DAVIS INVESTMENT GROUP

Registered Investment Advisor Firm

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5 PERSONAL INVESTING ERRORS

Market timing - Market timing is moving into or out of the market, or switching between asset classes or sectors based on fundamental or technical signals. Substantial dollars are invested in strategies that promise to rotate among asset classes and sectors, or to provide downside protection from a market meltdown.

The appeal is undeniable; however, "all in/all out" strategies aren't sustainable. Morningstar published findings that addressed that issue. Looking at US equity market performance from 1995 to 2014, missing the 10 best days of performance would reduce returns from 9.9% per year to 6.1%; missing the 20 best days would reduce the return to 3.6%. Most investors do not have a crystal ball to help with finding the best days.

Conclusion: Market timing isn't a sustainable strategy for success. It is time in the market, not timing the market. At Davis Investment Group (DIG), we don't encourage market timing as a strategy for all your accounts.

Top performing Mutual Funds always stay there – Chasing performance is among the most damaging investment behavior. Studies have indicated that in most asset classes, the top performing funds in one period tend not to repeat as a winner in subsequent periods.

Conclusion: Investors should have an educated point of view about future performance, and shouldn't consider past performance as a guarantee of future results. At DIG, every 2 months all utilized funds are analyzed to ensure they are still the top performing. If after 4 months they are still underperforming, the funds are replaced with a consistent and better performing fund in that asset class.

Index funds are safer than actively managed funds – Index and "smart beta" products are all the rage today. It is a mistake to exclusively focus on index or smart beta investments.

In 2010, widely used indexes had substantial exposure to the debt of the

PIIGS (Portugal, Italy, Ireland, Greece and Spain). When the European sovereign debt crisis began, these indexes took major hits.

Active managers assessing creditworthiness of countries and companies are better positioned to manage risk than indexes that are blind to bubbles. Many actively managed funds are considerably more diversified, thereby reducing risk.

Conclusion: Investors should understand the investment opportunity they are trying to access and determine whether an index or active investment alternative provides the best combination of risk and reward. At DIG, all listed funds at Schwab are reviewed in all categories, looking for the consistent and top performing funds, whether they are passive or actively managed.

High yielding stocks are a good bond substitute – Dividend-paying stocks are equities and have considerable downside risk. The current low interest rate environment has created an insatiable demand for yield from income-starved investors. Dividend equities have been big winners in 2016, with high-yielding utility sector leading the pack.

Utility stocks trade at 18 times next year's earnings, a high price-to-earnings (PE) ratio relative to the market and sector historically. Utilities are a slow growth, highly regulated sector potentially threatened by the growth of renewable energy sources and energy conservation. The dividend payout is not, in many cases, covered by current cash flow.

Many analysts would argue that utilities are in bubble territory and have considerable downside risk given their high PE, slow growth, high debt and constrained free cash flow.

Conclusion: dividend-paying stocks are an appealing part of the market, but have downside risk and shouldn't be considered a bond substitute. Given their lofty valuation, the downside risk for these stocks may be greater than the risk of bonds and bond funds. At DIG, dividend paying stocks typically fall into the value asset class, not the bond asset class.

Cash is safe – Cash is risky in lost purchasing power and opportunity costs. Many investors have moved to cash after two violent stock market slumps since 2000. I believe every household should have liquid emergency fund of three to six months and increasing cash or short-term investments as people near retirement.

But cash is a lousy investment. Cash can potentially diminish a portfolio given the impact of inflation. One million dollars in cash in 1976 is now worth $236,000 in current purchasing power. Even at today's low rates of inflation, hiding in cash may be risky.

Conclusion: Equities, despite volatility, historically have provided a better return than cash. At DIG, cash is part of a balanced allocation and the percentage is based on the risk/reward needs and goals. During times of contraction, an increase in cash is smart, but not a good long term strategy.

If you want or need more information on how to avoid these investing errors, I would be happy to discuss. Call or email me at the numbers below.

FED Watch

The FED left interest rates unchanged while saying risks to the US economy have subsided and the labor market is getting tighter, suggesting conditions are getting more favorable for an increase in borrowing costs.

Market observers give a 27% (and rising) chance of a quarter point rise in the Fed Funds, and an 18% chance of a rate cut. Go figure.

The next meeting is September 20th and 21st.

Davis Investment Group

Davis Investment Group is a fee-based Registered Investment Advisor firm servicing the needs of clients across the United States.

Davis Investment Group custodies all client assets at Charles Schwab & Co. Davis Investment Group's home office is located at 714 Marin Street, Suite #C, Vallejo, CA 94590. The telephone number is (707) 648-2024.

If you have questions or would like further information on this month's topics or any other financial or investment related subjects, including Social Security claiming strategies, please contact me by phone or through my email address at: bob@davisinvestmentgroup.biz