KWB Wealth

2018

2ND QUARTER NEWSLETTER

KEY TAKEAWAYS

- In Q1, the quickest 10% selloff from all-time highs occurred, but our clients remained steadfast.
- Large losses can be devastating, but missing out on large gains can be just as distressing for portfolios.
- Risk management doesn't have to be a binary, all-or-nothing decision. Making a call like that requires you to be right twice - getting out AND getting back in.
- Our outlook has not changed. We do not foresee a recession and barring a recession the markets tendency is to rise.

Risk Management Goes Both Ways

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Starting January 26th, 2018, the U.S. stock market (as measured by the S&P 500) fell over 10%, hitting its low on February 8th. It was the quickest 10% selloff from all-time high's in the history of the stock market. While we fielded a few calls from clients during this two-week span, it was a significantly lighter call volume than we've experienced in past market selloffs. Whether this was due to the swiftness of the selloff or due to our first quarter Newsletter release just prior to the selloff (where our first main point was that we expected a 10% selloff sometime in 2018), we may never know but we wanted to commend you all on your steadfastness.

Surely, some investors were panicking in those hectic few days and this got us thinking about volatility, panic, and risk. There is a well-used chart in the investment industry that shows how much gain is required to recover or breakeven after a loss.

Loss Incurred	Gain Required to Break Even
-20%	25%
-30%	43%
-40%	67%
-50%	100%
-60%	150%
-70%	233%

GRAPH ONE: Source — awealthofcommonsense.com, "Upside Risk Management," December 31, 2017.

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Gain Incurred	Loss Required to Break Even
50%	-33%
100%	-50%
150%	-60%
200%	-67%
250%	-71%
300%	-75%

GRAPH TWO: Source - awealthofcommonsense.com, "Upside Risk Management," December 31, 2017

As you can see, the steeper the loss incurred, the more gain it takes to break even on your investments. The 10% fall that occurred in the first quarter would require an 11% return to break even. However, a 50% loss requires a 100% gain to break even. Charts like this are important – and scary – proof that risk management is necessary in your portfolios. Large losses can be devastating both monetarily and behaviorally. We still hear stories of investors who have been out of the market since 2009 as the losses they sustained caused them to lose complete faith in investing. Generally speaking, some of the people that felt they mitigated their risks by staying out of the market may have missed out on a nearly 400% total return since the market bottomed on March 9th, 2009.

Which brings us to the other side of this coin . . . the side that no one sees. If large losses are being avoided at all costs, you may be missing out on significant gains without the proper "upside" risk planning. Graph 2 shows how much loss would be required to wipe out a large gain.

There have been many "market gurus" calling for stocks to fall significantly since 2009. For instance, let's say someone on financial television said after the market gained over 30% in 2013 that the market was due to crash or correct (trust us, there are plenty of "gurus" that made this exact prediction). Well, the S&P 500 is up over 60% since the end of 2013. It would take a 2008-like fall of 40% just for those predictions to break even and an even greater fall for those people to be proven "right."

All of this is to say that managing risk goes both ways. The media headlines that come across our desks rarely talk about the risks of the market climbing 100%. Inevitably, they talk about the latest "guru" saying that stocks could fall 50% from here – and typically these "gurus" have been making these same calls for years hoping to be right just once. Also, risk management doesn't have to be a binary, all-or-nothing decision. "Sell all of your stocks" is never a prudent decision, as it ignores the costs of being wrong. Always remember, when you make an all-or-nothing decision like that, you'll have to be right twice – getting out AND getting back in.

That's why we believe that our Advance & Defend (A&D) 2.0 models are suitable strategy options to approach this risk management problem. The A&D 2.0 models allow us to customize your portfolio to match your specific risk tolerance and to help mitigate risks on both the downside and the upside. Also, we know a great strategy that you can't stick with is a useless strategy. So, as your goals or behaviors change over the years we'll be able to adjust into models that fit your needs over time.

Ultimately, our market outlook has not changed. We believe that the recent volatility is completely normal, and we expected a return to a more typically volatile market environment this year as opposed to the stability we experienced in 2017. We do not see a recession occurring for the remainder of the year and barring a recession the markets tendency is to rise. If our market outlook changes, our Advance & Defend 2.0 models will respond accordingly.

At KWB, we're managing all these aspects of your financial journey. No one can manage downside risk and upside risk independently, they must be looked at together to help you pursue your goals. Our goal is to help you take care of these complexities on your road to Living Well. Our promise is to continue to innovate and enhance our value to you by constantly improving the future.

Thank you for your continued trust in KWB Wealth Managers Group. If you'd like to receive the KWB Quarterly Newsletter via email, please contact our Marketing Director, Elise Campbell, at our office - (800)478-8934 - or email us at invest@kwbwealthmanagers.com. And as always, please reach out to us if you have any questions.

The opinions voiced in this material are for general information only and are not intended to provide specific advice or recommendations for any individual. To determine which investment(s) may be appropriate for you, consult your financial advisor prior to investing. All performance referenced is historical and is no guarantee of future results. All indices are unmanaged and cannot be invested into directly.

The Standard & Poor's 500 Index is a capitalization weighted index of 500 stocks designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries.

Investing involves risk including loss of principal.

No strategy assures success or protects against loss. The economic forecasts set forth in this newsletter may not develop as predicted and there can be no guarantee that strategies promoted will be successful.

How the Tax Cut & Jobs Act Could Impact:
Your Taxes • Your Investments

Join us at one of the following locations:

Tuesday, May 1st

KWB Redlands Office • 1782 Orange Tree Lane • Redlands, CA 92374

12:00 PM: Heavy H'orderves Served • 12:30 PM: Presentation Begins

6:00 PM: Heavy H'orderves Served • 6:30 PM: Presentation Begins

Wednesday, May 2nd

Monrovia Public Library - Community Room

321 S. Myrtle Ave., Monrovia, CA 91016

12:00 PM: Heavy H'orderves Served • 12:30 PM: Presentation Begins

6:00 PM: Heavy H'orderves Served • 6:30 PM: Presentation Begins

This information is not intended to be a substitute for specific individualized tax advice. We suggest that you discuss your tax issues with a qualified tax advisor.

- Learn how the new tax brackets may impact your take-home pay
- Should the tax reform affect the way you invest?
- How might the tax reform affect businesses/markets?
- Stay informed with a current economic update.

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Please forward this information to friends and co-workers that will benefit from attending.