Davenport Watts & Drake

INVESTMENT ADVISORS, LLC

Investments • Financial Plans • 401(k) Plans

Volume 9, Issue 1

Tom S. Davenport
Investment Advisor Representative
Chief Executive Officer
Cell 601-672-9202
sonny@davenportwattsdrake.com

Hank Drake, CPA/PFS
Investment Advisor Representative
Cell 601-218-4784
601-437-8846, fax 888-272-1422
hank@davenportwattsdrake.com

Ellen Hazlewood
Client Services Manager
ellen@davenportwattsdrake.com

Linda Estes
Client Services Representative
linda@davenportwattsdrake.com

Suzie Pooley
Client Services Representative
suzie@davenportwattsdrake.com

Douglas White, PhD NSSA BFA™
Investment Advisor Representative
douglas@davenportwattsdrake.com

Jane Watts
Investment Advisor Consultant
Cell 601-613-1954
jane@davenportwattsdrake.com

Financial Peace of Mind

The overall trend for the last half century has been that markets increase despite periodic setbacks. For example, corrections (that is 10%+ declines) have occurred approximately every year and a half. We need to remind ourselves, in the words of Warren Buffet, "Sound investing is simple but not necessarily easy to do". It is a scary experience to watch your portfolio value drop. We posted a blog on our website in April of 2016 that may be of some comfort. The time of the post below is different, but the message remains the same. In early 2016, the stock market underwent an uncomfortable level of volatility, but investors who got out of the market missed one of the strongest run-ups in history through 2017. But our clients who held the course gained as the market soared.

Unquestionably the stock market has experienced severe volatility in recent months. But a review of the historical record provides a clearer perspective on market volatility over the decades that actually favors investors who manage to hang on even in the worst of market declines.

Since World War II, the stock market has experienced, on average, an intra-year decline of 14 percent each and every year. In that same period, the market ended lower, on average, by 18 percent every third year. Bear markets, with an average decline of nearly 30 percent, have occurred every fifth year. Yet, over that same span of nearly seven decades, stock market values have grown 100-fold, which means that, $1,000 invested in the stock market 70 years ago would have grown to $100,000 despite the periodic market declines.

The take away from this is that market declines have, thus far, been nothing more than a momentary interruption in an enduring market advance. Hence, volatility is simply a necessary phenomenon of a market that works. The stock market decline of 2008 will turn out to be nothing but a small blip for a portfolio invested for 20 years.

It took years for the investors who fled the market in 2008 to recoup their losses, while those who kept their sights on their objectives and otherwise stayed the course have enjoyed record gains in their portfolio. This clearly illustrates the human-induced danger of market risk – the risk of locking in losses as stock prices fall. History shows that the stock market rewards investors who avoid harmful behavioral traps such as attempting to time the market. The real detriment to an investor's portfolio isn't participating in the market decline; it's missing out on the market return that follows.

All of our past blogs are archived on our website (www.DavenportWattsDrake.com). Also on our website, you can sign up for our email list to learn more about specific market conditions.

Davenport Watts & Drake
INVESTMENT ADVISORS, LLC

234 W. School Street, Ridgeland, MS 39157
PO Box 2300, Ridgeland, MS 39158-2300

Phone 601-898-8069
Fax 601-853-8087

www.davenportwattsdrake.com

Focusing on your future...

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Investing Perspective

Davenport Watts & Drake clients have financial peace of mind because we have prepared their portfolios with safety in mind for when the next bear market comes. How?

First, we estimate based on client input, how much will need to be withdrawn for the next five years. That amount is invested in "safe assets". What are safe assets? Typically, we think of safe assets as money market funds (cash), cd's, bond funds, and other alternative investments. For example, if $12,000 will be needed annually, then $60,000 should be invested in safe assets. Sometimes a client's risk tolerance calls for an even higher allocation to safe assets. Once we have five years in safe assets, we invest the balance in various equity mutual funds. A typical DWD Balanced Portfolio will have approximately 30 funds. These funds are carefully selected from thousands of funds.

Now, there can be peace when the next stock market correction comes. For it will come. While every person is unique and there is no one exact formula that covers everyone, some guidelines exist:

- Never sell equities in a down market.
- After satisfying the five-year withdrawal need, rebalance to investments that have gone down in value. (This is extremely hard for most people.)
- If you are eligible for a 401(k) or other retirement plan and are in the accumulation stage, increase your monthly contribution if possible.
- Harvest tax losses by selling positions that have a tax loss and immediately buying a similar investment. Repurchase original position after 31 days.

For anyone reading this that is not a DWD client, what if the correction hits and you do not have five years of safe assets? Remembering to never sell equities in a down market if possible, here are some ideas that work if carefully planned:

- Have a home equity line of credit in place for needs during a down market. Rather than liquidating investments at market lows, you can draw on the home equity line of credit.
- Use margin on your taxable accounts. A margin account is where your brokerage loans you money on your investments. We recommend borrowing no more than 10% of portfolio balance.
- Borrow against other assets.
- Sell assets that have not been affected by the stock market.

Debt is like nitroglycerin and can blow up on you if not used carefully. If you decide to use debt, please work carefully with your financial advisor and have a plan to pay the debt off when the market recovers.

A properly designed portfolio and knowledge that markets always recover will carry you through market corrections. The only thing that matters is how you react to them. So review your plan during the good times for any pitfalls in order to have peace during the corrections.

About Our Firm:

Davenport Watts & Drake is a fee-only financial services firm offering asset management and financial consulting services to businesses, families and individuals. Our desire is to work with a select group of these businesses, families and individuals as part of their financial team, helping them with the many decisions throughout their lives which will affect the financial future of themselves and their families. The team has a common vision of a client-centered financial consulting firm that treats our clients as we would want to be treated.

Core Strategies:

- Asset Allocation
- Asset Diversification
- Periodic Rebalancing
- Long-term Perspective
- Minimize Income Taxes

Investment Services:

- Portfolio Management
- Individual Retirement Accounts
- Company Retirement Plans
- Personal Financial Plans

Investment Custodians:

- Fidelity Investments
- John Hancock

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