FINANCIAL SYNERGIES®
ASSET MANAGEMENT

Q1 2017

INSIDE THIS ISSUE

Two Brains Are Not Better Than One

MIKE BOOKER, CFP®, CHFC®, CFS®

SHAREHOLDER, FINANCIAL ADVISOR

I recently attended an investment seminar hosted by Ken Haman, noted behavioral scientist. He has spent many years studying the two sides of the brain and has concluded that, as far as investing acumen is concerned, two brains are not better than one.

One side of the brain, the neo-cortex, is the part that controls speaking and mathematics. It is the rational, analytical part of the brain. It is located behind the forehead, is very deliberate and capable of contemplating future

...Continued on next page

consequences of actions taken. As Mr. Haman says, "a person uses their neo-cortex when they decide to start a new diet."

A large cluster of more primitive structures sits below and behind the neo-cortex. This primitive brain controls the fight-or-flight response to threats. It operates instinctively, and generates strong emotions when presented with an imminent threat. Haman is quick to point out, "This is the part of the brain that sees a delicious piece of cake and quickly grabs a fork, ignoring the plans for the new diet."

Thousands of years ago, human survival was moment-by-moment with the environment full of dangerous animals or situations that could harm or even kill. A person either reacted correctly and survived or reacted incorrectly and perished. Early humans also faced challenges that required longer-term planning – like where was the next meal coming from. Careful thinking and planning was the key to survival.

Today, our survival instinct is still alive and well and it completely overwhelms the rational brain in response to a threat. Mr. Haman states, "The human brain has not changed in any meaningful way over the last 50,000 years – we still have the same hair trigger fight-or-flight mechanism. However, today's threats are different and our bears show up in our portfolio rather than our cave."

Applying this concept to investors, it is the neo-cortex alone that makes thoughtful, deliberate investment decisions involving the balance of risk and reward and considers probabilities of success or failure (all very scientific and lucid). But, as we all know, there are times when markets trend downward, and when this happens, "The directionality of the markets seems to profoundly affect investor's future security and even their immediate well-being. Once investors feel threatened, the fight-or-flight instinct takes over. This fast-thinking, instinctual part of the brain takes charge and is eager to act. To do something," says Haman.

In my experience as an investment advisor, telling a client to think "long-term" during times that their emotional side of the brain is in charge is largely ineffective. Haman agrees, "Such advice is like telling a person who is terrified of snakes not to worry about the snake in front of him because it is harmless. Fear always overwhelms logic; non-logical reactions are built into the human central nervous system."

What are investors to do? More importantly for us, how can we best serve you, our clients, when the volatility of markets has initiated the fight-or-flight response? While there is no obvious answer, I think the solution may lie in preparation. While I hate getting shots from the doctor, I appreciate the iconic warning just prior, "You are going to feel a little prick." This helps me prepare for what's coming. It doesn't mean I enjoy it, but I am ready. Competitive golf teaches me that disaster lurks around every corner and that I should expect bad bounces and lipped out putts from time to time – they are such an inherent part of the game. I know they are coming, I just don't know when.

Down markets are inherent to investing, too. We know they are coming, we just don't know when. In the last 90 years, markets have posted year-end losses 24 times, with just 11 of those losses greater than 10%. So, let's prepare ahead of time. Close your eyes, take a deep breath and imagine for a moment that the Dow Jones just dropped 1,000 points. A little scary, right? Good! Even though that's less than a 5% loss, that scare could trigger your fight-or-flight response. This natural, emotional reaction might get triggered for real when the Dow really does shed those 1,000 points (or more) at some point in the future.

When that panic sets in, the emotional side of your brain will want you to do something. That's fine, but I want that something to be this: Call us. Maybe my fight-or-flight response may be trying to surface, too, so let's talk each other through it. Remember, our firm is monitoring the markets, we know your goals, your objectives and, most importantly, we know you. And you know us. Together, I bet we can stop the emotional side of our brains from bullying the rational side into making an impulsive decision that we end up regretting. You are not alone.

Welcome Susie and Kevin!

We would like to welcome our newest team members, Susie Miller and Kevin Nelson.

Susie joined our team back in December as receptionist, coming to us with many years of administrative experience. She'll be the one greeting you at the door when you come to the office or calling you to schedule meetings. Susie lives in Cypress and enjoys spending time with her children and grandchildren.

Kevin joined our team in March as Financial Advisor, with 11 years of advisor experience. He will be assisting the advisory team with client meetings, on-boarding, and financial planning. Kevin lives in Meyerland with his wife Georgia and two children, Abigail and Elizabeth.

Going Global is Essential

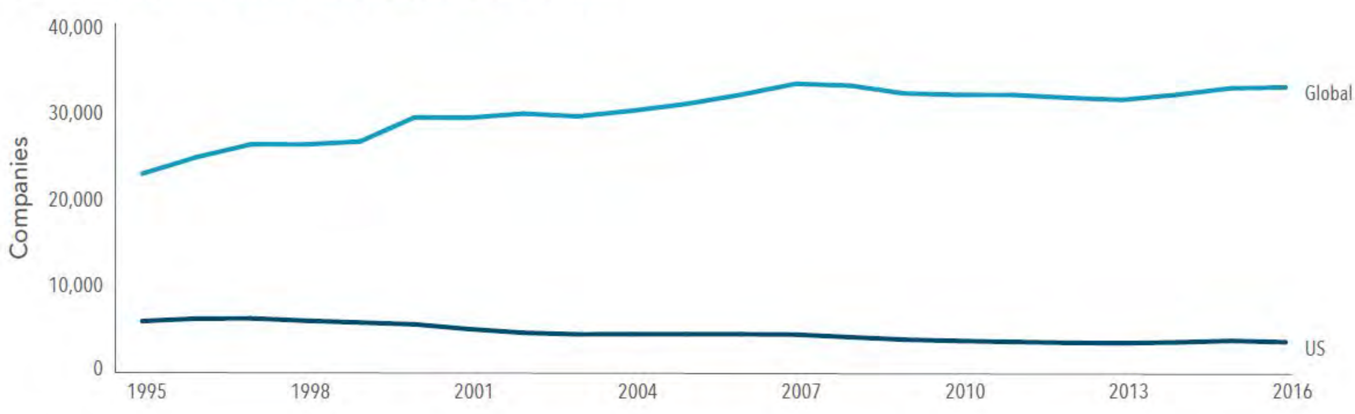
MIKE MINTER, CFP®, CFS® | SHAREHOLDER, PORTFOLIO MANAGER

In the past two decades, there has been a decline in the number of US-listed, publicly traded companies. A case in point: How many stocks make up the Wilshire 5000 Total Market Index? While the logical guess might be 5,000, as of December 31, 2016, the index contained just 3,600 names. In fact, the last time this index contained 5,000 or more companies was at the end of 2005.

Should investors be worried about this change? Does this mean there is a risk of being unable to achieve an adequate level of diversification in your portfolio? I believe the answer to both is no. When viewed through a global lens, a different story begins to emerge – one with important implications for how to structure a well-diversified investment portfolio.

When looked at globally, the number of publicly listed companies has not declined. In fact, the number of firms listed on US, non-US developed, and emerging markets exchanges has increased from about 23,000 in 1995 to 33,000 at the end of 2016.

Exhibit 1: Number of Publicly Listed Companies



Source: Bloomberg.

Source: Bloomberg.

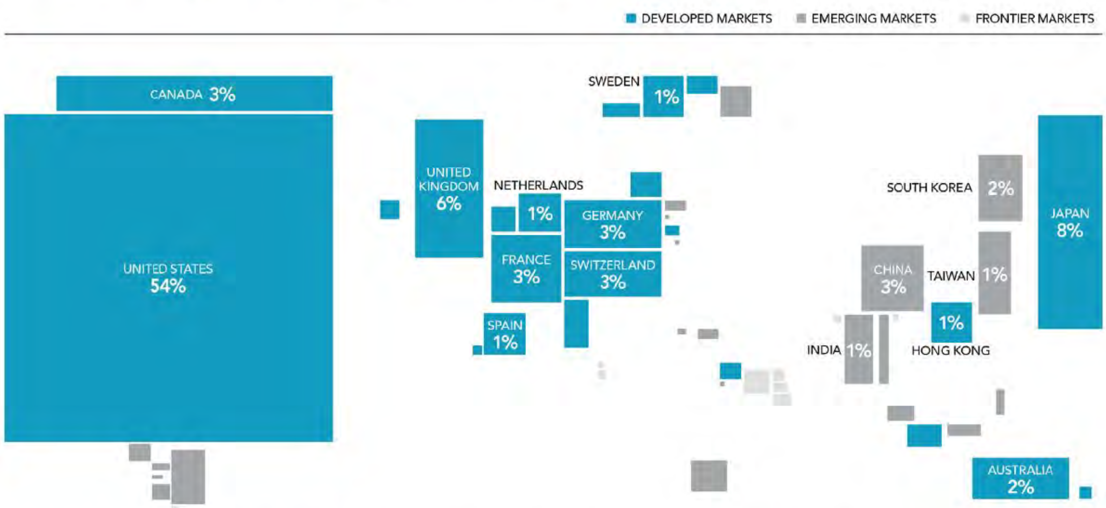
...Continued on next page

While it is true that in the US there are fewer publicly listed firms today than there were in the mid-1990s, it's clear that the increase in listings both in developed markets outside the US and in emerging markets has more than offset the decline in US listings.

A GLOBAL APPROACH

In the US, with thousands of stocks available for investment today, it is unlikely that this change will meaningfully impact an investor's ability to efficiently pursue equity market returns in broadly diversified portfolios. It is also important to note that a significant portion of the publicly available global market cap remains listed on US exchanges.

Exhibit 2: Percent of World Market Capitalizations as of December 31, 2016



Data provided by Bloomberg. Market cap data is free-float adjusted and meets minimum liquidity and listing requirements. Many nations not displayed. Totals may not equal 100% due to rounding. China market capitalization excludes A-shares, which are generally only available to mainland China investors.

Source: Bloomberg.

As noted in Exhibit 2, the weight of the US in the global market is approximately 50–55%. For comparison, it was approximately 40% in 1995.

The global equity market is large and represents a world of investment opportunities, nearly half of which are outside of the US. While diversifying globally implies an investor's portfolio is unlikely to be the best performing relative to any one domestic stock market, it also means it is unlikely to be the worst performing.

Diversification provides the means to achieve a more consistent outcome and can help reduce the risks associated with over-concentration in any one country. By having a truly global investment approach, investors can capture returns wherever they occur.

CONCLUSION

While there has been a decline in the number of US-listed, publicly traded companies, this decline has been more than offset by an increase in listings in non-US markets. The implications for investors today are clear – to build a well-diversified portfolio, an investor must look beyond any single country's stock market and take a global approach.

Sources: Bloomberg, Dimensional Fund Advisors.

A Cross-Atlantic Voyage

WILL GOODSON, CFP® | FINANCIAL ADVISOR

I want to share a recent story about one of our Pathway clients that can only be described as *amazing*.

Michael Matson and his wife, Sami, became clients under our Pathway program last summer. In our first meeting, Michael mentioned that he had a "unique" hobby – ocean rowing.

My first thought was, "OK, this guy likes kayaking off the surf in Galveston." It turns out, Michael was one of the instructors for the Rice University rowing team. Not only that, he and two friends had entered the Talisker Whisky Challenge, a 3,000-mile rowboat race across the Atlantic Ocean.

Yes, *that* Atlantic Ocean!

Michael and his crew arrive in Antigua at the end of the journey.

Michael embarked on the voyage in mid-December 2016. The race started in the Canary Islands off the western coast of Africa. Their destination was Antigua, over 3,000 miles away.

Michael decided to name their vessel "Anne" after Anne McCormick Sullivan, a deceased Houston firefighter. Michael and Anne were friends and served as volunteers with the Stafford, TX Fire Department. After joining the Houston Fire Department, Anne tragically lost her life in a massive hotel fire in southwest Houston in May 2013. Michael and his crew felt naming their boat Anne was a great way to honor his friend and local hero.

During their trans-Atlantic crossing, they encountered storms, whales twice the size of their boat, and even a 700-pound sea turtle. After 49 days, 14 hours, 4 minutes, and 20 seconds at sea, Michael and his crew touched down on the shores of Antigua. They were the first crew from Texas to complete the Talisker Whisky Challenge. They also set two Guinness Book of World Records as the only 3-man boat crew to row across the Atlantic and to do it in the fastest time.

Michael and Sami shared the experience with me after he returned to Houston. He lost over 30 pounds along the way and came back with a beard fit for the movie *Cast Away*. It is an unbelievable story and an experience Michael will never forget. When asked about his future rowing excursions, Michael said he plans to stick to smaller rivers and lakes for the time being. No more oceans, for now.

Be Prepared

BRYAN ZSCHIESCHE, CFP®, MS, MBA

SHAREHOLDER, FINANCIAL ADVISOR

This year, I've had the pleasure of introducing my eldest son to Cub Scouting. He and ten other 7-year-old boys make up our Tiger Den, and as their Den leader, I'm always on my toes. I'm also constantly reminded of lessons I learned during my own Scouting experience.

When I was 10 or 11, my dad and I decided at the last minute to attend a regional Scouting Jamboree. Because it was a mild East Texas fall, I headed out of the house in my uniform and a light jacket. About an hour after we arrived at the campsite, a cold front blew through bringing strong winds and a near-freezing rain.

My uniform and light jacket were woefully incapable of shielding me from the cold and rain. Our only saving graces were the heater in our Ford station wagon and the hand dryer in the campsite's small bathroom facility. I don't think either one of us has been as cold before or since that night. And thus, I learned the lesson of the Scout motto: "Be Prepared!"

Robert Baden-Powell, the founder of Scouting, said this of the Scout motto: "The meaning of the motto is that a Scout must prepare himself by previous thinking out and practicing how to act on any accident or emergency so that he is never taken by surprise." (emphasis added)

How can this lesson learned in Scouting help us as we turn to investing?

To start, let's look at the current market environment. We are experiencing a bull market that started at end of the financial collapse in '08 – '09. However, along the way this run-up has been interrupted by a number of market pullbacks as you can see in the graph below.[1]

It is easy to forget how frequently these declines have occurred and just how nasty some of them were: -16.0% in 2010, -19.4% in 2011, -12.4% in 2015, and -13.3% just last year, to name a few.

The past year has been terrific for the broad stock market, with only minor downturns since early 2016. But if history is any guide, it is only reasonable to expect a decline to occur sometime in the future.

...Continued on next page

So how should you "be prepared" to deal with market pullbacks when they occur?

1. **Remember that market declines cannot be timed.** Don't abandon a thoughtful investment plan in an attempt to time a peak.

2. **Remember that markets go up and markets go down.** Everyone knows this, but we all seem to be surprised when downturns occur. As Mike Booker advised in his opening article, prepare yourself for those downturns emotionally, and acknowledge that they are a normal part of investing.

3. **Remember that market downturns are temporary.** Even if a decline is prolonged, it isn't permanent.

4. **Remember that market downturns create opportunities for long-term investors.** Through additional investments and careful rebalancing, investors can exploit downturns by purchasing additional stock shares at lower prices.

5. **Remember to stay focused on your long-term game plan.** Since we know that markets experience declines, we build our portfolios using a diversified mix of investments. Some of those investments, such as bonds, have a good chance to make money when stocks decline.

6. **Remember to avoid the noise.** As Carl Richards put it, "Building long-term wealth is probably inversely related to knowing what the market did today."

Jason Zweig, editorial writer for the Wall Street Journal, said this in a speech given in 2001: "The only universal truth that the past offers about the markets is that they will surprise us in the future. And the corollary to that law is that the markets will most brutally surprise those who are most certain what the future holds."[2]

We have no idea what direction the markets will take over the next weeks, months or quarters. The most dangerous investment approach is one that presumes to know such things. But we can follow the Scout motto and be prepared emotionally so that when the market experiences its inevitable pullbacks, we aren't taken by surprise.

[1] Source: JPMorgan Guide to the Markets. March 31, 2017. p. 14
[2] Source: http://jasonzweig.com/fat-tails-thin-ice-2/

When Should You Invest?

HEATH HIGHTOWER, CFP® | SHAREHOLDER, FINANCIAL ADVISOR

The decision of "when" to invest in the market can be overwhelming. After all, it's hard to invest in the market when it's going down, and it's equally as hard to invest in the market when it's at an all-time high like it is today. Some investors rely on their own ability to outguess the market, but for many others, the fear of entering the market can be paralyzing. Unfortunately, doing nothing can be the worst decision of all.

Last month I met with a potential client who was struggling with this very decision. He's hesitant to invest his money because the market has been up and he feels that it will inevitably come back down. His account has been in cash for over 15 months, and he's missed out on the entire 2016/2017 bull market.

We decided to meet in a Charles Schwab branch near his home, and while I waited in the lobby I stumbled across this chart, which was very helpful in our conversation.

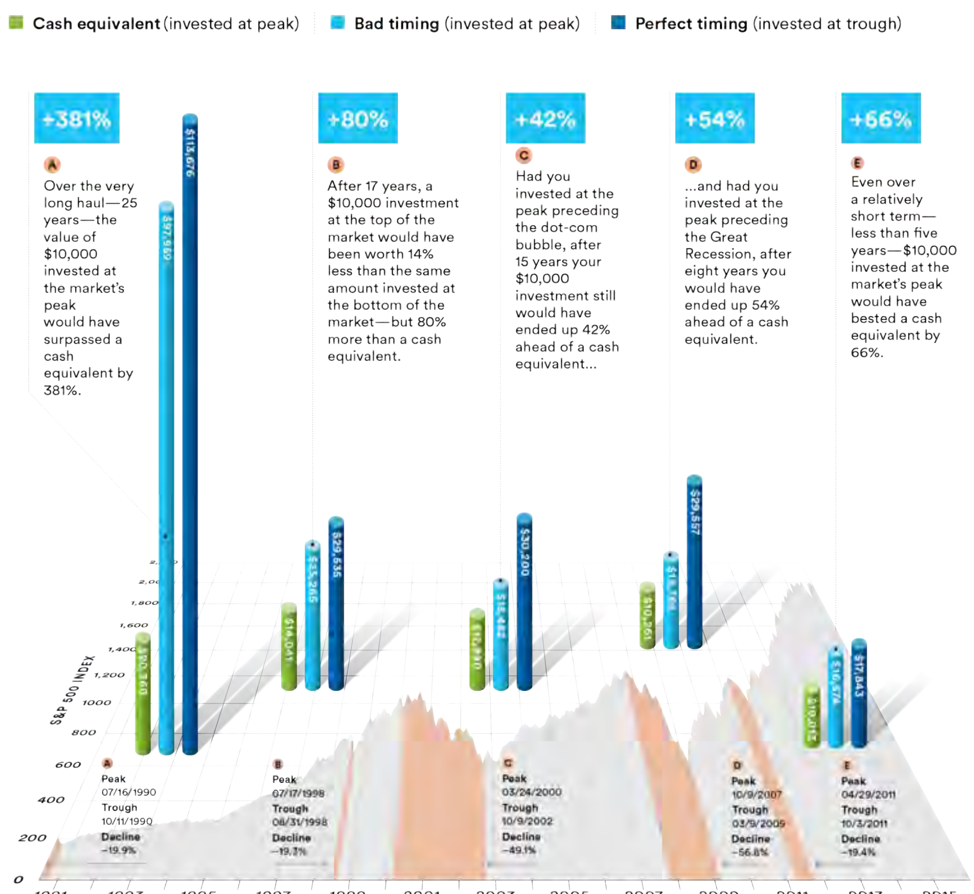
The chart is a little complex, but its message is simple: Whether you invest at the top or the bottom, in the long run getting into the market has historically beaten sitting on the sidelines. The chart compares how $10,000 invested in the S&P 500 would have grown if invested at five market peaks (bad timing) and five market troughs (perfect timing) vs. a cash equivalent through the year 2015.

As you may have expected, the portfolio that did the best was the one that was invested at the exact "perfect time". But it may surprise you to know that the portfolio that was invested at market peaks (bad timing) performed much better (381% better) than the cash equivalent. I also find it particularly interesting that the "bad timing" portfolio didn't do much worse than the "perfect timing" portfolio over the long-term.

As the old saying goes, it's about time in the market, not *timing* the market. If you're struggling to decide when to put your money into the market, consider whether the money is intended for a short-term purpose versus a longer-term purpose. Cash that is intended to be used or spent over the next 1-2 years should never be invested in the stock market. But if you have more time to let the money grow, the time to invest is right now.

Is There Ever a "Bad" Time to Invest?

Whether you invest at the top or the bottom, in the long run getting into the market has historically beaten sitting on the sidelines. Here's how $10,000 invested in the S&P 500® Index at five market peaks (a.k.a. "bad" timing) and five market troughs (a.k.a. "perfect" timing)—and held through year-end 2015—performed against the same amount held in a cash equivalent.



Source: http://www.schwab.com/insights/stocks/is-there-ever-bad-time-to-invest