Investment Directions

FALL 2018

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✦
NAVIGATE
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ARRIVE

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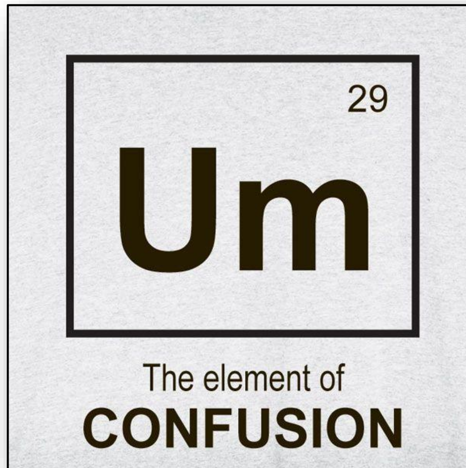

We are living in an interesting, some might say confusing, investment environment.

America's great companies are making money, yet their stock prices have been riding a roller coaster all year. Bonds are paying historically low interest and when the Federal Reserve raised rates in September, traditional, fixed-rate bonds generally got cheaper. Foreign investments have had a tough year, trade wars are looming, some say it's time to buy, others say it's time to sell.

With all these mixed signals, what is the smart money doing? What should you do?

Balance and Flexibility

My answer is to embrace balance and flexibility. I see opportunities before us if we do two things:

1- Don't over-concentrate, and
2- Make adjustments when that seems wise.

This is not as easy as it sounds. For example: major foreign stock indices have lagged major U.S. stock indices most of this year. Is now the time to sell U.S. stocks and buy foreign ones? That would certainly be counter-intuitive, is it crazy, or crazy like a fox?

Flexibility means willingness to make those changes when we think they make sense. Balance means we make course corrections rather than radical reversals.

Applying the Principles

As I write this, LPL research favors three sectors in the U.S. economy: financials, industrials, and technology. By the time you read it, that list may have changed. In a year, all those sectors may be off the list. Flexibility means not falling in love with a single stock or sector but being willing to go where opportunities arise.

Time In the Market Not Timing the market

To be clear, we are not advocating trying to "time the market." Timing the market is notoriously difficult and few, if any, can successfully predict market moves over the long term. What we are advocating is research and valuation. We buy what looks attractive, fully recognizing the price of any given stock or sector is impacted by many factors.

At Compass Advisors we do our research and formulate portfolios that we expect will perform well given our client's wants and needs and in our current environment. If any of these change, we may navigate to a new course heading.

By relying on sound investing principles, like balance and flexibility, we can avoid unnecessary confusion.

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In Support of Pessimism

Regular readers of this newsletter are aware of my optimistic leanings. Periodically I try to provide balance by offering the opposing view. The sentiments below were found at www.despair.com, an excellent source for misery, gloom and hopelessness.

Perseverance

The courage to ignore
the obvious wisdom
of turning back.

Give Up

At some point, hanging in there just makes you look like an even bigger loser.

Discouragement

Because there is nothing standing between you and your goals but a total lack of talent and complete failure of will.

Ambition

The journey of a thousand miles sometimes ends very, very badly.

Dream Small

It's your only hope for success, really.

Quality

The race for quality has no finish line- so technically, it's more like a death march.

Priorities

Hundreds of years from now, it will not matter what my bank account was, the sort of house I lived in, or the kind of car I drove... But the world may be different because I did something so bafflingly crazy that my ruins become a tourist attraction.

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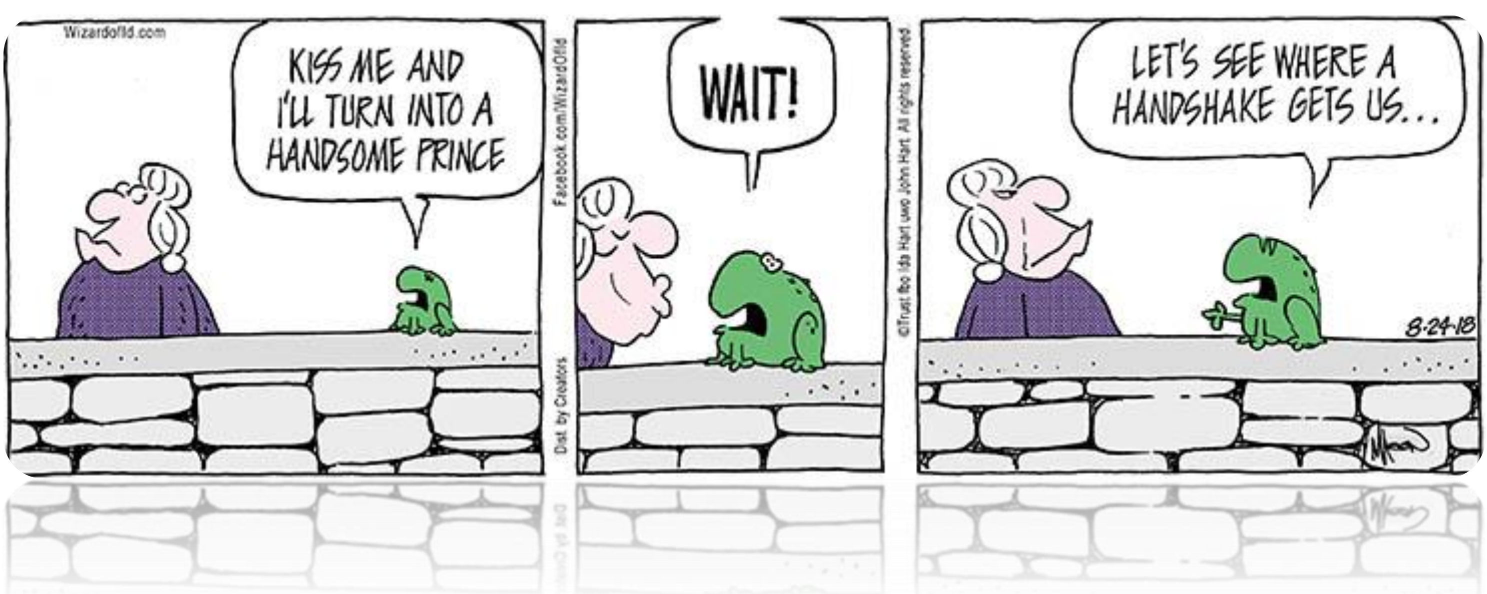

Risk Is A Complex Concept
… but hey, let's tackle it anyway.

To better understand risk, we need to start with your investment objective. Your goal may be to save to buy a home, build a source of retirement income, or pay for education expenses. When you define a specific objective, your investment strategy can focus on that goal – it can be designed with the goal in mind.

When you define a goal, you also identify the specific roadblocks you may face. Any obstacle that may keep you from achieving your goal might be considered "Risk."

This is a major change in perspective. In theory, the simple risk = volatility definition seems to make sense. In the real world, where your investment dollars reside, risk is much more than just volatility.

Objective-based Risks

To illustrate, imagine your objective is to provide sufficient lifetime income after you retire.

One element of risk you might face is volatility. Too much volatility before retirement might foster fear and cause you to give up on your strategy. Also, a big dip just before you plan to retire might result in fewer assets to generate the income you need.

A second risk you might face, is insufficient appreciation. Your future income depends on your future assets. If your retirement-day assets are small, your expected income might also be small.

A third risk is income overreach. How much income can your nestegg provide? If you draw too much, you might eat into your principal and run out of dollars before you run out of days. Generally, lifetime income requires lifetime assets.

Assessing and Addressing

Clearly, managing risk becomes more complex than simply striving to reduce the ups and downs of your account value. The best way to address risk for you depends on your specific objectives and personal situation.

This is precisely why "one-size-fits-all" portfolio construction seldom works. Your portfolio should be tailored to you; it should be based on your personal goals and your tolerance for risk.

Imagine two people, one younger, one older; each prefers limited volatility. The younger person might have 20 years to save for their goal, their greatest risk being insufficient growth. The older person may already be retired, their greatest risk being outliving their retirement savings. Even though they share the same desire for low volatility, their portfolios should probably look quite different to reflect the unique risks they face.

Principles in Action

We might act on these principles by doing the following:

1- Define your objective.
2- Assess your personal preference for risk.
3- Identify the greatest obstacles you might face.
4- Adopt a strategy considering all relevant risks.
5- Select investments appropriate to the needs of the individual.

This is how we at Compass Advisors approach portfolio construction. It is the first step in our 'Chart, Navigate, Arrive" strategy. As the slogan implies, this is just the beginning. Over time, things change: market conditions, interest rates, personal situations, etc. Clearly, ongoing monitoring and continuous risk assessment are also important.

Special thanks to American Funds: Capital Ideas. Concepts from their piece entitled "Rethink Risk: Attributes that matter most for goals-based investors" contributed to this article.

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To determine which investments may be appropriate for you, consult your financial advisor prior to investing.

All performance referenced is historical and is no guarantee of future results.

Stock investing involves risk including loss of principal.

The economic forecasts set forth in the presentation may not develop as predicted. No strategy ensures success or protects against a loss.

CHART ♦ NAVIGATE ♦ ARRIVE

New Tools for New Times

Know What You Own

Editor's Note: This article is related to creating purposeful portfolios of investments. If that sounds boring to you, did you see the Wizard of Id comic strip on page 2? It is quite funny…

Statistics: From Obtuse to Invaluable

For those of you still reading, I offer this analogy: Investing is a bit like baseball. Devotees keep statistics on everything imaginable. Things like how your favorite pitcher performed in away games against left-handed batters when playing at night – no kidding, they have a stat for that.

Similarly, stats are kept on Wall Street too; some fundamental and quite valuable, others more obscure and less helpful in the real world. One very popular method of constructing portfolios is built on analysis of historical statistics and we use it here at Compass Advisors.

Purposeful Portfolio Planning

We consider historical statistics on large American companies, small foreign companies, different types of bonds and a bunch of other assets. Among those other investments are sectors of the U.S. economy, like energy, technology and healthcare. Many of our portfolios include investments in specific sectors.

Peter Lynch, the famed portfolio manager, once said about stock portfolios, "Know what you own." That is the point of this article.

If you invest in sectors of the U.S. economy in your portfolio, something important occurred at the end of September this year. S&P Dow Jones Indices made changes to their sectors and some were quite significant.

New Sectors New Statistics

Without going into excruciating detail, almost 10% of the companies in the S&P 500 index were reclassified. Because of these changes, the future may look quite different from the past.

The information technology sector shrunk, the telecommunications sector was expanded and re-named communication services, and the technology sector lost some of its high fliers. Historical statistics for these sectors will now need a footnote.

Managing Expectations

As we look forward, we should take these changes into account. For example, if we invest in the new technology sector we should be aware it is much more concentrated in Apple Inc. and plan accordingly. If we invest in the new communications services sector expecting it to be defensive like the old telecommunications sector, we may be disappointed.

Knowledge is power. If we know what we own, we can better anticipate how our portfolios might perform.