Quarterly Booklet

JANUARY 2018

"It's not what you look at that matters,
it's what you see."

-Henry David Thoreau

ONE DAY
IN JULY

A Note from our Founder

During a basketball game in 8th grade, I drove to the hoop, with no resistance from the other team. My confidence soared as I netted two points, and crashed when I realized I had scored on the wrong basket.

2017, as an investment year, was that. It was a layup with no opponents - smooth and easy. The total return of every index we used was positive over the calendar year. For the second year in a row.

It's not common, and it won't keep happening. As the media hype engine cranks up in 2018, keep your expectations reasonable. Investments do not travel upward in a linear fashion, it's simply not how markets work.

With that gleeful thought, let's begin.

Dan Cunningham

What is a dividend?

A dividend is a payment made to the owner of a share of a business. Dividends are generally cash payments. In large index funds they are generally paid at the end of each quarter, though sometimes they pay once a year in December.

Dividends are a critical part of investment returns. In 2007, John Bogle, the founder of Vanguard, pointed out that over the past 81 years, dividends were responsible for 95 percent of the compounded long-term return earned by companies in the S&P 500.

Not all index fund dividends are taxed in the same manner, or at the same rate. Optimizing tax efficiency can add significant sums to overall returns.

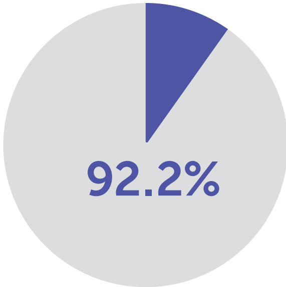
Source: Bogle Financial Markets Research Center, October 15, 2007

> "Borrowing money is like wetting your bed in the middle of the night. At first all you feel is warmth and release. But very, very quickly comes the awful, **cold discomfort of reality.**"

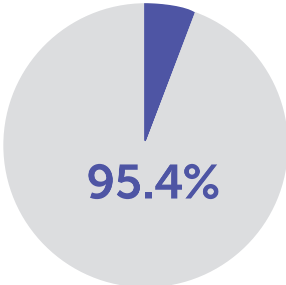
Warren Buffett, on America's debt culture

Whoops.

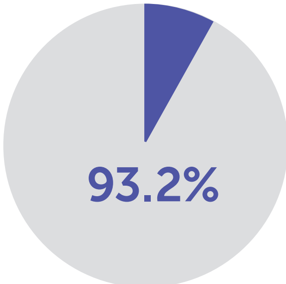
Over the past 15 years, this is the percentage of actively managed mutual funds that **did NOT beat their respective index:**



BIG COMPANY FUNDS



MID-SIZED COMPANY FUNDS



SMALL COMPANY FUNDS

Source: SPIVA U.S. Scorecard Year-End 2016

Stocks vs houses?
It's not even close...

A study from Credit Suisse Global and the London School of Economics determined that real housing returns in the United States, from 1900-2011 were 0.09% per year. Real return is the return in inflation-adjusted dollars.

What was the real return of equities over the same time period? 5.4%, or 6 times as much **per year**.

In addition, housing is illiquid, which means its real value should be discounted further. We can sell out of an index fund in a matter of seconds. Try doing that with a house.

But people perceive they are making more money in housing partly because they are using leverage, or debt, to increase their equity returns.

Housing is best thought of as a consumption item.

Statistics Source: London Business School, Credit Suisse Global Investment Returns Yearbook 2012

"When our financial system - essentially **our money managers** - put up zero percent of the capital and assume zero percent of the risk yet **receive fully 80 percent of the return**, something has gone terribly wrong in our financial system."

John Bogle, founder of Vanguard

Of the indexes we invest in for clients, which one performed best over calendar year 2017?

Emerging, markets, with a 31.37% gain. Note how much attention the U.S. markets received this year in the media. Yet massive returns were happening quietly in underdeveloped countries overseas. (30% plus returns in a year are rare.)

Based on Vanguard emerging markets index fund ETF, which owns stakes in 4,655 companies. This stat assumes dividends from emerging markets are reinvested in emerging markets, which is not how the One Day In July overall model always invests.

Source: Morningstar.com, 1/1/17 - 12/31/17

Is the gain in emerging markets good as an investor?

It depends. If you are retired and are drawing money from your savings in excess of dividends that are paid, then yes, it is good. You want your indexes to appreciate as much as possible.

But if you are in the savings phase of life, or if your savings are large enough that you are reinvesting dividends, it's not necessarily good.

Why not? Remember that our objective is to build a business for you that generates cash through dividends. An ideal situation is one in which dividends are rising and prices of stocks, or indexes, are falling. This allows us to buy more shares at a cheaper price for you. In essence we are using cash today to buy future cash flows "on the cheap."

Probabilities, we respect you.

What matters when considering an investment is not just the return, but the probability of obtaining that return. The probability contains the risk.

In quantum physics, there is a very small probability that if you throw a very small ball at a very thin wall, the ball might tunnel through the wall. This would be quite the party trick, and would make you as popular with a group of fifth graders as with adults.

The problem is, the mathematics behind this quantum effect are such that it will only happen once in the lifetime of many billions of universes. While the reward is high, the probability isn't.

Something to keep in mind for investing.

About One Day In July.

Many of you work with Hans Smith at One Day In July. Hans is a pilot, and he's no amateur – he can fly near the speed of sound. More important to me, he's never crashed.

ONE DAY
IN JULY

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