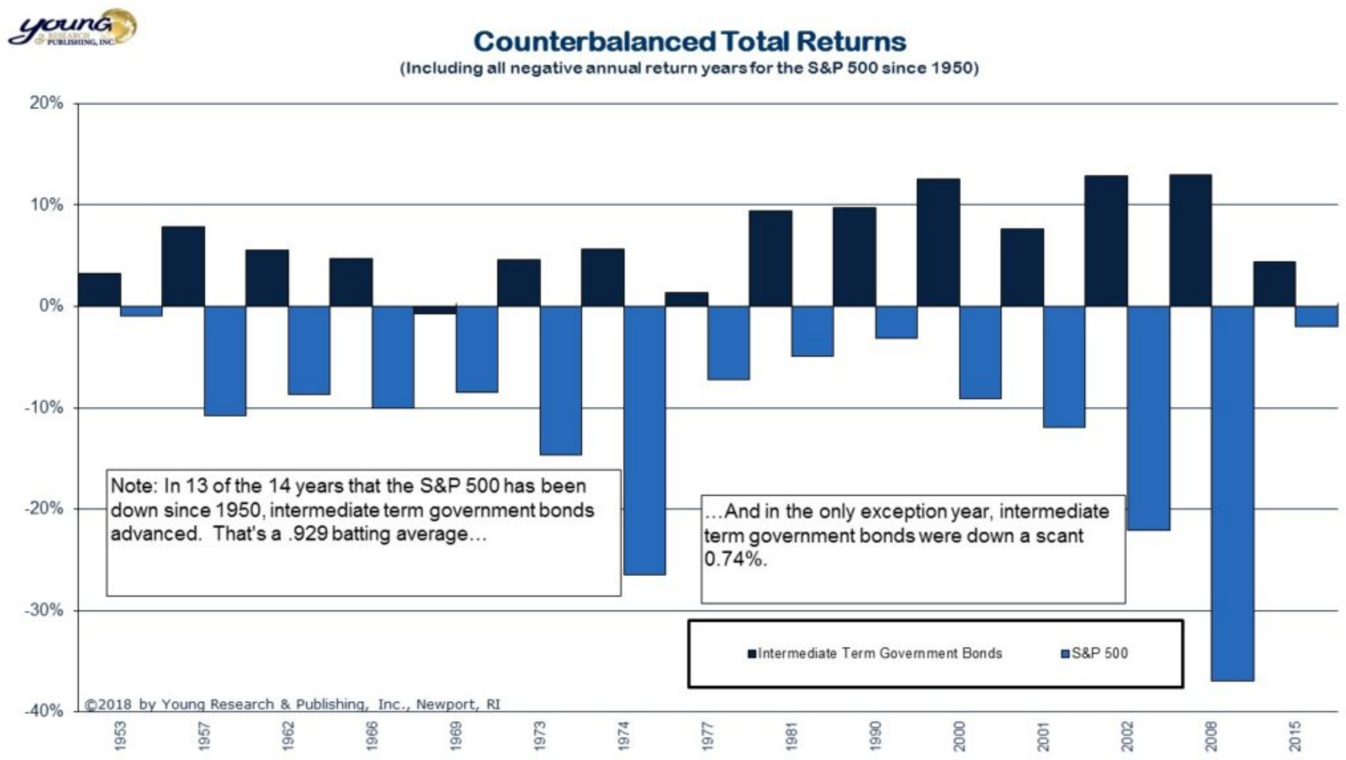
You Must Address the Issue of Risk

What risks are lurking in your portfolio? Calm markets have made many investors complacent. Are you one of them? Far too many portfolios that come across my desk are heavily invested in risky assets (yes, the S&P 500 counts) with no counterbalancing assets to tame volatility. Look at my chart below to gain an appreciation of just how helpful counterbalancing assets can be in your portfolio.

Here you are looking at the performance of intermediate-term government bonds (dark blue) in years when the S&P 500 (bright blue) lost value. Since 1950, government bonds have been up in 13 of the 14 years that the S&P 500 has been down.



In 1992 I explained to readers a timeless strategy for counterbalancing their portfolios. No matter where you are today in your investment journey, you must address the issue of risk in your portfolio. Read here what I wrote in 1992.

Regardless of your age or ability to take risk, your investment portfolio should be dominated by common stocks (equities) and related open- and closed-end funds on one side, and U.S. Treasury securities and related mutual funds on the other side….

Maintain balance in your portfolio and do not switch back and forth based on your view of the markets. I don't want you to be an events-of-the-moment shopper. Emotions are difficult to deal with when investing. If you allow emotions and events of the moment to dictate your investment thinking, you will frequently find yourself drawn to do just the wrong thing at just the wrong time in the market cycle. The old buy high, sell low advice lives on.

Designate a fixed percentage of your portfolio for Treasuries and related mutual funds and a fixed percentage for equities. Your age, financial resources, ability to take risk, and need for current income will combine to dictate how you should balance the two. In broad terms, my advice to you is to keep more than half in equities if you are a younger investor, and more than half in 1-10 year Treasuries if you are an ultra-conservative, income-oriented retired investor. Each of you has a different investment profile, so it's impossible for me to give you precise percentages. Your key is to set down your needs on paper, make yourself address the issue of risk, and then position your portfolio in two parts. Make changes only if your basic investment goals change.

You maintain balance because you do not have a crystal ball. Each day when I buy The Wall Street Journal, I look to see if tomorrow's date is on the masthead. Unfortunately, it never is, but it does emphasize that neither you nor I ever has tomorrow's headlines.

> *It is the unknown that drives the financial markets over the short and intermediate terms (months to quarters). Unless you are a fortune teller, you must accept short- and intermediate-term swings in the markets created by transient and unknown events. You do not want to invest based upon emotions created by events. Instead, invest with an understanding of the long-term principles of earnings, dividends and economic growth that in the end must govern the markets for financial assets.*

If you need assistance realigning your portfolio, or if maintaining balance takes too much time and effort, seek help. Firms like my family owned investment advisory service can take the weight of every-day management of your investments off your shoulders. If you want to learn more about the ways a Barron's Top 100 registered investment adviser (2012-2017) Disclosure is managing risk for its clients, read through the Richard C. Young & Co., Ltd. monthly client letters here. If you wish, you may sign up to receive an alert each time the newest letter is released. The service is free, even for non-clients, so you can easily gain an understanding of our risk management philosophy.

Don't let inertia hold you back from addressing the risks of unbalanced investments in your portfolio. Act now.

What Should You Buy?

Even after a mini-correction in the S&P 500, most stocks still aren't cheap. So what should you buy? In 1991 I wrote that utilities offered outstanding relative value compared to other securities.

> *Utilities Offer Outstanding Relative Value*

Three industry groups should be emphasized for new purchases in your portfolio over the next few quarters: electric, gas and telephone utilities. My number one mutual fund portfolio manager (this month's spotlight), Vanguard Equity Income Fund's Roger Newell told me recently that electric utilities are now his top industry choice with 18% of his $450 million portfolio now in utilities. Roger Newell is buying electric utilities—18% of his $450 million portfolio—because he feels the 1991 run-up in growth stocks and cyclical stocks has drained money from the utilities, and they now offer compelling relative value.

Today, outstanding would be an overstatement when referring to utilities' relative value, but there are some interesting opportunities to be had within the sector for the discerning investor. As always, a focus on dividends and dividend growth will serve you well over the long haul.

A Winning Strategy: Stay in the Game

There are endless cliches about never giving up and quitting being the surest way to lose. Finishing a race is a prerequisite to winning it. My son-in-law, E.J. Smith, managing director of our family run investment council firm, recently explained some of the philosophy behind what it takes to develop a winning investment strategy on his blog Yoursurvivalguy.com. He wrote:

"E.J., Has Your Phone Been Ringing off the Hook?"
Well this was a fun month for the stock market with wild swings from high to low of around 2,000 points in the Dow

Jones Industrial Average.

One question I'm asked on a consistent basis is "E.J., is your phone ringing off the hook?" and my answer is "no," and I know why. Most of you have been educated by Dick Young that investment success is achieved over a lifetime, not a month or two. Investment success is about hitting singles and doubles, taking some walks here and there and sometimes getting hit by a pitch. Staying in the game is key. It's a winning strategy because it puts compound interest into play. Spend a lifetime compounding money on a consistent basis and you'll wake up one day and say "Wow, I have a pile of money." It's funny, when I ask investors how they achieved their success. They don't talk about the stock market. They talk about working long hours, putting one foot in front of the other, showing up for work every day and s-a-v-i-n-g as much as they could save. Looking back 40-years, they know how tough it was to save $1,000. Compound that at 8% and it's $21,725 today. Not a bad start.

Click here to finish reading this post on Yoursurvivalguy.com.

Compound Interest is Key

For prudent investors, the last three years have meant watching the so-called FAANG stocks (and other speculative shares) rise at a rate that is seemingly unbounded by profits or dividends. The FAANGs have gobbled up an ever-larger portion of the S&P 500 index total market capitalization. Four of the five largest companies in the S&P 500 are now FAANGs.

Today's market environment feels similar to the late 1990s when speculation was dominant. To successfully navigate the environment then, I advised a focus on patience and compound interest.

> *Compound Interest Is the Key*
>
> *Legendary investor Phillip Carret used to say that investing genius consisted of one part patience, and one part compound interest. And Charlie Munger, Warren Buffett's long-time partner, will tell you that he is rarely without a compound rate-of-return table. As Munger says, "Understanding both the power of compound return and the difficulty of achieving it is the key to investing."*
>
> *If you adhere to a base of value, keep your portfolio turnover low to cut costs and taxes, and rely on the miracle of compound interest, you will set yourself on the safest and surest course to profit both this year and in future years. Craft your portfolio with counterweight building blocks that allow you to ride out the vagaries of the marketplace.*
>
> *Last year was the third consecutive year that growth stocks outran value stocks. But remember, growth and value tend to produce similar returns long term. One sector is ahead for a period, then the other has its day. Back in the two-tier market of the early 1970s, growth stocks had a field day at the expense of value stocks. But over the next decade, it was another matter. Value stocks clobbered growth stocks, and it's value stock that are cheaper now in 2000.*

The same advice can be given today. Patience and compound interest never go out of style.

Dow Down Over 1,000 Points

What great news for me and for you if you are actually an investor. I mean a real, seasoned investor. One who embraces common sense, patience and the acuity that comes with decades studying the power of consistent cash flow matched with the most powerful word in investing: *compounding*.

My business is, as are my own portfolios, based on exactly these concepts. Market volatility has zero to do with dividends, interest (the source of cash flow), or compounding. Absolutely zero.

In that I have no plans to sell my major holdings (many owned for decades), I am not concerned about short-term market swings. What does cause me to pay close attention is the potential opportunity to invest my regular cash flow more advantageously than during periods of market buoyancy. That's just common sense, is it not?

So, let's look at some of the information I urge my clients to use to make steady, long-term investing decisions. Linked here is intelligence you can actually use to improve your long-term investment acuity.

The *Young's World Money Forecast* (my online home base for intelligence gathering) display looks at 10 blue-chip long time Dow dividend payers with solid dividend growth prospects. Keep this invaluable little menu at hand for regular reference during periods of opportunity brought about by normal and expected short-term financial markets volatility.

Warm regards,

Dick

Quality Always Rises to the Top

Back in November of 1990 many investors were nervous about their portfolios. Iraq had invaded Kuwait and war seemed inevitable. That month, the UN Security Council passed Resolution 678. The resolution gave UN members the go-ahead to use force to remove Iraq's military from Kuwait if it remained there after January 15, 1991. It seemed only a matter of time before a big war would break out. Aerial bombardment of Iraqi positions began January 16.

Despite the fear that pervaded markets, I was very confident then in my investment portfolio, as I am today. I had built a portfolio conditioned to survive maximum distress. I was focused on the long-term prospects of my investments, not how they might be affected by transitory events. While expressing my focus on the long-term, I also explained my enthusiasm for investing in collectibles, specifically vinyl records. I wrote:

> *I like to invest in collectibles, not just in stocks and bonds. What once was the biggest record store in New England, the Harvard Coop, today sells no records, not a single one. Within 12 to 24 months, you will be hard pressed to find a record in a store. Even the old specialty vendors are facing such a decline in sales that they will soon become extinct. Forget new records—few if any will be made. We are told that the digital technology of CDs is what we need, and at substantial price premiums to records.*
>
> *Let me give you some important advice. Records will be back in style and with a rush as collectors and music aficionados*

finally realize that they've been had just a little. Yes, digital technology offers a clarity of sound missing on records from the 1940s, 50s, 60s and 70s, but digital also delivers a sonic deficiency. Digital does not have the warmth of vinyl recordings. The sound records produce is warmer. I consider myself to be somewhat of an expert on the subject with nearly 1,000 albums, stacks of 45s, and over 400 CDs. I've made the test often, and I hear a warmth from records not available from CDs.

I buy jazz and group harmony R&B records from the 1950s, and they are now darn hard to find. All my classical and show-tune aficionados know what I mean. …

45 Records From the 50s Can Cost Hundreds of Dollars Each

The U.S population is aging, is retiring early, and has money. With time on their hands, the surge in retirees will make the nostalgia/collectibles market boom. The records you like will not be available readily and will not be reprinted in record format—and the chase will be on. I'm seeing prices on 45s from the 1950s soar. Try to buy a Wrens or Valentines 45. You'll pay hundreds of dollars per record, if you can find one. Jazz, rhythm and blues, classical, and show tunes will lead the way. If you have an interest in any of these four types of music and like to collect, think vinyl, because your old favorites are going to become as rare as a balanced budget—and mighty expensive to boot.

Prescient, no? Baby Boomers and Millennials are today fulfilling my November 1990 prediction of a revival in vinyl records. Drawn in by a quality and warmth lacking in CDs and MP3s, Millennials have joined their Baby Boomer parents in fostering a vinyl resurgence. Quality has risen to the top.

My portfolio of high quality investments rose to the top during the market jitters of the Gulf War. And when the dotcom bubble burst, it powered through again. As the Great Recession hit, my high-quality portfolio persisted, suffering much less than the average. And I suspect that my portfolio, still focused on interest paying fixed income and reliable dividend payers, will succeed once again in the face of any new market upheavals. Just as vinyl has outlasted the advent of digital music technologies, a strategy focused on low risk and consistent returns will outlast an artificial bull market powered by low interest rates.

I stick to my investment game plan, and employ the same strategy for clients of my investment advisory, Richard C. Young & Co., Ltd. The firm's President and CEO, my son Matt Young, discusses taking stock of your investment goals and sticking with them in his most recent monthly client letter here (you can sign up for the letter here for free, even if you're not yet a client). I encourage you to read through Matt's letter and assess your own risk tolerance and game plan.

As for collectibles, my current focus is on Burgundy as an investment. You can read about my extensive research on the subject in these posts from Richardcyoung.com:

- **Wine Investing—Burgundy or Bordeaux?**
- **On the Ground in Burgundy with Dick Young**
- **In Burgundy, It's 'Raze the House, Plant more Vines'**
- **Blue Chip Burgundy Prices up 31%**
- **Burgundy or Bordeaux?**

Your First Step Toward

Investment Success

For over four decades, I have offered strategies and insights to help individual investors like you. My primary goal, whether in my monthly strategy reports, at investment seminars, or for current clients of my money management firm, has been helping investors achieve long-term investment success.

What you buy, what you sell, what price you pay, and which strategies you pursue all matter for your investment success, but they aren't the most important steps in the process. Focusing first on what the "good buys" are is putting the horse before the cart.

What's your goal? First define what investment success means to you and your family. Next, determine how much risk you can or want to take in your portfolio to achieve that goal.

Does investment success mean doubling your money in five years, even if that requires a portfolio with neck-snapping volatility and nights awake in a cold sweat? Or are you like me—a more patient investor who is more interested in preserving wealth and letting the power of compounding work its magic over time?

Ask yourself how much risk you can take or want to take.

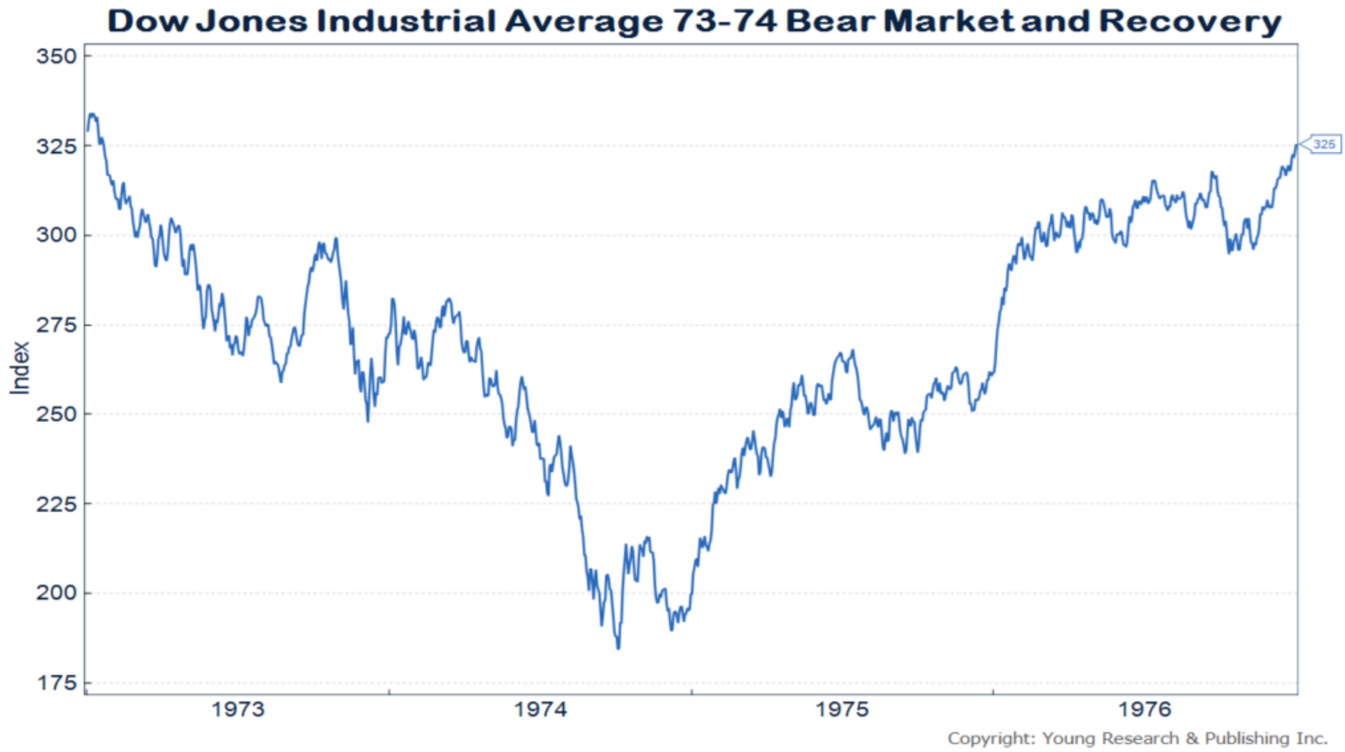
The success I want you to embrace comes from compounding and patience. I invest guided by the principles embraced through the decades by Benjamin Graham, Walter Schloss, and David Dreman.

Rising Dividends: Decades of Focus on a Winning Strategy

In 1987, I sat down with Bill Lippman for a conversation about L.F. Rothschild Fund Management's "Rising Dividends Fund." Bill had been the founder and president of the Pilgrim Group mutual funds for 25 years before he sold the firm. Bill then moved over to the New York based, L.F. Rothschild Fund Management, at the time a new subsidiary of L.F. Rothschild investment bank. (The Rising Dividends Fund would later become the Franklin Rising Dividends Fund, which still trades today, though this is not a recommendation to buy).

The Rising Dividends Fund focused on what I have been recommending to my readers for years; solid companies with strong records of increasing dividend payouts. I have been focused on dividend payments since my days at Babson reading Ben Graham and David Dodd.

Bill was interested in rising dividends as a way to protect his fund's owners from experiencing the type of punishment in their portfolios they felt in the bear market of 1973-1974. Those unhappy days of "stagflation" saw unemployment of 8.5%, CPI increases of up to 11%, and a drop in the Dow Jones Industrial Average of 46%. Afterward, investors were not eager to have their savings ripped apart again. The pain was so bad that even in 1987 when Bill and I discussed his Rising Dividends Fund, the lessons of 73-74 were still remembered well.



When we talked, Bill said "In 1973-1974, we had a really bad market. It was a disaster…and it went on and on for a couple of years. It seemed like it would never end. One then asks, 'Is there a better way?' As it turns out, yes, there is a better way. You must have a philosophy, and you must stick to it. Don't be the victim of the latest hot story that comes off the tape. And that's what we did that was different. We evolved a philosophy that made sense. We selected companies that increased dividends and had low debt and low P/Es. We wanted a solid game plan that we could follow with comfort through good markets and bad."

My focus for you today, just as it was in 1987, is on quality dividends from companies that are dedicated to increasing their payouts. As part of the RCs program at Richard C. Young & Co., Ltd., and in my recent coverage of the Dow stocks here on *Youngsworldmoneyforecast.com*, I consistently focus on finding companies that do just that.

Another thing Bill said in our discussion that really resonated with me was a piece of advice he gave to all investors "Put down in writing what you really believe in, and then stick to it." I encourage you to do that right now. Don't wait until later, or let inertia allow you to forget. Do it right now. Write down what you want to accomplish by investing, and how you plan to do it. Then stick to it.

The Dogs of the Dow and Dividend Dependability

Last month, I provided you with Young Research's dividend dependability ratings for the 30 blue-chip Dow companies. Young Research's Dividend Dependability ratings use a combination of fundamental and qualitative factors to rate the dividend safety of each Dow component.

Every company in the Dow pays a dividend and compared to the average dividend paying company, Dow companies have above average dividend safety, but that didn't prevent General Electric from cutting its dividend last year, or GM slashing its dividend while still a Dow component, or Eastman Kodak from cutting its dividend or, or, or.

High yielding Dow stocks are tempting to income investors. You are often talking about high yields on some of America's best companies. In a low yield environment, a 3%+ dividend yield on a blue-chip stock has inherent appeal. But if you are retired or soon to be retired, and you rely on your dividend income to fund expenses, a dividend cut could put a dent in your retirement income. That is especially true if you follow one of the more popular Dow dividend investing strategies—The Dogs of the Dow.

The Dogs of the Dow is popular partly because it has worked over long periods of time, but also because it is a simple strategy to follow. All an investor must do is rank the 30 Dow stocks by yield at the end of each year and buy the 10 highest yielding stocks in equal amounts. The stocks are held for the balance of the year, and at the start of the following year the process is repeated.

The problem with the strategy is that the highest yielding stocks may be at most risk of a dividend cut. A high yield sometimes means a stock is out of favor (that’s what Dogs of the Dow investors are hoping for), but it can also signal that the dividend is at risk. How do you avoid the problem?

That’s where Young Research’s Dividend Dependability ratings can help you. The highest yielding stocks in the Dow to start 2018 are Verizon, IBM, Pfizer, Exxon, Chevron, Merck, Coca-Cola, Cisco, Procter & Gamble, and General Electric.

Six of these stocks fall into the bottom third for dividend dependability. Those stocks include IBM, Exxon, Chevron, Merck, Cisco, and General Electric. The four that rate in the top twenty for dividend dependability are Verizon, Pfizer, Coca-Cola, and Procter & Gamble.

If you want to invest for yield, but reduce your risk of owning a company that may cut its dividend, you can replace the six Dogs of the Dow stocks that rank in the bottom third for dividend dependability with the highest yielding stocks from the remaining stocks that rank in the top two-thirds for dividend dependability.

Based on current yields, those stocks include Intel, Johnson & Johnson, McDonald’s, Boeing, Travelers, and United Technologies. Add those to positions in Verizon, Pfizer, Coca-Cola, and Procter and Gamble, and you are looking at an average yield of 2.8%. The average projected dividend growth for this group of stocks in 2018 is 6.3%. Compare that to the 10 stocks in the

Dogs of the Dow that have an average yield of 3.4% and projected dividend growth of 3.9%. You give up 0.60% in yield for the comfort of more dependable dividends and better dividend growth prospects.

Not a bad trade for investors who rely on regular dividend income.

For more on dividend dependability, read parts one, two, and three of my series on the subject.

The Dow's Most Dependable Dividend Payers Part III

Continuing with Young Research's dividend dependability rankings, the group of stocks listed below score best out of the 30 stocks in the Dow in terms of dividend dependability. Many of the most dependable dividend payers in the Dow have below average yields, but above average dividend growth prospects.

I have again listed the stocks in alphabetical order and provided the indicated dividend yield, projections for dividend growth in 2018, and commentary on why the stock scored where it did in terms of dividend dependability.

wdt_ID	Company	Indicated Yield	CY 2018 Proj. Div. Growth	Comments
1	WAL-MART STORES INC	2.08	1.97	A solid balance sheet, low earnings variability, and strong dividend coverage put WalMart in the top group for dividend dependability
2	VISA INC-CLASS A SHARES	0.69	17.39	Visa's strong earnings growth prospects, high dividend coverage, and low earnings variability make it one of the Dow's most dependable dividend payers.
3	UNITEDHEALTH GROUP INC	1.35	17.57	Strong growth and dividend coverage as well as low earnings variability put UNH in the top group.
4	PROCTER & GAMBLE CO/THE	3.00	1.87	A solid balance sheet, moderate growth, a good qualitative score, and a strong record of dividend growth keep P&G in the Dow's top group despite below average dividend coverage.

wdt_ID	Company	Indicated Yield	CY 2018 Proj. Div. Growth	Comments
5	NIKE INC -CL B	1.30	11.11	Above average dividend coverage, a strong balance sheet, and moderate earnings growth pushed Nike into the top group.
6	MICROSOFT CORP	1.97	7.55	Strong earnings growth, solid dividend coverage, and a AAA balance sheet drive Microsoft's dividend score.
7	JOHNSON & JOHNSON	2.38	4.82	A solid balance sheet, a strong record of dividend growth, and low earnings variability make JNJ one of the Dow's most dependable dividend payers.
8	HOME DEPOT INC	1.89	6.74	Strong earnings growth, good dividend coverage, an above average earnings variability score, and a good balance sheet pushed HD into the top group.

wdt_ID	Company	Indicated Yield	CY 2018 Proj. Div. Growth	Comments
9	BOEING CO/THE	2.32	20.42	Exceptional earnings growth, good dividend coverage, and a solid balance sheet helped Boeing.
10	3M CO	1.99	5.53	Solid earnings growth, moderate dividend coverage, low earnings variability, and a strong balance sheet put 3M in the top group for dividend dependability.

You can read part II here and part I here