

Comprehensive Investment Management, LLC

Fee Only Personal Financial Planning

Spring 2019

A Review of the Financial Markets at March 31, 2019

What a dream come true. At +13.6% the S&P 500 had its best quarterly start in twenty-one years and January was its best month in thirty years. On the other hand it's a dream that followed a nightmare 2018 4th quarter (-14.3%) including the worst December (-9.2%) for the DOW since 1931. Economic global growth expectations dipped so very low it looks like they are going to remain there for some time probably well into 2020.

The following article and charts describe the performance of a select group of mutual funds. Recent market activity can be newsworthy, but for investment purposes the performance over longer periods, while not predictive, is significantly more meaningful.

US Stock Funds

It makes sense to compare the performance of our stock funds to that of Vanguard's 500 Index fund. And even though the 500 had a great quarter our stock funds on average did even better. Except for the last year the return on our funds is considerably higher across all time periods. Small cap fund Brown Capital has reignited, up 19.5% for the quarter. That fire has been burning for some time because the fund's 10 year annual return is 20% and 15 year annual return is 12.5%. Among the large cap funds the top performer for Vanguard was Morgan Growth (17.4%). Vanguard has just merged MG into its US Growth fund. I wonder if after the great quarter Vanguard will change its mind about the combination. The Morgan Growth fund dates back to 1964 and is named for Walter Morgan who founded Wellington Management in 1928. In 1974 Wellington spun off a new entity, the Vanguard Group, led by the ambitious and controversial Jack Bogle who had just been fired by Wellington. No hard feelings, just different ideas about which way the firm should go. Fortunately for the investing public Bogle persisted with his ideas.

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Mutual Fund Categories	Quarter Return	Average Annual Percentage Returns Through March 31, 2019				
		1 Year	3 Years	5 Years	10 Years	15 Years
Short Term Bonds	1.9	3.5	1.7	1.7	2.8	2.8
Intermediate Term Bonds	3.6	4.5	2.1	2.7	4.7	4.1
US Diversified Stocks	13.6	5.6	16.3	12.1	17.4	10.8
Healthcare Stocks	11.7	12.1	12.2	11.9	18.8	12.8
Foreign Stocks	12.9	-5.9	12.4	5.9	13.3	8.6

Morningstar's Take on Vanguard's Bond Funds

There has been recent slippage in Morningstar's rating of the four Vanguard bond funds CIM typically recommends to its clients. Some funds that were rated Silver are now Bronze and some four stars are now two and even one. Here is brief summary of the current comments of Morningstar analysts on each of the funds. The reviews covers five fund attributes: process, performance, people, price and parent.

Intermediate Term Investment Grade / 3 Star Bronze - Alaina Bompiedi

"Despite a recent manager change, a stable process and low fee still give this strategy an edge."

Relative to its peers the fund takes on less credit and interest rate risk. It will likely lag in rallies and outperform in downturns. It follows a simple if not extraordinary process. Its long term middling performance record is due partially to its stash of treasury and high quality corporate bonds plus a relatively short duration. The fund's long term manager unexpectedly left last year.

Inflation Protected Securities / 3 Star Gold - Brian Moriarty

"This continues to be an excellent choice among inflation-fighting strategies".

Management will make modest active bets when opportunities arise but for the most part the strategy runs parallel to its benchmark. To pursue outside opportunities staff must get approval from upstairs. Long term Performance has been strong, helped considerably by low fees. The long term manager remains in place.

Short Term Investment Grade / 4 Star Bronze - Alaina Bompiedi

"The regimented investment process stabilizes this fund despite its recent manager change".

Portfolio managers have some discretion but a well defined internal benchmark grants little wiggle room. Follows a simple if not cutting edge process. The funds longer duration has caused it to under perform. The long time manager left (the same manager mentioned above).

Short Term Bond Index / 2 Star Silver - Phillip Yoo

"A good selection for conservative shorter term fixed income exposure".

The fund accurately captures its target investment universe, i.e. sensible at low cost. Its under performance is attributable to a larger than average commitment to government securities. The staff has extensive experience and is well equipped.

Not necessarily confidence inspiring report cards, but there's no need to rush for the exits. All four funds continue to be rated by Morningstar as Favorites. While we'd like all our funds to be five star gold, Vanguard's bond funds won't reach that level primarily because of its conservative nature. As noted, concern about staff changes, the reason for the bronze ratings, is offset by the tight ship Vanguard runs. The company is noted for its very limited delegation of wiggle room. Because of its lower cost, Vanguard can afford to be more conservative than rivals and still produce competitive returns.

CIM will continue to monitor these ratings. For some clients it will be recommending more risk and expected higher return by adding Vanguard's Hi-Yield Corporate Bond Fund (3 Star Silver) to the bond allocation. That's not a major change in strategy since the Hi-Yield fund itself sits at the conservative end of its benchmark's spectrum. The overall dim outlook for bond returns and recently reduced expectations for higher interest rates adds to the argument that now is a good time for an increase in bond risk.

Overall Morningstar gives Vanguard a glowing review: *"Innovative and iconoclastic from its origins, the firm's mutual ownership structure, commitment to low fees, and sensible active and passive investment strategies are industry hallmarks."* CIM notes that those attributes are primarily due to the legacy of the late John Bogle, who was forced at age seventy to retire from the company he founded.

Morningstar lists the following challenges ahead for Vanguard. Expansion to investors outside the US market who currently make up less than ten percent of the firm's customer base. Potential tension with independent financial advisors due to Vanguard's push into asset-management. Vanguard's ability to keep pace with its own growth, especially the service problems that have been extensively reported. It's CIM opinion that those pains have surely been added to by an ill-advised and poorly planned so-called "upgrade". Don't get me started on that.

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The Financial Markets (from page 1)

Foreign Stock Funds

The foreign funds had a quarterly double digit return of 12.9% recovering from a 12.1% decline in the previous quarter. That was not enough to get to a positive return for the last year but the performance is well in the black for the longer time periods, which is more important. Overall foreign markets and economies have not performed as well as the US since the Great Recession.

Bonds

The accompanying chart provides the performance detail of various Vanguard intermediate bond funds as well as two balanced funds, one of which holds mostly bonds and the other mostly stocks.

High-Yield Corporate bond funds are riskier than other bond funds because they invest in bonds that are rated below investment grade. That means the company that issued the bond has a lower than usual credit rating. Not a very appealing investment premise especially to the typical bond investor who's looking for low risk. That said, Vanguard's Hi-Yield Corporate bond fund is more conservative than most of the funds within its benchmark category. As the chart shows

Annual Returns Intermediate Bonds	1 yr	3 yrs	5 yrs	10 yrs	15 yrs	Since inception
Corporate	5.3	2.7	3.3	6.1	4.6	5.6
Treasury	4.5	.1	2.1	2.7	3.6	5.5
Treasury Inflation Protected	2.6	1.5	1.8	3.2	3.5	5.0
High-Yield Corporate	5.9	6.9	4.5	9.4	6.1	8.3
Bonds vs. Stocks: Annual Returns of Balanced Funds With Opposing Allocations						
Wellesley 65% bonds/35% stocks	6.6	6.1	5.8	9.3	6.7	9.7
Wellington 35% bonds/65% stocks	7.0	9.5	7.6	11.5	7.9	8.3

the fund has performed better than the other bond funds. If it was experiencing heavy defaults that would not be the case. The argument against Hi-Yield is that its market value moves in the same directions as stocks. The argument for Hi-Yield is it can provide better returns without the even higher risk of stocks. In recent years the bond market as a whole has not been performing at its historic levels and that's not expected to change until interest rates move higher which may not happen for some time.

Looking Ahead

The consensus, for what its worth, projects continued slow growth, but not so slow as to lead to a recession. Recent moves in the bond market have hinted at a possible recession and we are overdue for one. But it doesn't seem likely within the next year or two. Continued trade tariffs, the expansion of tariffs in Europe and a chaotic Brexit could change that. While the US is doing well, it's the global economy that might slow us down. The US makes up only half of the world economy. There is certainly no consensus that calls for us to consider a change in any of our stock fund selections or allocations.

For the past month, the market has held up largely because more stable aggressive sectors were doing well, utility and real estate, and big tech giants whose business is viewed as insulated from a soft global economy. The current debate over Fed policy highlights a tricky fork in the road. The White House is calling for the Federal Reserve to reduce the fed rate by a half of a percentage point, in effect, undoing two of its three increases in 2018. It's unusual for the White House to openly solicit actions by the Federal Reserve. Reserve Chairman Jerome Powell insists politics plays no role in its decisions. Growth drives an economy and profits drive stock prices. The current bull market is almost nine years old. If it lasts into September, it will be the longest on record.

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Personal Financial Planning Services

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Q & A with Ruth Bader Ginsburg

Q: Help Ruth, I'm sick. Fidelity just released its annual analysis of healthcare expenses in retirement. \$285,000!! That's the estimate a 65-year-old couple retiring this year will need over the course of their retirement. And that doesn't include long-term care, dental or supplemental medical premiums. How am I to come up with that kind of money?

RBG: Let's not get panicky here. First of all, retirement years are estimated to run about thirty years. \$285,000 spread over thirty years is \$9,500 per year, which is probably not too much different from what you have been paying. Does it worry you to know you'll also need another \$400,000 for food and household expenses? Take any amount of money and run it out thirty years and you'll get a big number.

Fidelity's estimate includes Medicare Part B and D, which for most couples currently runs about \$4,000. Although it doesn't include supplemental premiums it does include the costs that a supplemental policy would cover. So that may very well be a wash. It is the case that you may be accustomed to an employer paying for your health insurance but in retirement you will have to budget that expense for yourself.

The Fidelity report includes this gem: The average retirement age for Americans is sixty-two. One third of those who claim social security at sixty-two do so to pay for health care expenses until they are eligible for Medicare at sixty-five. That's not a good plan. For every year you hold off claiming social security until age seventy there is an 8% increase (8% times 8 years = 64% plus cost of living increases).

Life expectancy is now fourteen years longer than in 1935 when social security was started. Full retirement age then was sixty five, so today it would be seventy-nine. Most people find that scary. In its report Fidelity noted that a longer average life span was a key factor adding to its estimate. Of course retiring at seventy-nine won't work for most people. They may be living longer, but not necessarily staying healthy enough to carry anything close to the work load they carried in earlier years. At eighty six I am very fortunate be one of the exceptions.