SOUND
WEALTH MANAGEMENT GROUP
OF
RAYMOND JAMES®

HELLO VARGAS

We hope this finds you well! Since our last *SOUND NOTE*: Marisa Tomei's Phone Number, we have found the television financial pundits are at it again… Although we at SOUND Wealth Management Group try to remain rational and use fundamental and empirical data, we must also remain conscious that the world is not always rational, and investors commonly fall victim to habitual irrational behaviors. Many of these responses are influenced by the position of authority; one of our favorite behavioral authors, David McRaney, describes the "argument from authority" as such: *MISCONCEPTION: you are more concerned with the validity of the information than the person delivering it. TRUTH: the status and credentials of an individual greatly influence your perception of that individual's message*.^ If you see someone on TV say it, it must be true – right? From Duke University's Dan Ariely studies: if a television personality is wearing a lab coat when describing their predictions, viewers are more prone to believe the orator and perceive them as an "intelligent authority" with great information; if it was later revealed that the lab coat was actually an art smock, the viewers are less inclined to believe the same axiom (sorry artists)? Sometimes the headline data is downright the opposite of what is *really* happening and we at SWMG feel like we are living in the Bizarro World. In this *SOUND NOTE* we will address a few anecdotes of market behavior, some psychological investor pitfalls, and understated positive economic data.

Sometimes "the data doesn't mattah." We commonly cite the historical statistics of the equities market (S&P 500) to demonstrate that investing in good companies coupled with a financial plan will return satisfactory results over time. Since our last note, the market has dropped 6.95% and as much as 9.71% (from recent market close peak to lowest market close) leading some investors to interpret the movement as a harbinger for a great recession. We can assure you, there have been plenty of "financial authorities" who have touted a market collapse since the 2009 recovery. These premonitions have proven to be losing predictions, as the market has gained over 300% since March of 2009. Further, the statistics are not in their favor * (reference below) and they seldom declare a point to return to stocks. We have commonly poked Dennis Gartman, David Stockman, and Marc Faber, among others, who are – in our opinion – the best people to do the opposite of; when they say good bye, say hello, or bad bye. You are welcome to conduct an internet search on their past predictions; they have all commonly called for +40% corrections in the market on an annual basis. At some point they might be correct, but we would like to see more substance to a bear market call other than "it is due." In our Note *The Assistant To The Traveling Secretary* we demonstrated that the market is up 75% of the time in a calendar year*; a "market" investment – which is inherently diversified – has shown great odds of providing positive results. Using Ned Davis Research going back to 1945, the market has declined 5-10% 78 times with an average decline of 6% - that comes out to about once every year (arithmetically). The average length of time the decline lasted was 1 month and it took – on average – one month to recover. We are currently 7.11% off of an all-time high on the S&P 500 market close. Please see *Chart 1* compiled by Guggenheim Partners to gain perspective on the historical drops and recoveries over the past 73 years – didn't they also create the Museum of Miniatures? Chart 2 and Chart 3 illustrate the viewpoint of longer and medium term pullbacks over 20 years and 5 years, respectively.

Decline %	Number of Declines	Average Decline %	Average Length of Decline in Months	Average Time to Recover in Months
5-10	78	(6)	1	1
10-20	27	(13)	4	3
20-40	8	(27)	11	15
40+	3	(51)	22	58

Chart 1

Chart 2 (Source: ThomsonOne; Sound Wealth Management Group)

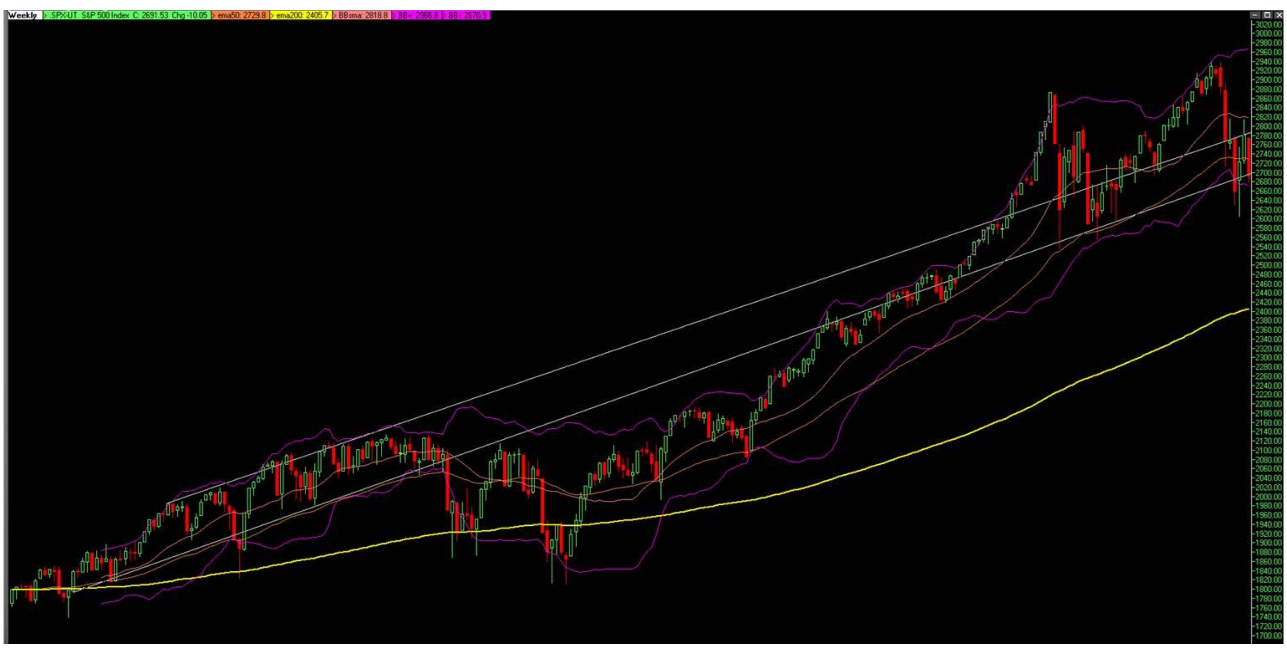

Chart 3 (Source: ThomsonOne; Sound Wealth Management Group)

So far in 2018, we have had two corrections; as of now, both were approximately 11% (greatest divergence intra-trading day) peak-to-trough. Earlier in the year the market put in an all-time high on January 26th and took 147 trading days to get back to a new high. Coming into a traditionally better season for the economic cycle, we will be watching this decline to see if it comes back with greater velocity. Quick resolve on the list of market fears can, and should, expedite the recovery, and we will still be seeing the benefits of tax reform and deregulation on corporate earnings for the upcoming quarters.

Barring any black swan events, we suspect the impetus for the upcoming recovery will be fueled by some political resolve, but mostly by way of share buybacks. In our SOUND NOTE *Incapable of Guile* we analyzed the history of repatriation (or corporate tax holidays) and what companies did with the saved money from these benefits. We highlighted that these actions historically do not do much for the average person in the front-end, however the shareholder received much different treatment. You are welcome to go back and read the note, but the summary is: companies bought their own stock. We feel this time is no different; with the recent dip in stock prices, companies like Apple Inc. (:AAPL)[5] – which has over $230 billion in cash (as of November 1, 2018 earnings) – have great reason to buy their stock back and/or their competition. Using Apple Inc. as an example, the interest on $230 billion cash *does* equate to significant dollars, however the stock offers a $2.92 dividend, 3.14 in free cash flow per share, and a trailing 12 month ROE of 49.4 (buying their own stock appears to be a better choice). There are a multitude of companies that have comparable balance sheets to substantiate significant buybacks and/ or acquisitions. We are starting to see these activities with International Business Machines Corp. (:IBM) buying Red Hat Inc. (:RHT) for $34 billion and Broadcom Inc. (:AVGO) buying CA Technologies (:CA) for $18.9 billion (to name a few).

So, with all of the fear about China trade, the news has been having a field day with misinformation, or withholding important truths. One should recognize that – at the end of the day – network news channels are in place to sell advertising, and their profitability is best accomplished by increasing ratings and viewership; the news is an infinite source of negativity and is at the cross-section of fear and greed. These outlets prey upon several irrational cognitive biases including the confirmation bias, brand loyalty, the availability heuristic, the argument from authority, and the argument from ignorance. We will delineate the confirmation bias and availability heuristic. Highlighting McRaney's writings *Confirmation Bias, MISCONCEPTION: Your opinions are the result of years of rational, objective analysis. TRUTH: Your opinions are the result of years of paying attention to information that confirmed* *what you believed, while ignoring information that challenged your preconceived notions.* To demonstrate this, if you watch FOX News, try watching MSNBC for a few days and vice versa. The information that you have an affinity for will probably "speak your language" while the opposite will be the Bizarro World; Reggie's Vs. Monk's. In the availability heuristic, McRaney describes: *MISCONCEPTION: With the advent of mass media, you understand how the world works based on statistics and facts culled from many examples. TRUTH: You are far more likely to believe something is commonplace if you can find just one example of it, and you are far less likely to believe in something you've never seen or heard of before.* This leads us to the narrative of the trade negotiations between the United States and China…

For months, there has been a palpable fear of what will happen if the trade talks become full blown wars that drag out for years and create massive disruptions to global trade. Using any of those key terms in a search engine will yield thousands of articles and opinions on *what-ifs*, but buried under the radar are the actual releases from government officials from both sides; the US side has positioned the talk in the ultimatum game. The United States' most recent prominent economic indicator (Gross Domestic Product, GDP) published 4.2% growth in Q2 2018, while China has announced a year-over-year decline – most recently at 6.5%. See *Chart 4* for the declining GDP growth of China. We believe China is feeling the grip of "man-hands," but will not kowtow. "Behind the scenes," but openly reported by the Finance Minister of China, the country is net cutting – CUTTING – import tariffs. Many textiles have been a focus of the US Administration, such as metals, and effective November 1st The People's Republic has lowered the import tariff from 11.5 to 8.4 percent. On the same day, the Chinese Finance Minister's Office announced a tariff cut on over 1,500 goods. This is for all countries on China's "most favored country status" – the US included. The overall tariff level in China will go from a net 9.8% in 2017 to 7.5% on imported goods in calendar year 2018. This data has been compiled directly from The State Council of The People's Republic of China (www.mof.gov.cn) or (English.gov.cn). Premier Li Keqiang has stated that China wants to "promote international economic cooperation and free trade, and render stability to the process of world economic recovery and the global financial market." Although China's production growth is slowing, the service sector is ramping up – now sitting as the world's largest importer of e-commerce goods; there is a great need to negotiate trade deals.

Chart 4 (Source: www.stats.gov.cn)

Much like in 2015, corporations have been using headline "buzz words" to tame future earnings expectations. These muffled forecasts were used to build what was a 12.25% return (with dividends) in 2016. As of the composition of this note, 90% of S&P 500 companies have reported Q3 earnings. According to FactSet research, 78% of these companies have beat earnings expectations and have an expected earnings growth of 25.2%. Jeff Cox (CNBC Finance Editor) points out that 138 of the S&P 500 companies have used the word "tariff" in their earnings; this is down from 157 in Q2 2018.

Presently, both Administrations have provided rhetoric that both sides are coming to amicable negotiations. It appears both camps are ready to T.C.O.B., but each faction wants to show it was *their* own initiative. We expect the upcoming G20 meeting on November 20th to be the time to watch for some resolve. On November 2nd, the Chinese Finance Ministry admitted that "without trade negotiations, their country may run into a deficit." The trade negotiations fall into the interesting bias of the "ultimatum game." *MISCONCEPTION: You choose to accept or refuse an offer based on logic. TRUTH: When it comes to making a deal, you base your decision on your status* – McRaney. The US is at a point in history where it can negotiate from a position of power. Sure, there may be some flies in the ointment of the US economy, but it is better positioned than almost any other nation – having the best bathroom in Midtown Manhattan (even better than Brand/Leland).

However, on the contrary, we can see how the lowering of the Chinese import taxes can be viewed as a negative. Although they have lowered the tariff rates on over 1500 goods, this is for specific goods that can be brought in from other nations, and possibly goods that exclude the United States. For example: the lowering of silica imports may benefit nations with larger silica deposits (opposed to the United States' larger exports). This contending consideration is something that we at SWMG will continue to monitor. It is our suspicion that better trade deals will be negotiated in the shorter-term (within the next 2 years), but the longer-term is yet to be determined; earlier this year President Xi Jinping was elected as the permanent leader of China – leaving him time to play "the long game." This *game theory* will certainly be interesting to watch over the coming years to see which side gets the better deal (Feldman or Kramer).

Image (Source: www.whitehouse.org)

We hope you enjoyed this note and we welcome any and all conversations. Please feel free to distribute our *SOUND Notes* to friends and family.

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^ McRaney, David (2012). *You are not so smart: why you have too many friends on Facebook, why your memory is mostly fiction, and 46 other ways you're deluding yourself.* New York, NY: Gotham Books/Penguin Group (USA) Inc.

[5] As of publication date, SWMG owns Apple Inc. (:AAPL) in the SWMG Rhapsody/All Authority and Ensemble Portfolios.

‡Satirical references from *Bizarro Jerry*; October 1996

The S&P 500 is an unmanaged index of 500 widely held stocks that are generally considered representative of the US stock market. Inclusion of this index is for illustrative purposes only. Keep in mind that individuals cannot invest directly in any index, and index performance does not include cost or other fees, which will affect actual investment performance. Individual results will vary.

The Consumer Price Index (CPI) is a measure of the average change in consumer prices over time of goods and services purchased by households; it is determined monthly by the US Bureau of Labor Statistics.

Gross Domestic Product (GDP) is the annual market value of all goods and services produced domestically by the respective country. Raymond James is not affiliated and does not endorse the opinions or services of the independent individuals or organizations mentioned.