RIVERVIEW QUARTERLY INSIGHTS

WHAT THE HECK?

If you were reading the financial news during the second quarter, by the end of June you might have found yourself scratching your head thinking "What the heck?," as the news cycle went from cheery and optimistic to doom and gloom in just a matter of a few weeks. Meanwhile the equity market experienced volatility, but by quarter's end, everything seemed to end up okay.

For instance, on May 3rd, The Wall Street Journal observed that U.S. worker productivity improved last year at the best pace in nearly a decade, "laying groundwork for stronger wage growth and continued economic expansion." Higher productivity, which often occurs early in an economic growth cycle, often leads to wage growth without harming corporate profits. The next day, an article in The Economist expressed the belief that fears of an economic downturn seemed overblown, observing that JP Morgan put the chances of a recession within the next twelve months at just fifteen percent. The basis for such optimism was the Fed's more patient stance on raising short-term interest rates, a persistently manageable rate of inflation and the fact that the pessimism that hung in the air at the start of the year might have been exaggerated.

This optimism seemed well founded. Over the last five years, the members of the OECD (a group of mainly wealthy countries) have added 43 million jobs. In 2018, the employment rate was higher than ever in Britain, Canada, Germany, Australia and 22 other OECD countries. And the facts are giving the lie to common misperceptions that the "gig" economy is leading to poorer-quality employment, and that automation is leading to fewer jobs (although automation is, undeniably, leading to fewer blue-collar jobs).

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But less than a month later, on May 30 The Wall Street Journal was reporting that the S&P 500 had dropped 5.5% for the month, and that bank stocks had done even worse, falling 7.5%, due to the fall in bond yields (which go down as bond prices go up; it's a short-hand indicator that investors are moving from riskier assets to safer ones).

On May 25th, an article in The Economist drew the comparison between "today's market chatter and the [apocalyptic] prophecies of medieval cults." Like 14th Century German heretics, today's investors are acting like they are "living in the end times or 'last days.'" Two forces drive this irrational behavior: on the one hand, an acknowledgment that times are still good, and there's probably still money to be made; and on the other, the recognition that, being late in the growth cycle and in the midst of a trade war, a recession must be looming.

This "last days" mentality became even more apparent on June 7, when the Labor Department reported that the economy added only 75,000 new jobs, one of the weakest jobs reports in the last decade and one that was broad-based across industries. In response to this disappointing economic news, the S&P 500 rose by over 1% the same day. This counterintuitive result apparently came about because investors believe the Fed will cut short-term interest rates in response. This increase in value capped off the best week the stock market had in six months, with the S&P 500 up 4.4% for the week. In other words, investors are pushing prices up based on the view that bad news is really good news if the Fed follows through on rate cuts.

Such short-term volatility is reflective of a broader trend. The fourth quarter of 2018 saw the markets move dramatically downward, then the first quarter of 2019 reversed that trend. According to FactSet, the S&P 500 went up in price by 3.93% in April, down by 6.58% in May and up again by 6.89% in June. These bounces are being caused mainly by the trade wars that the United States seems determined to wage against any country with which it disagrees, and the forecasting of the economic disruption that these trade wars might create. Further, each of the world's biggest economies has a weakness: the U.S. has a high rate of corporate leverage, China has incurred significant debt and Europe has persistent banking weaknesses. Even if the trade wars are peacefully resolved, any one of these additional factors could bring an end to the current growth cycle.

Ironically, this trade tension might not be all bad. In his "Streetwise" column in the June 12, 2019 edition of The Wall Street Journal, James Mackintosh made the point that the Administration's trade wars were being roundly criticized by economists and putting a damper on investment. However, "by holding back investment, the trade uncertainty might help to prevent or delay the excesses that so often mark the late stage of the economic cycle." History suggests that at this late stage in a growth cycle, "animal spirits tend to be overly positive." So, although tariffs are by no means "good economics," and although they could "trigger a downward spiral into recession," for the time being at least they may be helping the markets ease out of the growth cycle.

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As always, the cure for such apocalyptic, end-of-financial-days anxiety is to return to the long-term data. Our friends at Dimensional Fund Advisors ("DFA") each year provide huge amounts of market return data in their "Matrix Book." This year, they showed returns over 46 years (1973-2018) on a blended 60% stock, 40% bond portfolio. This model portfolio was highly diversified, including international and U.S. investments, small and large cap stocks, and with DFA's tilt toward value stocks, small cap stocks and more profitable stocks. The results of following this strategy faithfully over the 46-year period were impressive:

- The strategy produced positive annual performance 83% of the time.
- There were six recessions during this entire period, but the strategy generated negative returns in only three of those recessions.
- The best annual returns typically followed the worst annual returns (four of the top five best annual returns happened the year after a down year).
- This strategy typically recovered in the year after a down year, meaning that the return in the subsequent year was great enough to overcome the loss in the preceding year, allowing positive compounding to resume.
- There were only two exceptions to this one-year recovery: the 1973-1975 recession and the 2007-2009 Great Recession. In both of those cases it took two years for the strategy to overcome the losses stemming from those two events. However, given the severity of the equity market decline, especially during the Great Recession, a two-year recovery timeframe is remarkably short.

Such data is highly generalized, including assumptions that don't reflect actual results. And (let's all recite the investment advisor's creed) past performance is no guarantee of future returns. Nevertheless, it demonstrates the wisdom of maintaining investment (and emotional) discipline, of not moving in and out of markets based on headlines.

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Unemployment dropping, trade wars looming, interest rates falling, productivity increasing, political rancor growing. And still the world turns on its axis, unimpressed by such noise. One or two or ten years from now, we will look back at these stories and laugh (and maybe also weep a little). But our properly-tended portfolios will show the slow steady growth that always comes from following the plan.

SPOTLIGHT ON PLANNING

SOME PLANNING BASICS WITH LIFE INSURANCE

Life insurance. Just saying the words makes people feel uneasy, either because it forces them to confront their own mortality, or because it makes them feel like they're about to be "sold" something. This discomfort, in part, is what leads many people to be uninsured or underinsured.

Life insurance is a real need. Seventy percent of U.S. households with children under 18 would have trouble meeting everyday living expenses within a few months if a primary wage earner were to die today; further, 40 percent say they would immediately have trouble meeting everyday living expenses.

Perceptions about that need vary, though. For instance, a new study shows that 84 percent of Americans say that most people need life insurance. However, only 68 percent say they personally need it, and only 59 percent own some form of it. Even among those with life insurance, about 20 percent say that they do not have enough.

One of the main reasons people avoid having the insurance discussion is perceived cost. The same study says that 83 percent of consumers don't purchase more life insurance because it's too expensive. However, consumers believe life insurance costs nearly 3 times the actual price: most Americans believe a 20-year, $250,000 level term life policy for a healthy 30-year-old costs $400 annually; in fact, it would actually cost around $150. The overestimation is even worse among the young; 44% of Millennials overestimate the cost at five times the actual amount.

Another reason for avoiding insurance is the complexity. There are many different types of insurance products, each developed as the needs of the clients and the demands of the market have changed. Understanding how any one of them works is hard enough; choosing between them can seem difficult if not impossible at times.

This article will try to explain how life insurance products work and which products are most useful in a given situation.

I. Insurance Product Types: Term vs. Permanent

Although there are many different types of life insurance products, the subject can be divided into two broad categories: term (which is used to cover a particular period of time) and permanent (which covers the insured's entire lifetime).

a. Term Insurance

In its purest form, life insurance is simply the insurance company betting on the insured person surviving for one year. The company decides each year how much it must be paid (the "premium") to assume the risk that the insured will die in that year and that the company will then have to pay the stated death benefit to the insured's beneficiaries. The premium amount is based on factors like the insured's age, health and habits (like smoking or skydiving). As you might

imagine, the older an insured becomes, the higher the premium. This increased premium is directly related to the increased odds of the insured dying as they age.

This kind of "pure" insurance is called "term insurance." Originally, the term was one year at a time, with the premium gradually increasing each year. It's more common now to have 10- or 20-year "level" term, for which the premium cost is averaged over a chosen period of time. For example, instead of the premium starting at $500 in year one and growing to $1,500 in year ten, the premium might be averaged out to $1,000 per year for each of the ten years. The policy doesn't automatically lapse after the term expires. Rather, the premium at the end of the chosen term increases annually. Eventually, the term policy becomes more and more costly as the insured gets older, and often the policy owner will stop paying the premiums. As a result, the majority of term insurance policies simply lapse at some point, with no residual insurance or cash value to the insured. As its name implies, term insurance is most useful when the liquidity need is temporary (for instance, to replace salary for a younger couple in case one of them dies unexpectedly, but with the expectation that as the couple gets older, saves and reduces household debt, the insurance will become a less important part of their estate planning).

b. Permanent Life

Some insurance contracts don't end after a set term. In many situations, "permanent" insurance is more appropriate than term insurance. As the name suggests, a permanent policy does not automatically expire after a set term of years; rather it normally is held throughout the insured's lifetime (as long as he or she keeps paying the premium). With these "whole life" products, the premiums consist of a term insurance component (death benefit) and an investment component (cash value). When the insured dies, the "death benefit" is a combination of the cash value component plus term insurance value. Over time, the cash value within the whole life policy increases and effectively reduces the term insurance component. In this way the investment component helps to keep the premium on whole life policies stable over time. The insurance company invests the cash value component of the premium in very safe (state regulated) investments, like US Treasuries. If the insured lives long enough, the cash value in the policy increases to the point where it equals the death benefit, at which time the insurance company simply pays out the cash value to the insured. This normally happens on or before age 100. The owner of the policy can withdraw the cash value in the policy at any time or can borrow against it; however, if the policy has too little cash, it can lapse.

A more recent development in the permanent insurance world is "guaranteed no-lapse" insurance, which has a premium higher than term but lower than whole life, and which has no cash value built up. In addition to whole life and guaranteed no-lapse policies, there are a myriad of other permanent insurance choices.

c. Long-Term Care Hybrids.

As we live longer lives, the cost of health care later in life is becoming an ever-greater concern. As many as 70% of Americans will require long term care at some point in their lives, and current costs for long term care facilities can run anywhere between $70,000 – $150,000 annually in a semi-private or private nursing home. Meanwhile, traditional long-term care insurance policies, which pay for long-term care if the insured loses the ability to manage certain aspects of daily living, can be prohibitively expensive.

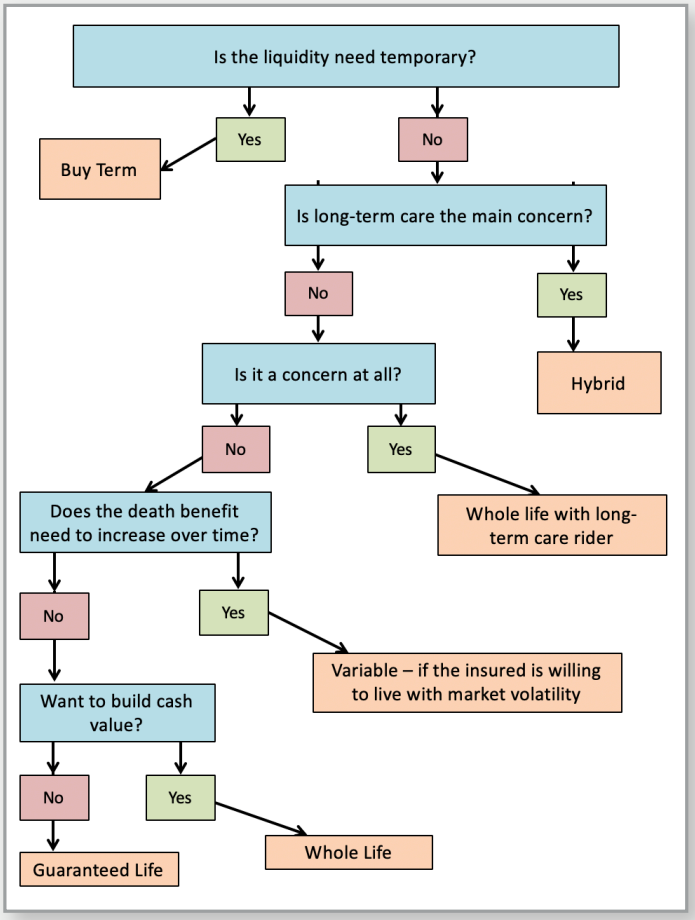
Recently, some long-term care coverage alternatives have been developed by the insurance industry. These hybrid alternatives do not provide comprehensive coverage the way traditional long-term care insurance does, but they can provide at least some benefit in the event it is needed. These include annuities with long-term care benefits, and life insurance with long-term care riders (a "rider" is an additional feature which increases the premium cost and which allows access to the cash value in the policy for long-term care needs). A discussion of these alternatives is beyond the scope of this article, and the products themselves are continually refined. An experienced life insurance advisor is critical to explaining the options available.

II. Choosing Among These Products.

As this brief introduction to insurance has shown, planning with insurance is complicated. Although the only way to make an informed decision about product selection is with the advice of an experienced life insurance advisor, we've attached a flow chart that can help you begin the process.

Most importantly, insurance should be chosen by appropriateness and need, not price. As we've discussed, term insurance is less expensive than whole life, but the chances of a term product eventually becoming unaffordable is high. Additionally, long-term care riders are generally only available with the more recent types of hybrid, cash value policies.

If you would like to discuss further the potential uses you might have for life insurance, please don't hesitate to contact us.



MARKET SNAPSHOT

MARKET SUMMARY – Short- and Long-Term Index Returns

	US Stock Market	International Developed Stocks	Emerging Markets Stocks	Global Real Estate	US Bond Market	Global Bond Market ex US
Q2 2019	STOCKS				BONDS	
	4.10%	3.79%	0.61%	1.29%	3.08%	2.75%
1 Year	STOCKS				BONDS	
	8.98%	1.29%	1.21%	8.81%	7.87%	7.61%
5 Years	STOCKS				BONDS	
	10.19%	2.04%	2.49%	5.29%	2.95%	4.43%
10 Years	STOCKS				BONDS	
	14.67%	6.75%	5.81%	12.19%	3.90%	4.44%

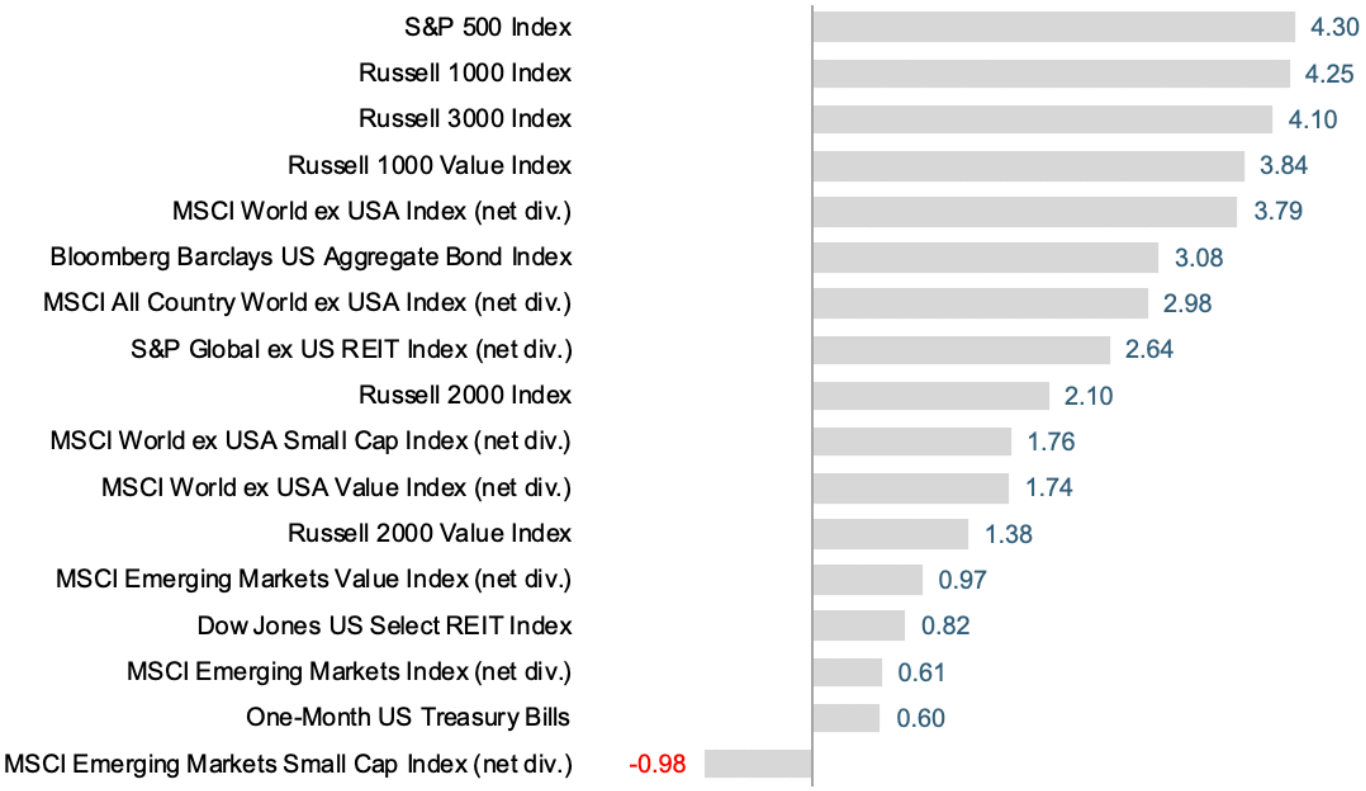
See important disclosure information

GLOBAL MARKETS - Second Quarter 2019 Index Returns (%)

Equity markets around the globe posted positive returns for the quarter. Looking at broad market indices, US equities outperformed non-US developed and emerging markets during the quarter.

Value stocks outperformed growth stocks in emerging markets but underperformed in developed markets, including the US. Small caps underperformed large caps in all regions.

REIT indices underperformed equity market indices in both the US and non-US developed markets



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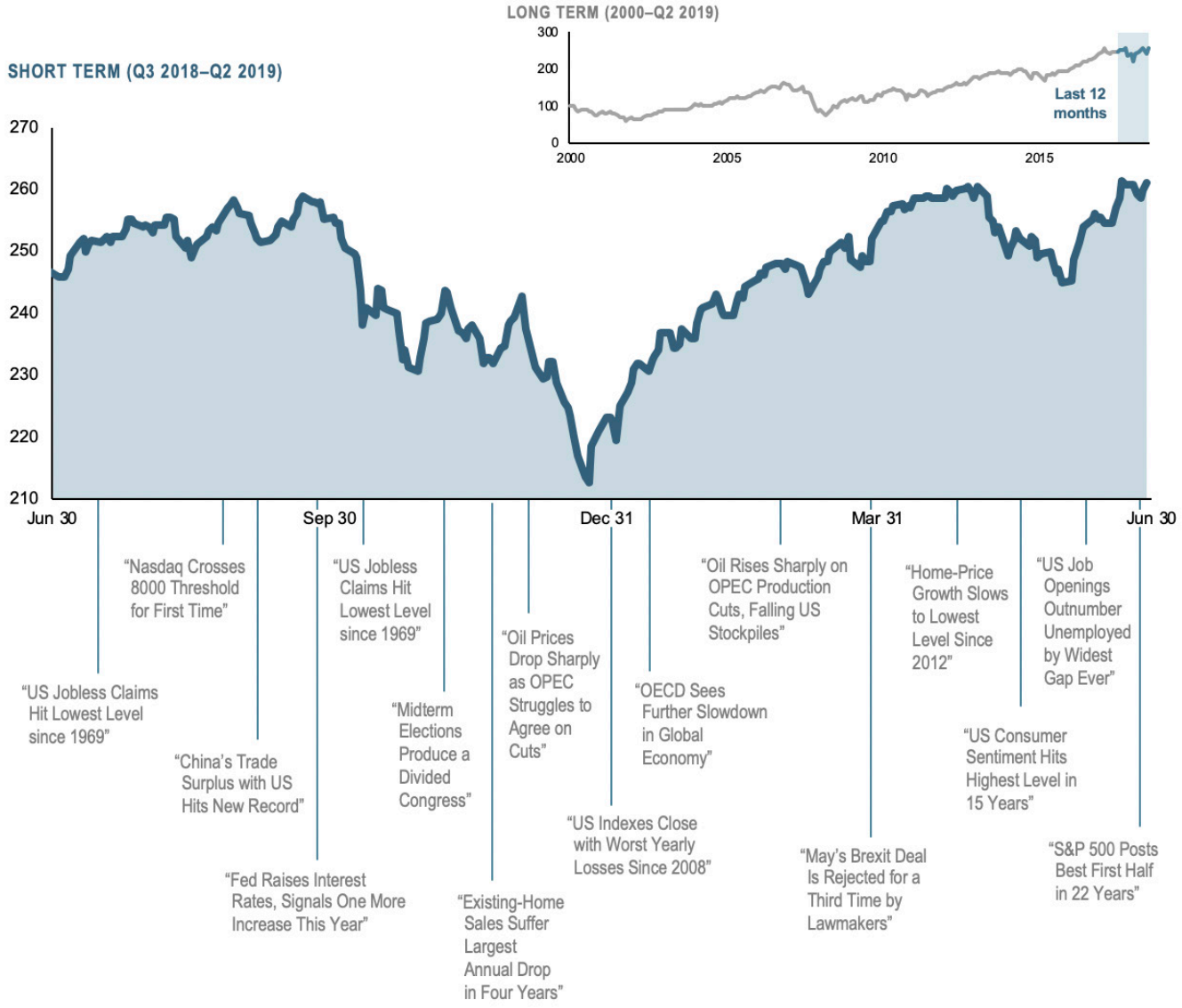
WORLD STOCK MARKET PERFORMANCE

MSCI All Country World Index with selected headlines from past 12 months

These headlines are not offered to explain market returns. Instead, they serve as a reminder that investors should view daily events from a long-term perspective and avoid making investment decisions based solely on the news.



Graph Source: MSCI ACWI Index [net div.]. MSCI data © MSCI 2019, all rights reserved. It is not possible to invest directly in an index. Performance does not reflect the expenses associated with management of an actual portfolio. Past performance is not a guarantee of future results.

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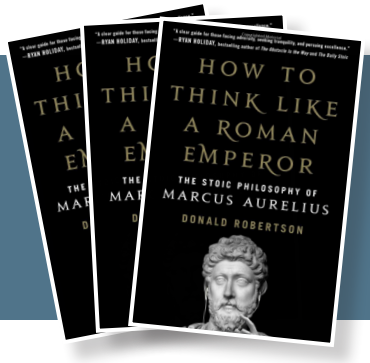
BOOK REVIEW



HOW TO THINK LIKE A ROMAN EMPEROR

by Donald Robertson

So I was reading a book of philosophy by Marcus Aurelius, the Second-Century Roman emperor . . .

(Seriously? Could you BE more pompous???)

No, wait, bear with me. Philosophy wasn't always an academic (some might say marginally relevant) exercise. The ancient Greeks and Romans viewed philosophy as a way of life, a set of guiding principles. Your philosophical view (much like religion today) dictated the rules by which you lived; it was a matter of life and (in the case of Socrates, for example) death.

In fact, Stoicism was a main inspiration for two forms of modern psychotherapy: Cognitive Behavioral Therapy (or "CBT") and its precursor, Rational Emotive Behavioral Therapy (or "REBT"). Both share with Stoicism the idea that our emotions are mainly determined by our beliefs. Change our beliefs and we change our emotions.

In the past few years, books on Stoicism have become more common. One of the best of these is How to Think Like a Roman Emperor: The Stoic Philosophy of Marcus Aurelius, by Donald Robertson. The book is designed to help the reader follow Marcus in acquiring Stoic strength of mind. According to Robertson, Stoics "can teach you how to find a sense of purpose in life, how to face adversity, how to conquer anger within yourself, moderate your desires, experience healthy sources of joy, endure pain and illness patiently and with dignity, exhibit courage in the face of your anxieties, cope with loss, and perhaps even confront your own mortality."

For those of you who are rusty on the classical education you got at Oxford, Marcus Aurelius was a Roman emperor for 17 years, beginning in 161 A.D., and Stoic philosopher. He was the last of the rulers traditionally known as the "Five Good Emperors," and the last emperor of the Pax Romana, an age of relative peace and stability for the Roman Empire. Marcus' reign was marked by military conflict in both the Eastern and Northern parts of the Empire. In between ruling the world and leading armies, Marcus wrote his Meditations, one of the few surviving (and possibly most influential) books on Stoicism from the Classical world.

Robertson's book follows the life events of Marcus: his childhood, his adoption into the imperial family, his training from several Roman philosophers of different schools, his rise to Emperor and his military exploits. At each point in Marcus' life, Robertson describes the evolution of his thought as reflected in the Meditations and the development of his strength of character despite or because of his many challenges and illnesses. Interspersed with this biography, Robertson also describes the development of Stoicism itself.

Stoics focus on the things that truly matter in life. While they were not ascetics (they knew wealth was preferable to poverty, health to sickness, life to death), they believed that such worldly benefits were good only if they were used wisely. Virtue, not wealth or happiness, was the only ultimate goal worth pursuing. "The Stoic Sage, or wise man, needs nothing but uses everything well." Stoics seek a sense of joy from living with wisdom and virtue; an aversion to vice through the pursuit of dignity and integrity; and the desire to help ourselves and others through friendship, kindness and goodwill.

Marcus went so far as to say that "life is opinion," that the quality of our life is determined by our value judgments, not external events (even changes in health) because those value judgments shape our emotions. Marcus sought inner peace through his own thoughts rather than pleasant surroundings; he "tells himself that resilience comes from his ability to regain his composure wherever he finds himself." In this way Marcus was able to maintain his own joy even during the many years he spent on the battlefield leading Roman legions.

Stoics work to limit the harm caused by physical or emotional pain in life: "complaining and chattering too much about our problems just makes them worse, and, more importantly, it harms our character." Instead, Stoics worked to separate their mind from the sensations causing the pain, believing that it was the judgment about the sensation rather than the sensation itself that is the most upsetting. Further, it is fear of pain that does more harm than the pain itself.

Stoics also maintain what Robertson calls a "reserve clause;" that is, the acknowledgment that our expectations should be reserved for what is in our actual control. As we work toward any external event (perhaps like a growth in our portfolio or getting to retirement), we must always be aware that the outcome is not entirely up to us. If you fail to act with such a reserve clause, then any failure to achieve an external goal becomes an evil, a source of distress. Instead, we can cope with such failures by trying to imagine as many different setbacks as possible that we might encounter as we pursue a goal, visualizing them in advance to take away the distress. For example, if there is a market downturn a year or two before you retire, you may have to put retirement off a while; visualize what that looks like and how you might cope with it (for example, by finding a part-time job that might be enjoyable).

Although Stoics often refer to the "Gods" as having the ultimate control over a person's destiny, Stoicism is not a religion. One could easily be a Stoic Christian, a Stoic Buddhist or a Stoic Muslim (in fact, reading Robertson's description of the philosophy demonstrates how much overlap there is between Stoicism and all of the world's religions).

Robertson, a trained psychologist, often describes the correspondence between classical Stoicism and modern psychotherapeutic techniques. He intersperses practical tips on how to incorporate a Stoic perspective into a person's life, through techniques like keeping a journal, perhaps listing qualities of people you admire (just as Marcus did in his own book). He also describes a "learning cycle," in which you prepare for the day ahead in the morning; try to live according to your values throughout the day; and then review your progress in the evening.

The relevance of Stoicism to investment philosophy is clear. It's an investor's thoughts about the markets, not the markets themselves, that is often the source of angst. Investors can control their asset allocations, but not the outcomes of those allocations. Developing a discipline in thinking about investments, one which includes visualizing negative outcomes in advance and therefore preparing for them, is hugely helpful for developing peace of mind.

Robertson's book is not perfect. He spends a great deal of time on Marcus' early development with mentors, not all of whom were Stoics. He also engages, toward the end of the book, in speculation about Marcus' feelings at the end of his life (which I found trite). And reading any secondary source is never as fulfilling as reading the Meditations themselves. Despite these reservations, however, Robertson's book is a very readable introduction to an approach to living that deserves much more attention, particularly in our own divided and often superficial age.

IMPORTANT DISCLOSURE INFORMATION

INVESTMENT AND INSURANCE PRODUCTS ARE: NOT FDIC Insured | NOT Bank Guaranteed | MAY Lose Value.

Past performance is not a guarantee of future results. Asset allocation does not guarantee better performance and cannot eliminate the risk of investment losses. Indices are not available for direct investment. Index performance does not reflect the expenses associated with the management of an actual portfolio.

Market segment (index representation) as follows: US Stock Market (Russell 3000 Index), International Developed Stocks (MSCI World ex USA Index [net div.]), Emerging Markets (MSCI Emerging Markets Index [net div.]), Global Real Estate (S&P Global REIT Index [net div.]), US Bond Market (Bloomberg Barclays US Aggregate Bond Index), and Global Bond ex US Market (Citi WGBI ex USA 1-30 Years [Hedged to USD]).

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