



Qtr Notes

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Quotes

Money makes people rich; it is a fallacy to think it makes them better, or even that it makes them worse.

Terry Pratchett

The best time to plant a tree was twenty years ago. The second-best time is now.

Anonymous

Time is like money: the less we have of it to spare, the further we make it go.

Josh Billings

It's not how much money you make, but how much money you keep, how hard it works for you, and how many generations you keep it for.

Robert Kiyosaki

Invest in yourself. Your career is the engine of your wealth.

Paul Clitheroe

The Case for Diversification

Every now and then, we get a quarter where the markets are doing great, yet somehow the portfolios aren't quite keeping up. Which are the right numbers to have faith in?

At mid-year, markets and portfolios were both moving sideways, battling to stay positive. In the third quarter, the US stock market decoupled from the rest, climbing to new highs. That's always a welcome event, since our largest exposure is to US stocks. But of our dedicated asset classes, only US stocks soared, while the other pillars of our asset strategies, bonds and foreign stocks, continued to struggle.

It's frustrating when a prudently invested portfolio feels left behind by a good run in one market sector. But the truth is that this is exactly what diversification does, and why it works over the long run. If all investments moved together, rising and falling in unison, there would be no place to hide when the market falls. Do you want all your eggs in the same basket, one that fell 49% and 57% during the last two recessions? Feels great on the way up, but not so much on the way down.

Prudent portfolio managers work diligently to look ahead and identify risks that could harm client wealth: diversification keeps client portfolios prepared for those risks while still moving forward, albeit in smaller steps. The different pillars of diversification address different risks. It's far from perfect and doesn't always keep up with a hot market, but it's a more consistent and trustworthy method.

Here are just a few reasons to stay diversified, especially when things seem to be going so well:

- To protect from identifiable risks
- To protect from unidentifiable risks
- Because we might get inflation
- Because we might get deflation
- Because identifying a bubble is impossible

Index	9/30/2018	YTD
Dow Industrials	26,458.31	7.0%
S&P 500	2,913.98	9.0%
MSCI EAFE	1,973.59	-3.76%
Bloomberg US Bond	2,013.67	-1.6%
US Treas 10-yr yld	3.1%	

- Because timing a bubble is even more impossible
- Because there are other economies with more growth potential than the US
- Because emotions (fear, worry, overconfidence, greed, etc.) are an investor's worst enemy
- Because one market doesn't go up forever; different markets cycle in and out
- Because volatility is back
- Because it forces investment in unpopular sectors (buying low) and rebalancing away from overexposed growth (selling high)
- Because crystal balls don't exist, and there is no such thing as easy money

Whatever the fourth quarter and beyond may bring, our goal is the same: to keep protecting and growing your wealth.

US Economy and Mid-Term Elections

The economic recovery is aging, but instead of slowing, we've seen an acceleration in growth this year. US GDP will surpass 3% in 2018, better than the 2% average of the past few years. Signs of the improving economy are evident in expanding manufacturing activity, retail sales, and elevated consumer sentiment. Corporate executives are also feeling confident, thanks to deregulation and tax reform, credited with contributing to this year's 20% earnings growth.

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Year-End Checklists

When Aretha Franklin died earlier this year, her lawyer revealed that she had never gotten around to making a will. This raises the question: what are we not getting around to? Each year-end is a good time to go through the essential checklists:

- Review your tax withholding: are you penalty-proof?
- Max out your retirement account contributions
- Review your charitable contributions strategy in light of the tax law changes
- Review beneficiary designations on all accounts; update them if needed
- If you are on Medicare, open enrollment runs from October 15 through December 2018
- Take your Required Minimum Distributions on any IRAs and retirement accounts not managed by Firestone Capital Management (we will take care of any accounts under our management)

Along with short-term items, there are also long-term decisions to revisit:

- Draw up or update estate documents (wills, trusts, powers of attorney, health care powers)
- Review or update insurance coverage (umbrella policy, life, disability, LTC, etc.)
- Pay down debt
- Review spending habits and saving goals
- Review charitable involvement
- Establish a retirement or succession plan for your business
- Update retirement planning

The US Economy

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Unemployment levels are near historic lows, and today we have a record-high number of vacant job postings which need to be filled. As the labor market tightens, we would normally start seeing wages rise more, but that hasn't happened just yet. In August, employees saw wages rise just 2.9%, slightly ahead of inflation.

Given the major economic gains, the Federal Reserve is no longer working to further stimulate economic activity. Instead, the Fed is focused on maintaining inflation and employment near current levels. To prevent the possibility of the economy overheating, the Fed raised its benchmark interest rate another 0.25% in September and forecast it would do the same in December. Holders of cash will welcome this news, as savings accounts and money market interest rates should finally edge above 2%. Longer term bond rates haven't gone up as much, and the spread known as the "yield curve" has actually narrowed. As investors, we keep a close eye on this indicator: historically, when this spread hits zero or goes negative, it heralds a recession. But as long as the yield curve remains positive, as it is today, it suggests further economic growth ahead.

The "elephant in the room" remains trade and trade wars. After decades of running large trade deficits, the Trump administration believes the costs of trade have risen too much for the US and its workers. Trump first began imposing tariffs in January of 2018, followed by escalating tariffs applying to ever more goods. Tariffs are a headwind to growth, but proponents view them as a temporary negotiating card.

Late in September, the news broke that NAFTA would be replaced with "USMCA", the US-Mexico-Canada Agreement. Along with the new name, the USMCA has new language intended to help US manufacturing, but largely keeps trilateral trade between the US and its neighbors intact. Markets cheered news of the trade agreement and are hopeful but not as optimistic for a similar quick conclusion to our trade dispute with China.

Trade will be a big talking point in the upcoming mid-term elections. Americans head to the polls in November with all 435 House of Representative seats and a third of the Senate up for election.

Political analysts and pundits are already crunching the numbers, weighing voter surveys, and doing their best to forecast the mood and will of the public. The election results will be viewed as a referendum on the President's entire agenda: trade, immigration, health care, social services are all subjects of extensive debate. Whatever the outcome, the political atmosphere leading up to and following the results will be rife with negativity. Don't let it get to you.

With most of the business-friendly programs proposed by the Administration already in place, there will likely be little immediate impact on the economy from the elections. Consider tax reform, just passed into law and unlikely to be reversed. For our clients, the most important new development in tax reform will be whether municipalities are able to give their residents a way to exceed the \$10,000 cap on deductions for state and local taxes. Several cities in New York are already working to achieve this goal.

The election results will ultimately impact the economy, but not necessarily in the immediate future and not necessarily how most would predict. Whatever the outcome, we expect the White House to push an infrastructure package: both sides of the aisle should support spending to repair roads and bridges. Growth may slow some next year, as the immediate impacts of tax cuts fade, interest rates continue to rise, and the costs of tariffs make their way into our shopping carts. Exactly how fast the economy grows is uncertain, but we are constantly reminded that the economy and people are resourceful and resilient.

History isn't guaranteed to repeat itself, but it's good to note that for every mid-term election since 1962, stocks were up overall during the twelve months following the election. So far this year, US stocks have outperformed other parts of your portfolios. As we approach the end of the year, we are reviewing portfolios to make sure we maintain the proper balance in client accounts. Now is a very good time to have a meaningful discussion about your portfolio with your team at Firestone. Please reach out so we can discuss your concerns, review your financial plan, and ensure your portfolio is properly aligned with your goals and risk tolerance.