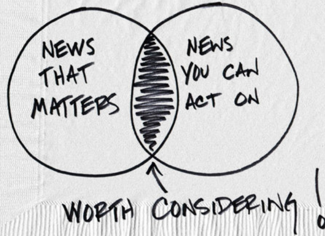

QUOTABLE

"Prediction is very difficult, especially if it's about the future." Nils Bohr, Nobel Prize in Physics, 1922.

"Political storm clouds loom over the global economy. From Washington to Beijing, the financial markets are in thrall to seismic political events." *Financial News*, January 2013

"Although investors are not as complacent as they were heading into 2000 or 2007, it is still hard to believe this will be a bumper year for returns." *The Economist Magazine*, January 2013

"Analysts are predicting no end to the volatility that has gripped markets over the New Year period, posing dilemmas for investors wondering how to invest in 2013." *The Australian Financial Review*, January 2013

"It takes 54 months of expansion for many professional economists to realize a recovery has started." Dan Gross, *The Daily Beast*

Reading between the lines of 2013

When we see a story in the news repeatedly, we have a tendency to think it must be important. Thinking something is important often means we feel we should do something about it. This year, there were a lot of catchy headlines in the financial news, and most of them represented little more than noise. There were, however, a few important themes in 2013 that may affect your financial plan as we head into 2014.

1. The market was up sharply.

Up over 26 percent in 2013, the Dow Jones industrial average had its best year since 1996, but what does that mean for you? If you have not already done so, it is probably time to rebalance your portfolio. Based on your plan, you will want to review how your portfolio is apportioned among stocks, bonds and cash. Even though stocks look really good right now, the last thing you want is to let the market drive your decision-making. You may think you are comfortable with the greater risk of having more invested in stocks right now, but what about six months from now?

If you do not have a portfolio built on a plan (for example: diversified, split among stocks, bonds, cash and so forth), then it is time to build one. Do not let the current excitement around stocks trick you into thinking you should go all in. It's not safe even if "everyone else is doing it." That's something teenagers say right before they do something stupid.Don't be a teenager with your finances. Take the time to become clear about your goals and build a portfolio that will get you through both the ups and the downs that will hit the market.

2. Interest rates are still low, but …

It may seem as if interest rates will stay at historical lows forever, but don't bet your house or your portfolio on it. Now is a good time to hold a lifeboat drill. Ask yourself: What will happen to your financial picture if rates go higher? Higher rates may mean fewer options, so now is the time to do what you can to protect yourself against a rise. Do you have an adjustable-rate mortgage? Consider locking in your rate. Then, take a look at your portfolio. You want to make sure the portion of your portfolio that is meant to be "safe" (for example, bonds) is actually safe.As an example, if you have bond mutual funds, make sure you understand what you actually own. Start by looking at the current average credit quality, maturity and duration. Remember that higher credit quality and shorter maturities equal less risk. The reason you own bonds is to provide safety and to allow the stock portion of your portfolio to work for you, so make sure they are actually as safe as you assume. The last thing you want to do right now is buy a bond or a bond mutual fund that offers a higher yield at the expense of large principal loss if interest rates go up. However, do not be drawn into thinking you should move to cash and wait for interest rates to go higher. We know people who have been waiting for rates to go *up* for years. Yes, earning a ridiculously low 2 percent in a high-quality, intermediate-term bond does not sound exciting, but 2 percent is better than cash. So be safe, but avoid being stupid.

Sometimes predictions are right. When they are, it is often attributed more to luck than skill. One study looked at the stock-picking performance of 2,076 mutual fund managers over a 32-year period. It concluded that the stock-picking skill of these managers was statistically indistinguishable from zero.

This is the time of year when the "pros" come out in droves, full of themselves, and offer the rest of us their predictions for the coming year. It is counterintuitive to appreciate the fact that they are emperors with no clothes, pretending to have an expertise that doesn't exist.

3. Housing markets improved.

After the bubble burst, it seemed as if housing might never recover. But with low interest rates and improvements in the economy, we have seen some positive movement in housing. What does an improved housing market mean for you?

If you have been waiting to sell or buy, now is a good time for a review. While your home's value may not be at 2006 levels, it might have recovered enough to give you options. Run the numbers and see. You may find that 2014 is the year to exit your holding pattern if you have wanted to sell. And if you are thinking about buying, given where interest rates are, it may be worth looking at your options there.

Review your finances and know how much house you can really afford, so you can avoid surprises when you apply for a mortgage. And don't let the fact that the housing market has recovered a bit trick you into buying more than you can afford. As we have learned, housing prices can and will go down.

While we are a big fan of shutting off the noise and not reacting to headlines, there are times when we need to put the news in context. These three stories are great examples of the kind of news that we want to think through to understand how it might affect our financial decisions. Of course, you may end up doing nothing, but by taking the time to weigh how these big events fit in your overall financial plans, you will lessen the odds of future disappointment.

As 2014 gets underway, there are still plenty of gloomy stories to fill the newspapers—including ongoing speculation of what happens when the US Federal Reserve begins tapering its monetary stimulus program.

This isn't to say these stories are necessarily incorrect. Most of them accurately reflect the sentiment prevailing at the time they were written and the uncertainty about the future, as expressed in prices.

But as an individual investor, there is not much you can do about that. These expectations and uncertainties are already built into the market. Investing is about what happens next. We don't know what happens next. That's why we diversify.

And think about this: If any of the gurus who regularly appear on financial television or in the newspaper really had a crystal-clear view of the future, why would they bother sharing it with the world?

It makes more sense to focus on what's in your own control.

In the meantime, many happy returns!

We wish you a happy, healthy and meaningful 2014.

Transitions Wealth Management, LLC