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INSIDE:

Capital markets, earnings

Interest rates, bonds, inverted curve update

In this catch all article, we take a high level view of the capital markets and the movements that have occurred so far in the year as well as a historical peek at interest rates and their effect on one of the safest asset classes, bonds.

Earnings and Capital Markets

John A. Kvale, CFA, CFP ®

This fantastic chart (see Page 2) shows the eventual correlation of earnings and capital markets, from our friends at Factset. The blue line is the S&P 500 while the dark line is earnings. While it may seem at times capital markets are totally disconnected from reality, much less earnings, markets do (eventually) follow earnings. Divergence often occurs as market participants attempt to anticipate the next event.

(see **Bond,** Page 2)

Why we like high deductibles?

Health insurance, auto insurance and homeowners are the main types of ongoing insurance that allows you more control in your cost via the deductible.

The PLUP, personal umbrella and life insurance policies are notably missing from this conversation as they have little control in deductibles.

Before we begin, its worth reminding a

(see **Higher,** Page 4)

The emergency fund

Simple concept for future safety

It is so simple of a concept but one that is easy to fail. The general rule is to keep 3-6 months living expenses somewhere available, for safety.

Those early in their careers with less dependents and less overhead will find this very manageable. Those of us with a few chips in our armor from big recessions, life's curve balls

(see **If less,** Page 6)

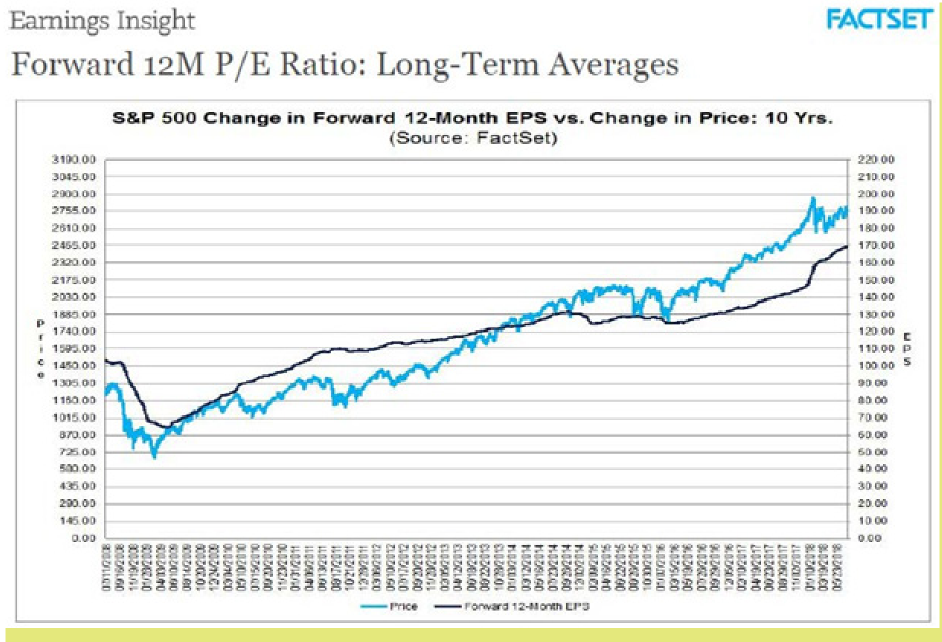
Capital markets, earnings

Bond headwinds likely soon to be tailwinds

(continued from Page 1)

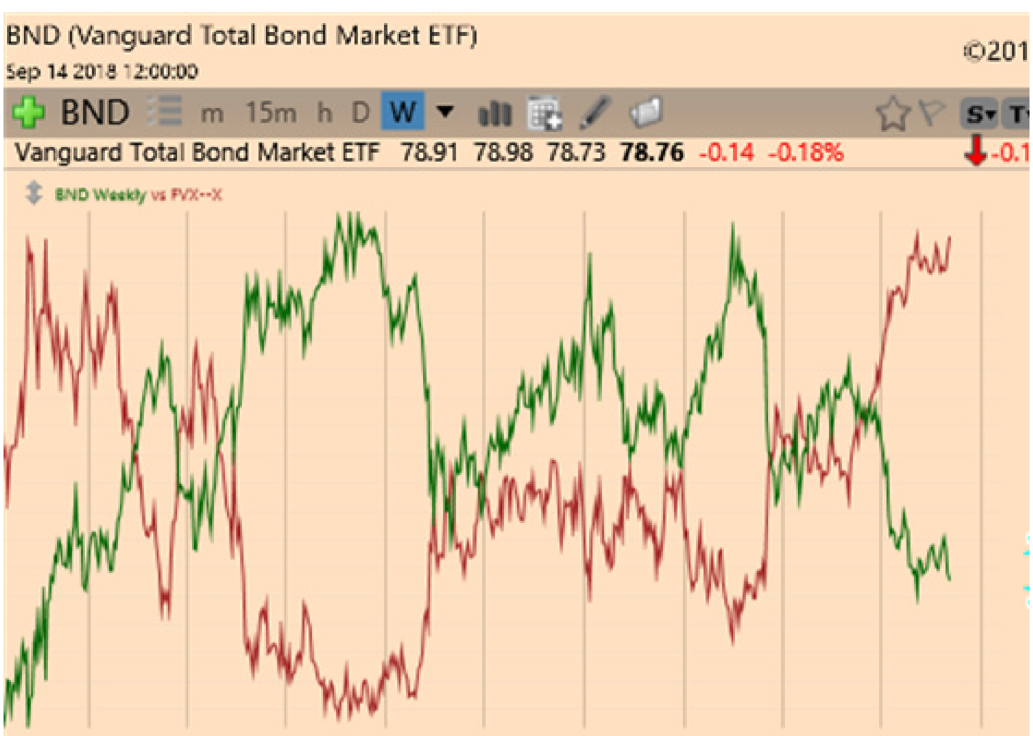
An old saying goes, markets have anticipated 10 of the last two recessions; said another way, fearful divergences occur and over reaction is the norm.

In the year 2018, we are happily racking up huge earnings by publicly traded companies but for the most part, markets are much more subdued. This is actually good news, as the longer this occurs, the greater value (cheaper) capital market will be. If earnings are high and markets are not following, value is being created.



Rising interest rates and the effect on bonds

The following chart (below) is busy but needed to help explain the effects interest rates have – short term- on bonds.



There is a very indirect correlation to bonds and rates – as rates rise, bond values will have headwinds, in the short term. Longer term this headwind becomes a tailwind and increased dividends fill our pockets.

The U.S. Federal Reserve has held rates at an unprecedented low for almost a decade. While it may seem unique now that rates are rising, this cycle is the normal. Rising rates put pressure on even the safest asset class over the short term but longer term this becomes a tailwind.

Shorter term bonds will eventually ride the rate increases as the rise occurs, while extremely longer term bonds may have larger headwinds, a reason not to have significant allocations to extended term bonds unless specifically needed.

How high until rates cause problems?

It's about 5% according to our friends at JPMorgan as shown in the following chart (see chart top of Page 3). The perpendicular line

(see Far from, Page 3)

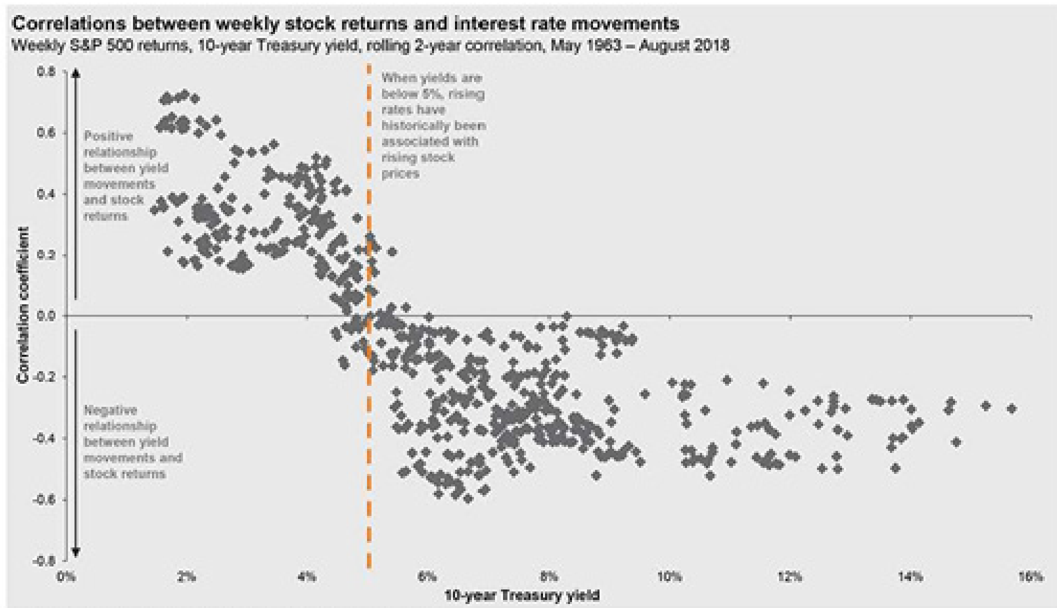
Capital markets, earnings

Far from problem interest rate, curve levels

(continued from Page 2)

in orange in the chart resides at about the 5% level. Historically, according to this chart, is an area that will cause problems for the economy and capital markets.

Currently rates are WAY below this level near the 3% range, a far cry from our historical problem mark; however, we believe that since rates have been so low for so long, this problem level may be lower. We again are no where near an even lowered problem level but are monitoring.



Source: FactSet, FRB, Standard & Poor's, J.P. Morgan Asset Management.
Returns are based on price index only and do not include dividends. Markers represent monthly 2-year correlations only.
Guide to the Markets – U.S. Data are as of August 31, 2018.

J.P.Morgan
Asset Management

Inverted yield curve update

While we discussed the inverted yield curve exhaustively last quarter, apparently the word is out as we heard and read everywhere on this topic in the last 90 days.

When everyone begins focusing on such an item, it frequently looses it's effectiveness and predictability. With even Federal Reserve discussions on the topic we will continue to monitor the yield curve and acknowledge the sudden popularity of the topic.

So far so good!

With gradual rate increases on the horizon, we look to be in good shape to digest these from an economy and capital market standpoint. Bond headwinds will likely soon become tailwinds as we are far from a problem interest rate point and no-where near the inverted yield curve levels. We will continue to watch.

Higher deductibles on policies may save money in long term

(continued from Page 1)

healthy emergency fund is a monumental part of being successful with this strategy. More on this in greater detail but broadly it is a very good idea to always have three to six months emergency living funds set aside at all times in your life!

The auto insurance example

One of the easiest examples is the good old automobile insurance. We like high deductibles of near $1,000 due to the tremendous longer term premium savings that will occur over time.

We certainly acknowledge that changing your coverage deductible to a higher amount today and having an accident tomorrow is bad luck and will throw you into the hole but over time, if you are not a repeat offender, your saved premiums will more than pay for the higher deductible.

Let's say you have a deductible of $250 or even $500 and you are in a fender bender that will cost you $1,100 to fix. We would argue you should never ever have a claim for that small amount of cost over your deductible; and as such, should have a higher deductible.

We would also argue you may want to pay out of your pocket up to around $2,000 to $2,500 in repairs. In addition, in many cases we have found that there is an "insurance" rate to fix the car and an out of pocket rate, which from personal experience can be dramatically different.

Your car is stolen, totaled or involved in a major damaging event? That is what your "major medical" automobile policy is for so call away.

If you are in doubt of the amount, find out the amount BEFORE calling your insurance carrier, as they will be aware of your incident and will monitor it once you have placed the call no matter if you make the claim or not.

Health insurance example

Let's face it, the insurance industry wants us as consumers to take more control over our medical expenses. Rather than run, embrace this coming inevitable change and review higher deductible health insurance plans.

Similar to the auto example, if you opt for a higher deductible plan and something happens in the very short term, you will be in the hole on this decision; however, time is your friend.

Having your health coverage pay for that visit to the doctor for a cold is nice and may make you feel good after you leave the office; however, if you dig deeper, it is likely you may be paying dearly for the "free" visit.

Many higher deductible health plans have special provisions for a regular annual checkup and blood work as they of course want you to take care of yourself and prevent future problems; however, those friendly illnesses shared by the young ones or contracted by a young family member may be worth paying out of pocket.

The higher deductible health insurance plan also opens the possibility of the Health Savings Account (HSA), one of our favorite, pre-tax, above the line, non phased out savings plans.

Similar to the auto example, an absolute must is to have your medical coverage pay for extensive illnesses as these can be extremely costly and are the most important part of health insurance coverage, the major medical expenses.

Homeowners insurance deductible

Yep, there is a higher deductible option for your homeowners policy as well. This option is usually in the form of a percent of the dwelling.

Be careful when reviewing these options as our experience has shown premiums and out of pocket costs can vary greatly depending on the geographic area of your dwelling and a higher percentage deductible can get out of hand if you are not careful on a higher priced dwelling.

Bottom line, the homeowners policy has more moving parts due to the differences in coverages, geographic area, dwelling itself and your claim history. Take extra time in adjusting this deductible, but once you get clear on all costs, obligations and options, it's likely you will find savings in this as well.

The general theme of all of these techniques is to self insure the little things, which are actually most likely to occur and use your insurance coverages for peace of mind on the major items.

In general, by covering the lower cost items out of pocket, your long term savings in premiums will more than pay for themselves. Again, there can be short term set backs and there are always situations where a higher deductible may not be correct, but reviewing your deductibles and cost benefits of a higher amount may be long term in your best interest. JK

Don't leave home without it

PLUP: Personal Liability Umbrella Policy

What's a PLUP? A Personal Liability Umbrella Policy. It is a good idea not to leave home without one in many cases

The personal incident

The case for a Personal Liability Umbrella Policy made it's mark early.

Within two weeks of being married, literally the week we transferred our auto insurance to one carrier, the new Mrs. was involved in a stop and bump.

While exiting a fast paced Dallas, Texas West bound 635 heading onto the service road towards Greenville Avenue, the opposing on ramp to 635 demanded cars cross in an X like manner in order to get off and on.

This exchange of speed of exiting, a fast highway, versus acceleration from a slower frontage road, onto the fast west bound 635 made for the perfect unnecessary stop, creating a rear end collision for anyone but the most careful, as there was no reason to stop other than to initiate a collision from behind.

This technique is especially good when there are allegedly six people in the car, however the Mrs. could only remember five members of the family.

Bringing home such wonderful news less than two weeks into wedlock was not the most enjoyable but after a careful review of the incident, a quick check of the drivable vehicle damage, radars were up.

This event occurred on a Sunday evening. Mid-Monday morning, a call was placed to the new jointly carrier insurance company only to find out that there had already been six lawsuits placed, each at $10,000 (oddly, just under the normal refutable max by most insurance companies).

Brows were raised by both carrier and ourselves at the light speed efficiency of such suits. In a very strange turn of events, one of the alleged injured died while receiving minor chiropractic treatment.

There were five payments of $10,000 paid out and the case was closed. Whew!

If this personal, unassuming event has not shown you the possible need for the PLUP, here are the details of why you may want to look into an Umbrella Policy.

Cost – usually $200 - $500 annually max

In a world of sometimes seemingly ever higher costs, the PLUP is very affordable. Experiences have shown annually, cost of usually between $200 - $500 for $1 million - $2 Million in coverage. (Yes, that is correct, $200 - $500 annually.)

Where to get it?

In most cases, you would want to call your auto/ homeowners agent. The PLUP is most cost efficient when added to your current policy.

This coverage is an add-on to your auto or homeowners policy. This coverage kicks in as a pseudo major medical similar upper limit coverage for liability should you need the extra protection.

Given the cost, it is easy to see this coverage is not utilized frequently but had the personal experience above been slightly different, maximum limits could have easily been met, needing the Umbrella for continued asset protection.

Insures your base coverages are correct

Another neat and settling feature of the PLUP is that it mandates that your standard or base coverages are correct. The reason for this is that the Umbrella Policy actually sits on top of your standard coverages, again similar to a major medical policy sitting on top of your standard health coverage, to only kick in when the base coverages are maxed out.

Said another way, your Umbrella coverage will not allow you to just use it as your coverage, Your standard/ base coverage will need to be in order, prior to allowance of a PLUP policy. We like this automatic review.

When applying or adding a PLUP rider to your policy, you may find your carrier demands different amounts of your base coverage. We applaud this discovery as you likely were underinsured in your base coverage and needed adjusting.

If your cost increased dramatically, be sure to check our article on "Why we like high deductibles."

What you are protecting coverage

The most obvious assets at risk are after tax dollars such as checking, savings and investments including Revocable Trusts. In a bad situation, without the PLOP policy these assets may be at risk in the

(see PLUP, Page 6)

Emergency fund reduces stress, pressure

(continued from Page 1)

and experience, may want this number to be higher. Whatever level makes you "sleep better" within reason, of course, is likely a good level.

Reasons for a higher level

1. Possible job change – need higher emergency funds
2. New family member- Higher is better
3. New home – expect unforeseen expenses. They always occur. (Has anyone ever built or bought a home in less time and for less money than they thought? Nope, it's in our nature.)
4. Salary fluctuations i.e. commissions – Err on the higher side of that emergency fund.
5. Others dependent on you – Business owner, large family, solo income earners, college or wedding... a bit higher is better.

Stability reasons for a normal/lower level

Dual similar incomes – lower emergency fund is ok

Very stable job – smaller side of the living expenses will work

Where to invest ? Safety first

A long time friend always commented on the Mason Jar, full of money, buried in his back yard (an old depression era tale).

All kidding aside, your emergency fund should be bullet proof safe. While that has been hard over the last decade, not earning much interest, now finally we can get a few percentage points on our emergency fund but that is only to keep it from being lazy. It is not an investment and should not be put at risk by stretching for a return. No risking, it needs to be there when the sky is falling.

Big benefits

The most obvious benefit to having a health emergency fund is less stress. Financial issues are well known to be a couple's top stresser and frequently relief is felt as the healthy emergency fund is completed, when no pressure was ever felt in the first place.

Self covering the small things, such as our "higher deductible" article will turn into big savings in the future.

You CANNOT achieve the higher deductible savings technique without a good emergency fund.

Warren Buffet and his huge war chest of cash may be an exaggerated example of how opportunities present themselves for those that are liquid but in an infancy way, liquidity via your emergency fund will certainly not close doors to other opportunities.

Keep it healthy. Plan for draw downs then refill as fast as possible. And keep it safe then let the stress drift away! JK

Don't leave home without it

PLUP: Protection for equity, accidents

(continued from Page 5)

event of a liability judgement is made on you.

Equity in anything that is outside of protected accounts such as an IRA or other retirement plan. Think home equity, property or assets that have no lien against them or have equity, all of which are possible fair game in a nasty battle.

Business interests that would include equity. As a point of clarity, the Umbrella does not protect you from a business liability made during the normal course of business activity; only an outside event attaching itself to your business equity.

Accident examples

The crazy accident at your home, where an acquaintance falls down unexpectedly and injures himself badly and you later find out that this acquaintance is not so friendly and has a desire to hold you accountable for their incident.

Those with kids that may have kid friends over and a similar occurrence from above happens.

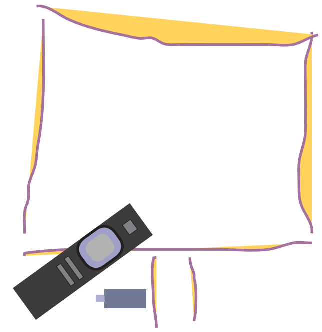
Anyone who drives the streets today has some possible liability. As mentioned in our personal opener, the outcome of the personal situation could have been much different.

If your name is in the fine print somewhere, I.e. President, CFO, V-P or chief anything, you may be seen as "rich" and a target. High profile people are easy targets in many cases. Even if you do not feel you are a worthy target, as long as others perceive you as a good target, you are!

In closing, this article has generated the idea of two additional thoughts, "Why we like high deductibles" and "Importance of an emergency fund." All are interconnected and you can review these topics starting on Page 1 in this newsletter. JK

App of the quarter:

Add on hardware streams programs at good rates



Most quarters we come across a neat new App that we like to share and once, have even had a repeat appearance with one of our very favorites.

This quarter we are reviewing not an App but a neat new hardware component. It has many well healed competitors, that may be a better fit for you; however, we only have experience with our friend and the experiences have been spectacular!

Meet the Amazon Firestick.

Visitor of the office know we have TV's piping in news, (sports), weather and even old movies at slow times of the day. Being in a commercial office address, we have little option but commercial services, UNTIL NOW.

With this handy device, we are able to stream our programs at much more reasonable rates.

While traveling with the tennis player, off times in the evening's sport a much needed reprieve from the day's stress. Due to the frequency of travels, accommodations are usually rustic (cheap) at best.

Enter the Firestick. Within three minutes most of the home stations are ready to go, making for a more relaxed, home like feeling.

Rustic accom-modations lend themselves to old and rarely streaming Wifi connections. Not to worry, while a more steady streaming Wifi is needed, a fast speed is not.

Most techie sites say a speed of 2-3 mbps (this is really not that fast at all) is needed. Buffering occasionally occurs during evening hours but is the unusual, rather than usual.

By taking our home connections with us, the Firestick has become a money saver, as our home costs are not duplicated and even the few premium channels are available on the packages we have.

There are various ways to configure individual packages, beyond our level of knowledge but if one was starting from a blank slate, configuring a basic, specific to your interest package would likely be even more of a money saver.

Multiple units are allowed at same time and with a feeble search under our belts, we have not been able to determine the maximum but have not hit it as of yet either.

As mentioned earlier, there are many competitors. Roku seems to be the most popular but we have no knowledge of any other systems but the Firestick. It may be worth choosing carefully.

Since purchasing our original device, the price is ½ at about $20. That's ok; it has saved us tons and accomplished all that we wanted and more.

It may be worth giving this device or this concept a try if it fits the situation. We have been thoroughly impressed!

JK

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Parting thoughts for you...

We are happy to welcome Jen Hill on board and look forward to bringing you up to speed with her fantastic Wall Street background and experience. Give her a shout if you like; she is excited to get to know all of you!

Don't forget our annual early bird Holiday Party, which is on Nov. 17 (Saturday before Thankgiving) from 3-5 p.m. at Dallas Athletic Club. Save the date. We look forward to seeing you there!

We have some exciting news to share but are forced to keep it under wraps until after the printing of this newsletter; not to worry, when we are able, we will be shouting.

Hope you enjoyed the multiple idea article that spawned from the PLUP (Personal Liability Umbrella Policy). The Emergency Fund and High Deductible ideas fit in perfectly as the ideas clarified. We hope you enjoy.

In our catch all market article which hits on earnings, rates and an update on the inverted yield curve, we look to be in good shape.

See you at the Holiday Party, if not sooner!

Dates:

Oct. 8 - Columbus Day - Dallas TX and surrounding area Fair Day - Schools closed

Nov. 4 - Daylight Savings

Nov. 17 - J.K. Financial Holiday Party 3-5 p.m. DAC

Nov. 22 - Thanksgiving Holiday, U.S. Capital Markets closed

Dec. 25 - Christmas day, U.S. Capital Markets closed