The Meridian Memo

Meridian Financial Advisory **1/2/2018** [Edition 1, Volume 1]

Happy New Year!

Dear Meridian Clients:

First, we want to thank you for partnering with Meridian. We take your success very seriously.

Portions of this inaugural newsletter may be more technical than future newsletters.

There are 2 important objectives we want to share, that we have when positioning client portfolios.

We want to understand the market better than our competitors and use that knowledge to influence our long-term client strategies for their benefit.

1) In light of historical returns and risks (i.e. volatility measured by standard deviation) associated with different asset classes we structure portfolios to maximize the return to risk ratio for a given goal (i.e. risk or return target). That requires diversification, allocations (based on investors' risk profiles and investment horizons), and rebalancing systematically. Investors should view their portfolio considering their investment horizons. Average returns over horizons that span multiple years are more predictable than over shorter periods. If it is a shorter investment horizon, the client would be positioned in an asset with a smaller 1 year standard deviation.

2) We commit a portion of every day to reading market research reports we have found most insightful and that have demonstrated the most predictive power. "Old Wall" (as Hedgeye founder Keith McCullough calls them) analysts' 'buy and sell' ratings mean very little to us. They are always behind the curve and selling unoriginal consensus viewpoints that won't get them in trouble if they are wrong. Based on information provided by the market we form an opinion. Rates of change matter more than absolute values. It's not "good" or "bad" but rather "better" or "worse" that concerns us. Market history colors our recommendations and influences how we position clients in the first place. We want to understand the market better than our competitors and use that knowledge to influence our long term client strategies for their benefit. We will dedicate a portion of these notes to communicating our views of the market. Since we have already committed a portion of this newsletter to other issues we will keep our market analysis brief.

As this is our inaugural newsletter, we want to take the time to thank you for the confidence you have placed in Meridian Financial Advisory and the opportunity to serve you. We take that trust very seriously. It inspires and motivates us. Our desire is that you achieve your financial goals as you have discussed with us, helping you preserve, protect, and responsibly grow your assets. Every client of Meridian is treated as a member of our family whose success is our success and somebody with whom we want to build a dedicated and enduring relationship.

Market View

So, What is Our Take? Where are the Biggest Opportunities and Biggest Risks?

Almost everyone begins their discussion of the market talking about stocks. As exciting as that is, because many of our clients are either in retirement or approaching retirement and consequently have large bond portfolios we will start there. Fixed income is an essential part of anyone's portfolio (young or old). It pays income and offsets price movements in one's equity portfolio. Notwithstanding the indispensability of bonds in a portfolio there are some notable risks associated with them we should consider. We will try not to get in the weeds too much but environments where interest rates are rising can pose challenges for bonds. The price of bonds and the yield [1] of bonds move in different directions (inversely). Market gurus have been saying for a long time that yields are going to move upwards quickly and substantially, and so far they have been proven mostly wrong. That may be changing. In the intermediate term[2] at least, the risk is that rates move higher as they are currently in a bullish phase. That is because economic growth has accelerated, some inflation has presented itself, and our central bank has started raising rates. That means the price of bonds could move lower. You can take comfort knowing that would be offset by the income generated by the bonds and, at present, the bull market in equities. Most clients, even conservatively positioned ones, have at least 25% of their portfolio in equities. Before we look at the price of the S&P 500 or the Dow Jones Industrials, we at Meridian look at 2 indicators. We look at the yield of the 10 year Treasury Note ^TNX and the price of a core bond portfolio that we use in a lot of portfolios $AGG. These often move inversely. As ^TNX moves up, $AGG generally moves down and vice versa. Finally, we look at the Vanguard Short Term Treasury Inflation Protected Securities (TIPS) portfolio $VTIP. We include these in most client portfolios to offset price risk in core bond portfolios. TIPS become more valuable as inflation increases which is often synchronous with rising interest rates. This portion of clients' portfolios will go a long way in offsetting risk in bond portfolios associated with rising interest rates.

We have a view on stocks, but we do not want to make this first newsletter too long. Without going into as much detail, we can say stocks will likely continue to move higher notwithstanding valuations or the age of the bull market.[3] That is our outlook for the intermediate term. [4] Bull markets don't die because of old age. They end when economic growth decelerates, inflation and rates rise too quickly, or companies begin to default. We are looking for these signals.

The companies that have been the strongest in 2017 are high growth ones. The tech sector $XLK and the bio tech sector $IBB have performed especially well. Value companies and low growth companies have experienced marked under-performance relative to growth companies and the market as a whole. We make sure we contextualize these intermediate term trends within the framework of longer term historical trends, which are of primary concern to us.

New Year Financial Checklist

- ✓ Pay down credit card debt that was accumulated over the holidays or throughout previous year.
- ✓ Build a 6 month cash reserve fund to cover unexpected expenses or job loss.
- ✓ Rebalance your investment portfolio.
- ✓ Maximize retirement account contributions.
- ✓ Check your credit report at: annualcreditreport.com.
- ✓ Track your expenses using: youneedabudget.com, mint.com, or with quicken software quicken.com.

"I retire on Friday and I haven't saved a dime. Here's your chance to become a legend!"

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[1] Yield can be thought of as the income of a bond divided by the price of the bond

[2] 3 months or more

[3] As of Nov 25, 2017, this bull market has lasted 104 months and the S&P 500 has risen by 290% (since March 2009). The average bull market lasts 72 months and gains 200%. Since 1940 the average bull market has lasted 96 months and gained 231%.

[4] 3 months or more

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