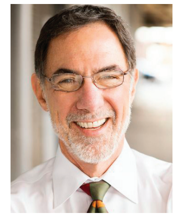
Perspective

October 2015 By Davis Riemer



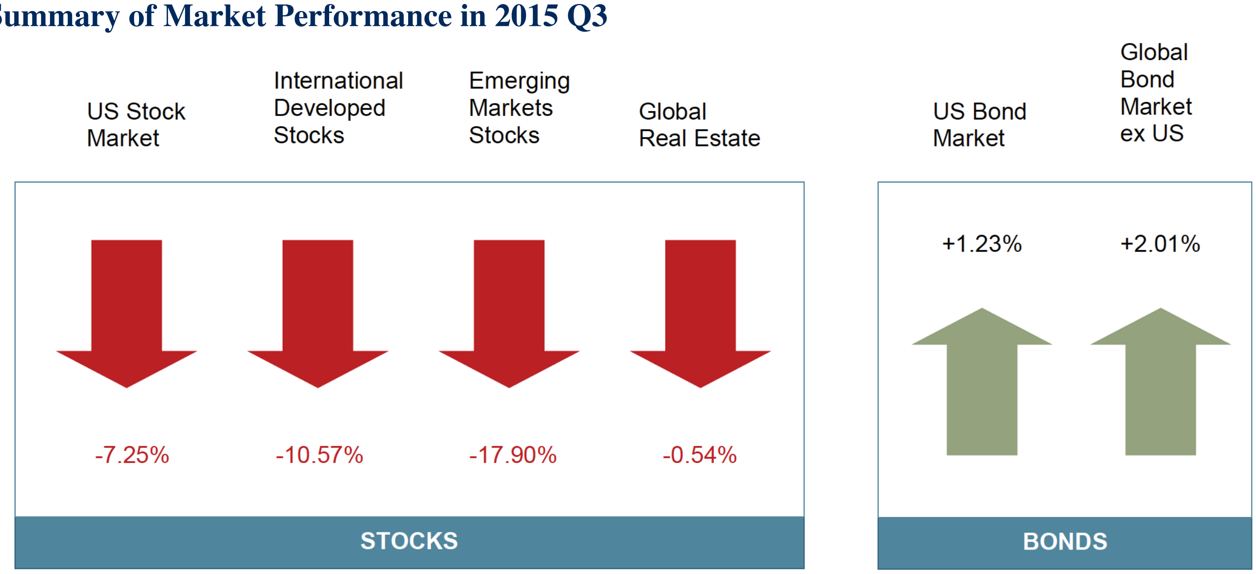
DHR Investment Counsel, Ltd.
The Fine Art of Wealth Management

In this issue, after the "arrows" chart below of broad market performance, we offer our own comments on an article by Gretchen Morgenson of the New York Times, discussing "non-rational" behavior of investors. We believe that view partly explains the performance of value strategies since 2008 – below expectations, but still understandable, given economic circumstances. That leads to our next section, a fuller discussion of the historical performance of value and growth strategies, which also supports "hanging in there" and "staying the course" with value strategies, because they have shown superior results over time. Changes in stock markets, as well as changes in investment style, comprise the focus of the next section, "Bubbles," which features dialog between two Nobel Laureates in Economics. Then, after that, for all of you aged 65 and over, Louise has written about the annual renewal of Medicare coverage this fall, between October 15 and December 7. She offers some interesting information to you, that basically urges you to be careful, especially when dealing with Part D providers. As always, *"Caveat emptor"* is worth keeping in mind. We close with thoughts on work in the "Money Art" collection. Thanks for your attention.

Rational Understandings, Insights and Intuition

The chart below is self-explanatory. It can only please bond investors. Interestingly, with smaller losses, REITs outperformed all the stock categories. In portfolios, we call that "positive contribution to negative performance." (Is joke!)

Summary of Market Performance in 2015 Q3



"Never argue with a fool, onlookers may not be able to tell the difference."
- Mark Twain

Gretchen Morgenson, financial columnist for the New York Times, recently wrote an article for the paper on a pending change in behaviors of stock market investors. The volatility in the last weeks might well mark some of the changes anticipated in her article. I have added to and also paraphrased her text with mine, producing a mixture of the two. (My apologies to Ms. Morgenson.)

Until the recent decline, and no matter the news, investors simply bid share prices up, producing a surge in growth stock performance and a market top. Now, that has changed. As investors absorb the meaning of the volatility, perhaps other less rational market behaviors might prove ephemeral, as well. Does this portend a change in investors' attitudes?

Any attempt to understand the "mind of the market" is a chancy venture, at best. However, when one major investment assumption is proven wrong, for example that the growth of China's economy will continue unabated, then other behaviors might also come to be viewed as suspect. Will companies with no earnings continue to trade at high valuations? Are corporate profits being artificially elevated with share buy-backs or other tactics? Will the Fed (like Mighty Mouse!) always come in "to save the day?"

Francis Gannon, an investment manager at Royce Funds, a highly regarded small cap and value investment firm, noted that, these days, a third of the companies in the Russell 2000 Index do not earn any profits. A majority of the performance of the Russell 2000 came from companies that actually lost money. Gannon said: "The laws of finance have been suspended for some time. Now that is starting to crack. I think we are on the road to normalization." Gannon further commented that, when prices stop rising and turn down, two particular groups of investors might accelerate the decline. One, a perennial group, consists of those who buy stocks on margin, playing on the ever-narrowing ledge of momentum. The other is a product of our time. Because bond and savings yields have been so low, many traditional "savers" have bought stocks simply in order to get a viable yield. Both of these groups lack some of the characteristics of long term equity investors. As a manager whose firm buys quality companies with quality earnings, Mr. Gannon is eager to work in a market where investors behave more rationally.

As a firm that relies on the history and patterns of long term performance of rational markets, DHR hopes the same. Such a change would allow a return to success of value investing principles, the long-left-behind step sister of glamorous growth siblings. Major shifts in market sentiment are unpredictable as to timing, but we can be hopeful.
(End of comments on Morgenson's article.)

That leads to a fuller discussion. With the continued performance of the domestic and international stock markets, reaching back now to 2008, a value investor has had to work to maintain conviction and a positive outlook. When one's strategy lags for as long as 7 years, it can make one wonder. Clifford Asness, one of the very best in our stock market as both writer and manager, says that, by its very nature, a long term strategy will not work successfully unless it causes pain now and then. Well, I have been feeling some pain. When that happens, I return to the research and thinkers. Clients rely on our word, which we appreciate. Nevertheless, even for us and, I suspect, especially for clients, external sources of information can provide support. Some digging turned up the two charts on page 3, each displaying different aspects of the same phenomenon – the long term superior performance of value strategies. We encourage your study, even if brief.

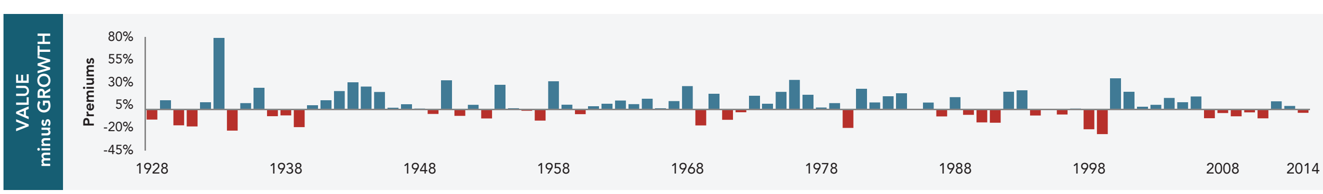
Since investment charts usually involve technical matters, some explanation will help. In their calculation of performance, both charts use the same definition of terms - the “Fama/French U.S Value Index” and the “Fama/French U.S Growth Index.” These are not mutual funds. They have no management and no expenses. Past performance offers no assurance of future performance.

The lower chart displays the historical tendency of value strategies to outperform growth strategies in the domestic stock market over various periods of time. The periods in this chart are “rolling periods.” That means, for example in the 15 year period chart, a new fifteen year period begins each month and runs for the succeeding fifteen years. This does create statistical inter-dependency within each period. How many periods are there? 871 overlapping 15-year periods, 931 overlapping 10-year periods, 991 overlapping 5-year periods and 1,028 overlapping 1-year periods.

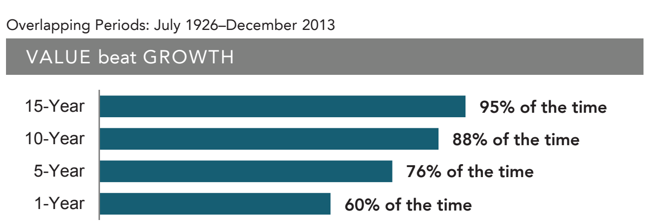
The top chart displays the annual results that led to the accumulated results shown in the lower chart. In this chart, the percentage difference of performance, measured on the scale at the left, displays the result of subtracting the growth performance from the value performance. The “up” bars are positive for value, the “down” bars show periods when growth beat value. A quick count will show that the recent period of under-performance of value is somewhat longer than prior periods. We say: “Not to worry. That is not unexpected in risky circumstances. (Investing).”

You will notice that the longer one waits in the strategy, the higher the probability of long term success becomes. One can draw an analogy to an athletic team sport. One wants to win at the end and, if one does do that, then having had the lead throughout the contest makes little difference – except to the ability to hold on. Of course, unlike team sports, investing has no “final outcome” across markets. Individual investors do need their money, however. This creates a need for time-based planning, liquidity sources and careful assessment of risk. Holding on means patience means faith means sources of belief. Theory, evidence, common sense – those are our sources, and you all know the answer to “What will DHR say?” “Stay the course.”

Historical Performance of Value and Growth Styles, Rolling Multi-Year Periods



Historical Performance of Value and Growth Styles, Annual Periods



A Sixth Sense
Bubbles

"I'm Forever Blowing Bubbles"
Pretty bubbles in the air,
They fly so high, nearly reach the sky,
Then, like my dreams,
They fade and die.
(Jaan Kenbrovin, 1918)

Robert Shiller and Eugene Fama, both Nobel Laureates in Economics, appeared on NPR's "Planet Money," from which this excerpt has been taken. Shiller is probably the most famous analyst of - and Fama the most famous skeptic of - financial bubbles. Shiller predicted the two great bubbles of our time - the tech bubble in the late 90's, crashing in 2000, and the housing bubble in 2007. The following has been arranged for flow.

Shiller: "In the late '90s, I wrote my book 'Irrational Exuberance.' I rushed to get it out, because I wanted it out before the crash, not after. I felt that same way in the 2000s with the housing bubble."

Fama: "I don't think there's anything in the statistical evidence that says anybody can reliably predict bubbles, or when prices will go down. *(Emphasis on reliably)*. So, if you interpret 'bubble' to mean one can predict when prices will go down, it can't be done. So, what happens each time, is that the media goes in and finds somebody who predicted it. Then, that person gets anointed."

Moderator: "So, was Shiller one of those people who were anointed by the media?"

Fama: "Oh, yes."

Moderator: "What would prove to you that bubbles are predictable?"

Fama: "Empirical evidence that would show me that one can predict in some reliable way when these things will turn."

Moderator: "So what is your challenge to Robert Shiller? He should predict the next bubble?"

Fama: "Well, not just the next one. You know, 'statistically reliable' means more than two, really."

Moderator: "The next ten?"

Fama: "Well, the next ten would be really convincing. Yeah. Then I'd be convinced."

Moderator: "Professor Shiller, Fama says he would believe there are bubbles and predictability if you could predict ten of them in a row."

Shiller: "But I won't live that long! You know, these big bubbles are rare events that play out over years."

Moderator: "If you lived long enough, do you think you could make good on Gene Fama's request that you predict ten bubbles in a row?"

Shiller: "If I lived long enough - yeah."

***DHR:** So, when deciding whom to believe, as the carnival barker says - "You pays your money and you takes your chances!"*

DHR's clients and readers of our *Perspective* know that we join the side of statistical reliability. We try to be circumspect about claiming it as "the absolute truth," but nevertheless, we believe that no-one "knows" the future – it is uncertain. Many people make predictions – inevitably some will be proven correct. That historical fact offers no reliably predictive information about the future. We endorse statistical reliability as the basis on which to found investment planning and strategy.

"The public cannot be too curious concerning the characters of public men."
- Samuel Adams

Getting On About Getting On

By Louise Rothman-Riemer

"Being Mortal" by Atul Gawande is a New York Times best-seller published in 2014. In this book, which is available at Diesel A Book Store (the store is just below DHR Investment Counsel), Gawande clearly and comprehensively discusses the topic of medicine and what matters at the end of our lives. Aging, medicine, Long-Term Care and end of life choices are increasingly found in current articles in newspapers, periodicals and on the web.

Issues associated with elder care are often important and at times urgent topics for clients of investment advisory firms. Advisors are frequently asked about how best to deal with an aging parent or other relative. And of course, many older clients are concerned about choices for themselves.

Gawande, along with other authors on the subject of aging, stress the importance of and invaluable help that can be gained by going to a gerontologist. Gerontology is the official title given to the medical specialty relating to the elderly. While an increasingly significant specialty, it is one that doesn't pay as well as others. Therefore we are facing a substantial shortage of gerontologists just when our geriatric population is increasing geometrically.

In today's culture and society we often focus so much on youth and being youthful that we momentarily convince ourselves that we can put off thinking about old age and its needs to sometime in the future, usually a lot later in the future. But time marches on and birthdays mark our advancing years whether we like it or not.

Historically, as a country, we began more assertively addressing the needs of our elderly population in the 1930's when Franklin D. Roosevelt's administration established our Social Security system. The Depression had stripped most families of their financial security and it was especially an issue for older Americans. The test of time has proven the worth of Social Security in helping provide financial independence and security for a very large segment of our population.

As a nation we took the further step of providing medical support and security of our oldest population fifty years ago when President Lyndon B. Johnson signed the Medicare Program into law. For the last five decades Medicare has been providing health care and improving the medical experiences of millions of older Americans. "Medicare" has taken a great financial burden off of families as they care for and assist their aging family members who now are living longer than ever.

Which brings us to this moment, as now is the time when Medicare recipients can make changes in their plans. **Between October 15th and December 7th is the Medicare Annual Enrollment Period (AEP).** If you are a Medicare recipient it is important that you act now to make any changes you deem appropriate or necessary to your Medicare elections for 2016. **If you miss the Dec. 7th deadline you are locked in to your current program for another year.**

Surprisingly, as reported in Investment News, a financial industry publication, **90% – 95% of recipients pay too much for their Medicare Coverage.** Why does this happen? It happens

> *"Every gun that is made, every warship launched, every rocket fired signifies, in the final sense, a theft from those who hunger and are not fed, those who are cold and are not clothed."*
> - Dwight Eisenhower

because people do not make sure to match their current needs to the coverage they purchase. This is particularly true of the Medicare Part C (Advantage) and Part D (prescription drug) plans. It is important to review your plan to insure that the drugs on your plan's formulary include reasonable prices for the drugs that you actually take. There are often differences in plan and drug prices from one year to the next. In the Fall all plans announce new pricing and benefits.

If you are a Medicare recipient you have undoubtedly received a letter from your carrier telling you that you should review your coverage to make sure it continues to meet your needs. Unfortunately it is easy to make the assumption that little has changed and that you would not benefit from switching carriers. This may not be the case.

You should particularly consider your options if you have had a major medical issue or if your prescriptions have changed in the past year. If you have moved in the past year that can also have an impact on the pricing of your plan, and yes, some areas of the country are more expensive than others.

It is advisable to look at all aspects of your plan, not just the premium. Does your plan have an acceptable co-pay, deductible levels, and if appropriate, co-insurance? You should also double-check to make sure your doctor, an easily-accessible hospital and other related services are still covered by your plan at a reasonable price.

If you have questions or are uncertain about any aspect of your plan there are services available to help you. Online services can be helpful; go to **Medicare.gov** for a better understanding of plans available in your area, medication coverage specifics, and specific network providers. You can also call Medicare 24/7 at 800-633-4227.

Shiptacenter.org is the State Health Insurance Assistance Programs site that directs consumers to free Medicare counseling and assistance. Furthermore, every county in the country has Medicare consultation and education services available. You can check out public services offered by the U.S. Administration on Aging at **Eldercare.gov**. You can also call for assistance at 800-677-1116 Monday-Friday 9am – 8pm.

We are, indeed, all mortal and as with the stock market, we cannot know the future or necessarily correctly predict how our lives will play out. But we can be informed and Gawande's book is an easy introduction to the subject of aging and what we will all face to one degree or another.

In closing we remind you that the time to act on Medicare Coverage is now. You do not want to miss the deadline and be locked into a plan that is not best for you for 2016. We strongly advise you to plan ahead, take the time to really review your options and plans, especially your options for Parts C and D, and if appropriate, don't hesitate to change.

"Brother, Can You Spare a Dime?"

In 2009, in a Wisconsin art gallery, I saw a fascinating hand-made ring. The ring's precise detail marks an obsessive maker - just the kind I like so much.

It attracted my attention because the constructed top rises an inch above the band and features a four-sided pyramidal shape, with each of its four sides covered with a cut-out of the pyramid that appears on a one dollar bill. The artist, Tim O'Neill, was there and, in conversation, I learned that he intended to make a series of five rings, to be called *"The Financial Crisis Rings."* From his perspective on economic events in 2008 and 2009, he had found rich subject matter for his work. So, we commissioned the entire five rings, which are: *Pyramid Scheme, House of Cards, In God We Trust, Let Them Eat Cake, and (my favorite) Brother Can You Spare a Dime*.

Tim told me much about his work, but I will only cover three elements here. He wanted first to speak to the economically and politically powerful, also to illustrate aspects of the recession for those who have little, and finally, employ the symbolism of jewelry.

Jewelry symbolizes wealth and power. For ages, mankind has honored the signet ring, kissed the King's or Pope's rings, and marveled at the Hope Diamond *(Le Bijou du Roi)*. This piece of jewelry displays status. To employers and investors alike, Tim would say: "Who creates your wealth? Do you think about them?" He would ask all of us: "Does our society acquiesce too much to power?"

He first made the ring *"Pyramid Scheme,"* which he drew directly from the news about Bernie Madoff, which illustrated the range and depth of greed and corruption. Then, as he says, "one thing (ring) led to another."

He then made *"Let Them Eat Cake."* Most of us are familiar with that phrase, often attributed to Marie Antoinette. Although there is no record of her ever having said that, the import of it is powerful. It illustrates callous disregard of the many by the few, whose situation is untroubled by economic ills and whose consciousness does not extend to the plight of the poor.

Tim next made *"In God We Trust."* Our history and economic texts teach us that the U.S. monetary system was originally based on the gold standard, but now is essentially based on faith. This brings two elements forward: Nestled in a surround of 18 karat gold on the ring, an image of George Washington (cut from a dollar bill) peers out at the viewer. Let us remember that we are being watched by those in power. Then, there is the matter of faith, and the fact that mankind's most powerful faith is religion. Hence, the top of the ring is shaped into a cross.

Tim then moved on to *"House of Cards."* The imagery that immediately comes to mind from this phrase is of a tumbling pile of cards, falling due to inherent weakness in an otherwise pretty structure. So, naturally, Tim used cut-up pieces of credit cards to illustrate the effect of the accumulated debt in our country, leading to the housing crisis, credit swaps, massive economic dislocation and homelessness across the country.

Then, last, he made my favorite, a ring named after the song from The Great Depression: *"Brother Can You Spare a Dime?"* Mounted on the ring's band is a wheel barrow. The barrow is filled with stacks of dollar bills and on its side appear the words "Wall Street." The wheel is a 1931 Mercury dime, also known as "The Liberty Dime." The photographed side of the coin shows a design known as a "Fasces", a bundle of rods with a battle-ax, symbolic of unity, wherein lies the nation's strength. The wheelbarrow was an oft-used tool in the 1930s, and as well a picture of the rich making off with barrows full of money, while the poor stood in the bread lines. Many know the song (*"Brother …"* - lyricist "Yip" Harburg, composer Jay Gorney) in which a beggar speaks back to the system that stole his job. Gorney said: "I wanted to write a song to make people think. It isn't a hand-me-out song of 'give me a dime, I'm starving, I'm bitter' - it isn't that kind of sentiment." The song asks why the men who built the nation – the railroads, the skyscrapers – who fought in the war - who tilled the earth and who did what their nation asked of them, now that the work is done and their labor no longer necessary, should find themselves abandoned and in bread lines.

James Baldwin said: "The purpose of art is not to provide answers, but rather to ask questions." That song - that ring, those rings - carry questions from Tim to us all. The possession of wealth is a symbol of fulfillment of the American dream of individualism, opportunity, work and success. However, does not the possession of it also ask of us that we be humble about it? That we remember its ultimate source, to be grateful for our own blessings, and to be compassionate to those with less?

"You cannot help the poor by destroying the rich.
You cannot strengthen the weak by weakening the strong.
You cannot bring about prosperity by discouraging thrift.
You cannot lift the wage earner up by pulling the wage payer down.
You cannot further the brotherhood of man by inciting class hatred.
You cannot build character and courage by taking away men's initiative and independence.
You cannot help men permanently by doing for them, what they could and should do for themselves."
- Abraham Lincoln

DHR Investment Counsel, Ltd.
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5435 College Avenue, Suite 200 • Oakland, California 94618 • 510.596.2580 • www.dhrcounsel.com