
American Century Short Duration	HS	0.4%	1.3%	1.6%	1.2%
Pioneer Short-Term Income	HS	0.6%	1.4%	1.5%	1.3%
PIMCO Low Duration	HS	0.5%	0.5%	1.4%	1.1%
Vanguard Short-Term Investment Grade	HS	0.6%	0.9%	1.9%	1.7%
American Century GNMA Income	HI	1.7%	0.4%	0.9%	1.7%
Diamond Hill Corporate Credit	LI	-2.3%	0.3%	6.5%	4.5%
Miller Convertible	LI	-7.3%	-6.1%	3.0%	2.6%
Bond Funds - Tax Exempt					
Tax-Free Intermediate Bond Average		*1.2%*	*0.8%*	*1.7%*	*3.1%*
Vanguard Muni Limited Term	HS	1.1%	1.6%	1.1%	1.3%
T. Rowe Price Tax Free S/I	HS	1.1%	1.1%	0.9%	1.1%
Vanguard Muni Intermediate Term	HI	1.7%	1.3%	1.9%	3.2%
Vanguard Ohio Long-Term	HL	1.9%	1.0%	2.7%	4.7%
Stock Funds - Domestic					
S&P 500 Index		*-13.5%*	*-4.4%*	*9.3%*	*8.5%*
Equity Fund Average *(Morningstar Mgr Agg US Core EW)*		*-16.4%*	*-9.7%*	*6.8%*	*5.1%*
Schwab Large Cap Growth	LG	-15.5%	-1.4%	10.5%	10.0%
Parnassus Endeavor	LG	-17.1%	-13.5%	8.0%	9.0%
T.Rowe Price Dividend Growth	LV	-9.2%	-1.1%	9.6%	8.7%
WisdomTree US Quality Dividend Growth	LV	-12.9%	-5.2%	10.4%	8.9%
American Century Equity Income	LV	-7.5%	-4.4%	9.0%	7.9%
Goldman Sachs US Equity Dividend & Premium	LV	-11.9%	-6.6%	6.5%	6.4%
Hennessy Focus	MG	-13.1%	-10.5%	4.6%	5.3%
John Hancock Multifactor Mid-Cap	MB	-15.7%	-9.6%	7.4%	N/A
John Hancock Disciplined Value Mid-Cap	MV	-16.8%	-14.9%	4.1%	5.3%
SPDR S&P600 Small Cap Growth	SG	-19.6%	-4.1%	10.3%	7.4%
Neuberger & Berman Genesis	SB	-16.5%	-6.7%	8.4%	5.0%
Diamond Hill Small-Cap	SV	-16.9%	-15.1%	2.3%	1.5%
SPDR S&P600 Small Cap Value	SV	-20.5%	-12.7%	8.2%	4.9%
Wells Fargo Small-Cap Value	SV	-19.5%	-18.8%	7.1%	2.6%
Stock Funds - International					
Morgan Stanley EAFE Index (Foreign)		*-11.5%*	*-14.2%*	*4.5%*	*0.7%*
Oakmark International	LV	-16.3%	-23.4%	2.4%	-0.5%
Schwab Fundamental International Index	LV	-13.0%	-14.2%	4.6%	0.6%
John Hancock International Growth	LG	-14.1%	-12.3%	4.3%	4.2%
Thornburg Developing World	LG	-6.2%	-15.2%	5.6%	-0.7%
Harding Loevner International Small Company	SG	-16.9%	-17.6%	3.5%	1.9%
Hennessy Japan	LB	-13.9%	-6.6%	11.1%	10.7%
Stock Funds - Specialty					
Salient-Forward Select Income (REIT)	MV	-8.9%	-8.8%	1.7%	3.9%
Neuberger Berman Real Estate Securities	MV	-5.4%	-5.4%	3.1%	6.9%

PLAN FOR A HIGH DEFINITION LIFE

Steve Henderly, CFA, Nvest Wealth Strategies, Inc.

According to a recent study, 90% of Americans will spend more time planning for vacation than they spend planning for retirement. Similarly, we often observe firsthand how many do not truly know where their money is spent; and they do not devote time to gain more clarity about it. Life becomes a foggy trip without rich meaning.

No one purposely sets out to have an undefined financial life… it just happens to us as we become a part of the culture in which we live. It's human nature which spans all of time; we repeat actions generation after generation. One of the wisest men to ever live, Solomon, offers sage points in the Bible's Ecclesiastes which can be simplified to these thoughts:

- the more money we have, the more we want;
- the more we have, the more we spend;
- the more we have, the more we worry;
- the more we have, the more we lose;
- the more we have, the more we leave behind.

Without a sense of priorities for what we do with our financial resources, there is nothing to hold us accountable for the way we spend - unexamined priorities lead to unrestrained spending. The good news: all of Solomon's points can be directly addressed by developing an honest picture of how you live and examining where resources actually flow compared against your priorities. When there are mismatches, there is opportunity for better alignment and creation of a budget that leaves you feeling more satisfied and confident about the future.

For example, some younger individuals often state that savings will need to wait for one reason or another. They may be saddled with student debt while seeing lower earnings than expected in a few years. But regardless of one's situation, there is opportunity to develop thoughtful financial habits early that create flexibility for the future. The first habit is to put at least 10% of pay per year including any employer matching into a tax-advantaged retirement account. The second is to save an additional 5% or more in an "emergency" fund to serve as a buffer in the event of an unexpected expense or decline in income. Once that emergency fund balance covers 3 to 6 months of expenses, the 5% saving rate can be committed to a longer-term goal. If these two goals cannot be accomplished, one's budget should be refined.

At the other end of the spectrum, some individuals with lots of income seem prone to losing track of where money is being spent. Then as a transition to retirement occurs, financial life can feel impossible, and even provoke significant anxiety about the prospects of living a dramatically different lifestyle.

As you enter a New Year in 2019, we advocate pursuing a resolution of "planning for a High Definition life". Planning in "high definition" requires an honest assessment of what your financial life presently looks like, comparing it against priorities, and being specific about what you want for the future.

The difference between a dream and a goal is that dreams are only about the destination, not the journey. A goal requires systems, processes/planning, and structure to facilitate the desired end result. If you would like to start planning, or enhance your plans to be in "high definition", we would enjoy introducing you to that process in 2019. It's part of how we help you achieve financial peace of mind!

SPECIAL TAX NOTICES:

Official tax-related documents and 1099 information will be delivered directly from Schwab to clients with taxable accounts (such as individual, joint, or trust accounts) around mid-February. These 1099 forms detail realized gains/losses and dividend or interest income generated in your account during the 2018 tax year. Schwab intentionally delays delivery of these documents until mid-February to reduce the issuance of corrected 1099 forms.

For retirement accounts, forms detailing distributions (Form 1099-R) will be delivered in mid-January. Reporting of contributions (Form 5498) are made available *after* the April 15 tax filing deadline; if you are <u>planning to make a Traditional or Roth IRA contribution for the 2018 tax year, it must be received by Schwab not later than April 15</u>. Contributions received after that time will either be returned to you or posted as a 2019 contribution. This deadline applies even if you are filing for an extension. If you would like us to furnish Schwab's tax documents to your CPA or tax professional as they become available, please provide us with their contact information in an email.

IMPORTANT: Nvest will not be distributing internal reporting of an annual "tax summary," as we found it creating confusion for clients about what documents are "official" and needed for tax preparation. Further, tax reform effective for the 2018 tax year eliminated many personal deductions - including those for professional services (such as legal fees, accounting services, investment management, and etc.) to help offset the increase of the standard deduction and lowering of marginal tax rates. Please do not hesitate to alert us with any questions on these topics.