ANDREWS LUCIA
WEALTH MANAGEMENT LLC

Monthly Investor Letter — July 2019

With so many ups and downs in the stock market over the past few quarters, investors may be tempted to try to predict the stock market to avoid declines and benefit from the gains. Yet there is already a group of professional managers—called tactical asset allocators—who are trying to time the market.

Tactical asset allocators generally tell investors they will avoid stock market declines and participate in stock market gains. This promise appeals to most investors since we are all interested in growing and preserving our wealth. But does the track record of tactical asset allocators support their promise? Thankfully, we came across a 2019 study that sheds light on this subject.

Investment research firm Morningstar had an analyst examine how tactical asset allocation mutual funds performed over the past decade. (Mutual funds are great to review since they are required to publicly publish data, and that data is readily available.) Morningstar looked at how the tactical-allocation category average performed versus a balanced mutual fund (i.e., a 60% stock and 40% bond mutual fund). They used a balanced fund for comparison purposes since tactical funds can be fully invested in stocks or fully invested in bonds at any time, but they tend to be in stocks more often than bonds, so having a higher allocation to stocks creates a relevant comparison.

The results were lackluster.

In their research, Morningstar found that the average tactical fund underperformed the balanced fund by an average of 3.2% per year over the past 15 years ending in 2018. Morningstar also calculated rolling three-year returns from 2006 to 2018 for the average tactical fund and the balanced fund and found that tactical funds never outperformed the balanced fund..

Since the research doesn't support the promise of improved upside, does it support the promise of softening the downside? The answer is no. Morningstar looked at how tactical funds performed when the balanced fund experienced a decline in a given month over the past 15 years ending in 2018. This time period includes the global financial crisis and multiple market corrections, so there were plenty of opportunities for tactical managers to add value. However, the study found that the average tactical fund declined an additional 5% on average any time the balanced fund declined.

This is why we favor our investment approach over others like tactical asset allocators. We don't believe we can predict what stocks or bonds will do on a daily, monthly or quarterly basis. We believe we should invest in stocks for growth and bonds for preservation, and that the balance between those two assets in an investor's portfolio should be determined by their willingness, ability and need to take risk—not some managers hunch or an algorithm's output.

If you have questions about your investments, need to inform us of family or work-related changes or simply want to discuss any financial planning needs, please reach out. We are here to help you reach your financial life goals.

Sincerely,

Scott J. Lucia, CFP & Robert J. Lucia, CPA/PFS