THE WAY 2 WEALTH®

ALL SEASON INVESTING

A GUIDE TO PROSPERING IN ANY MARKET ENVIRONMENT

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All Season Investing
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Introduction

Most of us have heard the Chinese curse: "May you live in interesting times." Though we certainly do live in interesting times, they are far from cursed. In many ways they are the best times the world has ever known: Global per capita gross domestic product (GDP) is at an all-time high, as is life expectancy, level of education, health care and human rights.[1] But while the world has made remarkable progress, it also faces remarkable threats from inflation to climate change, pandemics to deglobalization, quantitative tightening to the risk of an expanding hot war.

So are we headed toward ever greater freedom and prosperity, or into the lion's den of war and financial collapse?

If this report could reliably answer that question, it would be worth a lot more than its weight in gold. The curse of any moment in history—and possibly of this moment more than most—is that we don't know what will happen next. Uncertainty about the future is a fact of life. Because we don't know what to prepare for, decision-making can sometimes feel like a shot in the dark. But as Dwight D. Eisenhower said: "Neither a wise man nor a brave man lies down on the tracks of history to wait for the train of the future to run over him."

With regard to finances, many people try to avoid the train by dodging and weaving, changing their investment strategy every time the train shifts direction. This reactive approach rarely allows them to stay ahead of the economic curve as they run to catch up to the markets' latest fad.

But what if there were a way to position your finances so that you could not only avoid being run over by the train, but could prosper no matter which way it heads? We're not the first wealth managers to ponder this question.

We will discuss some of the better-known portfolio strategies for weathering good times and bad by the likes of value investing great Benjamin Graham, Nobel Prize winner Harry Markowitz, two-time Libertarian presidential nominee and investment advisor Harry Browne and billionaire hedge fund manager and historian Ray Dalio.

The All Season Portfolio reflects our admiration for all four. We have learned from each of their portfolio strategies, as well as from dozens of others. What we bring to the table, as outlined in this paper, is a simple way:

- To save, protect and grow the half of your money that you and your family rely on come hell or high water; and

- To individualize the growth half of your portfolio by discovering and investing in your personal Way2Wealth DNA.

[1] Angus Deaton, *The Great Escape: Health, Wealth, and the Origins of Inequality* (Princeton University Press, 2013).

Flow Not Force

So much of nature runs in cycles: the seasons, the tides … life itself. Although the patterns repeat, the particulars do not. The same can be said of the economy. Looking back, the cycles can be identified and mapped, but their timing and the form they take always vary, making it nearly impossible to predict when the next phase of the cycle will begin or just what it will look like.

Still, just as we can know that the seasons will change without knowing exactly how or when, so economists and historians can give us a rough idea of where we are in the economic cycle and what the next phase is likely to be. Mark Twain may have expressed it best when he said, "History doesn't repeat itself, but it often rhymes."

Many investors today have a sense that all is not right with the world, that change is in the air, though they may not be able to put their finger on why they feel that way or what the change will be. Economists such as the Austrians (*Box: Austrian Business Cycle Theory,* **below**) and historians such as hedge fund maestro Ray Dalio are in general agreement that our economic and historical season is about to change, and probably not for the better.

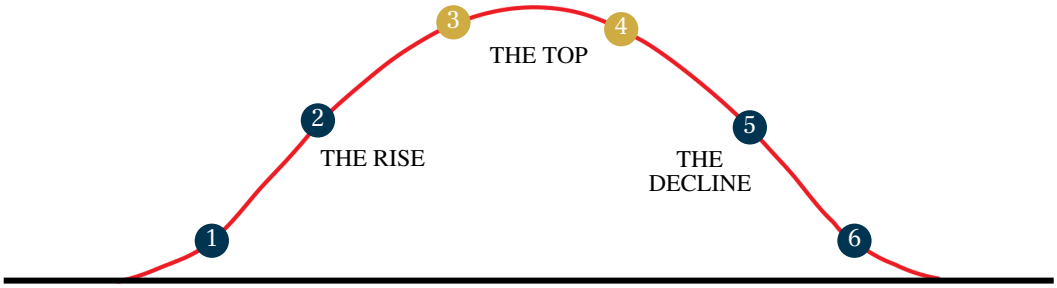
Dalio's latest book, *Principles for Dealing with the Changing World Order*, examines the rise and fall of nations and empires to identify predictable stages in that cycle (*Chart 1*, **next page**). His view is that the U.S. has entered "Stage 5: Bad financial conditions and intense conflicts."

Box: Austrian Business Cycle Theory

Despite its name, Austrian Business Cycle Theory is not a theory about how businesses operate in Austria. Rather, it was developed in the 1920s by economists Ludwig von Mises and Friedrich von Hayek, who were both—you guessed it—Austrian, to explain why most economies go through regular cycles of boom and bust. Von Hayek won the Nobel Prize in economics in 1974.

According to their theory, loose monetary policy by central banks combined with stimulative fiscal policy by governments leads to excess borrowing, which creates distortions in how companies and consumers allocate time and resources (malinvestment). Much of the excess borrowing is allocated to production that is misaligned with consumer demand or, worse, is non-productive.

Austrian economists see the inevitable correction (recession) that results from excess borrowing as a necessary reset, erasing the distortions it caused. Once the economy resets, the process tends to start all over again (*Chart B1*, **next page**).



1 New internal order and new leadership

2 Resource-allocation systems and government bureaucracies are built and refined

3 Peace and prosperity

4 Excesses and widening of wealth and other gaps

5 Bad financial conditions and intense conflicts

6 Civil wars and revolutions

Chart 1: Ray Dalio's Typical Big Empire Cycle (Simplified Version).
Source: Ray Dalio, *Principals for Dealing with the Changing World Order.*

Nor is he alone in that assessment. Mark Thornton, an Austrian economist and Senior Fellow at the Mises Institute writes: "A decade of artificially low, near zero interest rates and trillions of dollars of quantitative easing, not to mention … the trillions added to federal debt and even negative interest rates and oil prices, would suggest that this is not the moment to go all in." [2]

Even if their warnings prove to be mistaken, volatility and uncertainty remain the watchwords of our current economic environment. So what is an investor to do?

In the Aesop's fable *The North Wind and the Sun*, those two forces of nature vie to see which is more powerful by attempting to remove a man's cloak.

Austrian economists acknowledge that a correction can sometimes be staved off by even greater stimulus to the economy. The lowering of interest rates, increased money printing and fiscal measures undertaken in the U.S. in response to the 2008 financial crisis and later to the COVID-19 pandemic are two recent examples of this. However, according to Austrian Business Cycle Theory, such stimulus only postpones the inevitable recession and makes it worse once it arrives.

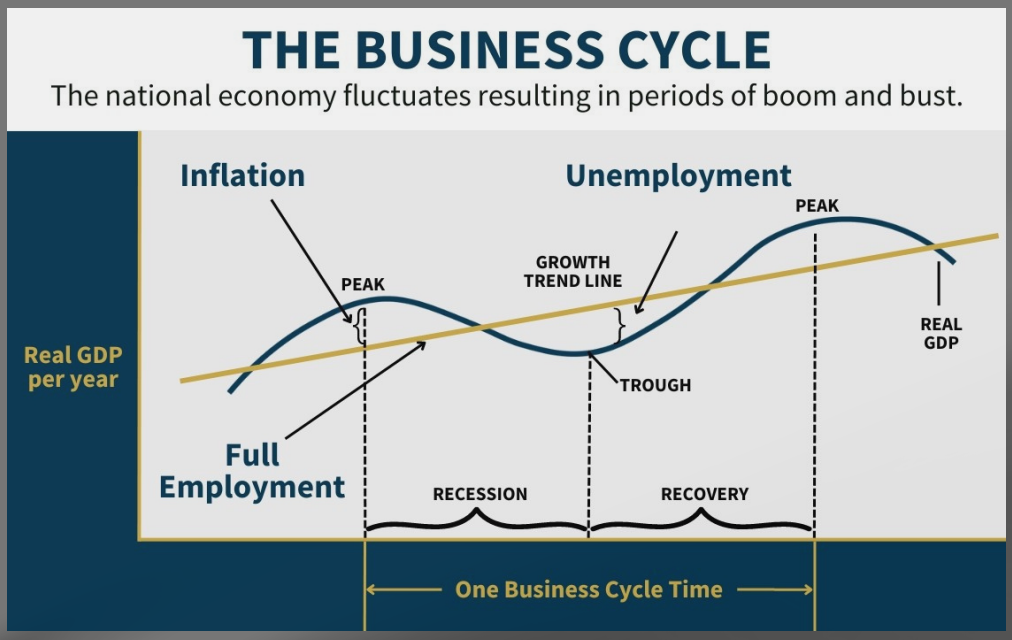


Chart B1: The Austrian Business Cycle.
Source: MisesIndia.in

[2] Mark Thornton, "Austrian School Scholars Are Right to Be Worried about This Economy," *Mises Wire*, May 4, 2020 (mises.org).

First, the north wind blows ferociously at the cloak to tear it away from the man, but he only pulls it more tightly around himself. Then, the sun beams gently down on him until he warms up enough to take it off of his own accord.

In investing, as in nature, it often makes more sense to work with existing conditions than to fight them. Permaculture attempts to apply lessons learned from natural cycles to agriculture and land management in order to create a thriving, sustainable ecosystem that requires little if any intervention. Some especially astute economists and investors have taken a similar approach to economic cycles, crafting strategies that work with those cycles to maximize sustainable returns without having to rely on market timing or shifting asset allocations.

Here is a brief overview of some of their portfolio strategies:

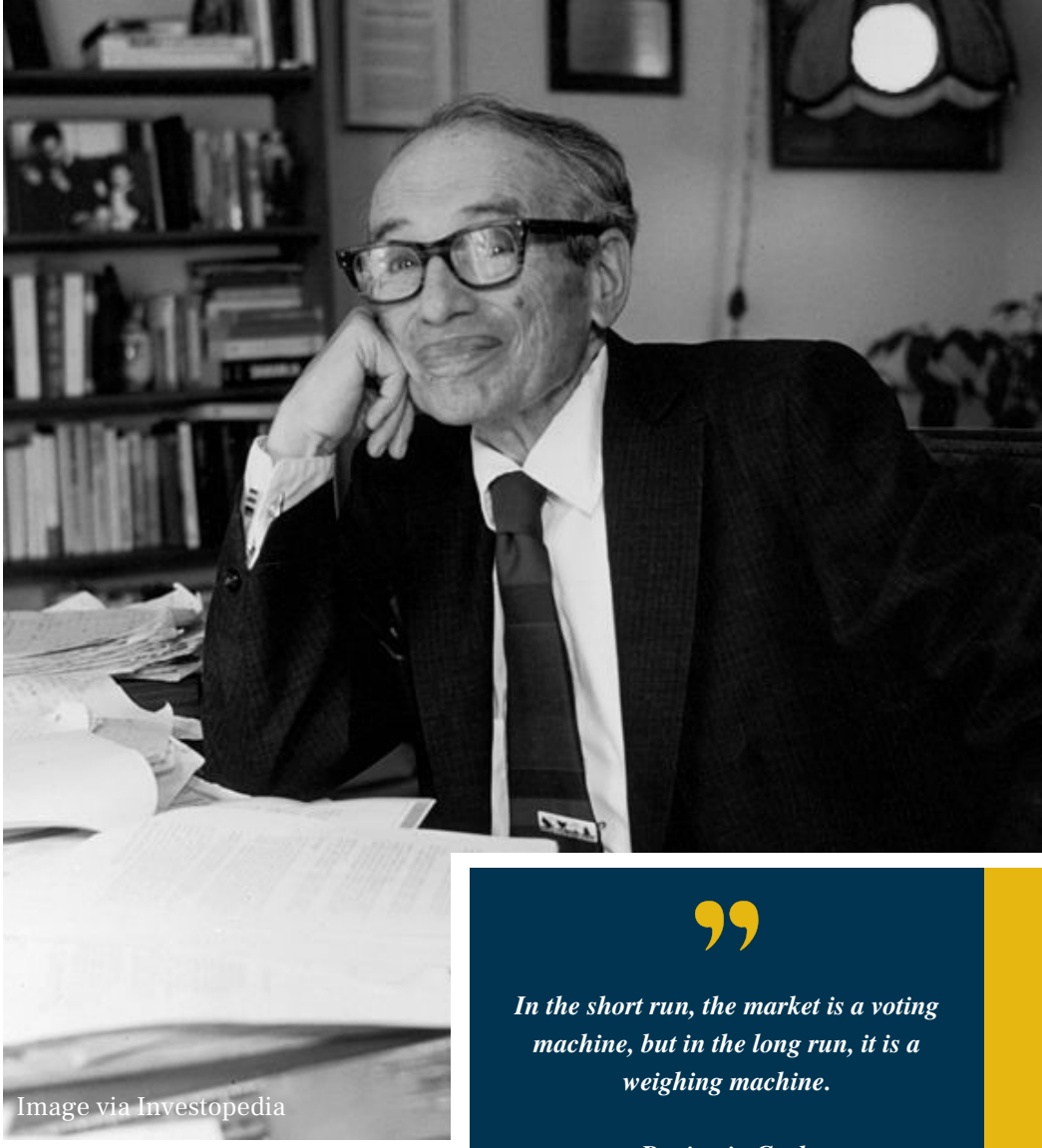


Image via Investopedia

> *In the short run, the market is a voting machine, but in the long run, it is a weighing machine.*
>
> *— Benjamin Graham*

Foundational Portfolio Strategies

SECURITY ANALYSIS AND THE 50/50 ALLOCATION

In his 1949 book, *The Intelligent Investor*, value investing great Benjamin Graham, whom Warren Buffet cites as his mentor, suggested that investors should have no less than 25% and no more than 75% of their investable assets in stocks, with the remainder in bonds.

The range allowed for adjustments depending on economic and market conditions, but since he did not believe that investors could successfully time the markets, he concluded that in practice the best allocation was 50% stocks and 50% bonds. Given that both stocks and bonds were still selling at deep discounts in the wake of the Great Depression and World War II, this allocation model was hard to fault.

Graham's earlier book on fundamental stock analysis, *Security Analysis*, remains the go-to text for how to pick individual stocks.

However, by 1976 Graham had concluded that, given the sheer number of securities analysts then plying their trade, the limited potential rewards of individual stock analysis no longer justified the cost and effort.[3] In that sense, he embraced the efficient markets hypothesis propounded by Harry Roberts in 1967, which proposed that all available information is immediately reflected in stock prices such that neither fundamental nor technical analysis of individual securities (Alpha, or unsystematic risk) can generate returns in excess of those of an asset class as a whole (Beta, or systematic risk).

[3] "A Conversation with Benjamin Graham," (*Financial Analysts Journal*, September-October 1976).

MODERN PORTFOLIO THEORY

The founder of Modern Portfolio Theory (MPT), Harry Markowitz, also focused on markets in their entirety rather than on individual securities within those markets. In his 1952 dissertation, *Portfolio Selection* (and his later book of the same name), he calculated that the optimal risk/return ratio for a portfolio consisting of a broadly diversified basket of U.S. stocks and U.S. bonds is 60% stocks and 40% bonds.

MPT provided a mathematical tool for investors to determine how to maximize their returns for a given level of risk. It revolutionized portfolio construction and won Markowitz a share in the 1990 Nobel Prize in economics. The 60/40 allocation became the touchstone for how to maximize investment returns.

One important consideration for designing a portfolio that does well during all phases of the economic cycle is to choose assets with low or negative correlation. Assets that tend to rise and fall together (positively correlated assets) reinforce positive returns when economic conditions favor them but also reinforce losses when they don't. Choosing assets that do well under different economic conditions (negatively correlated assets) helps smooth out returns in a portfolio, making it less volatile.

While stocks and bonds had a low correlation in the 1950s, it has become less and less consistent in recent years, with positive correlations increasingly common during periods of economic stress.[4] This has made the 60/40 allocation less useful for portfolio diversification. MPT also assumes an unlimited time horizon, taking no account of when an investor might need to draw down some of his or her invested assets.

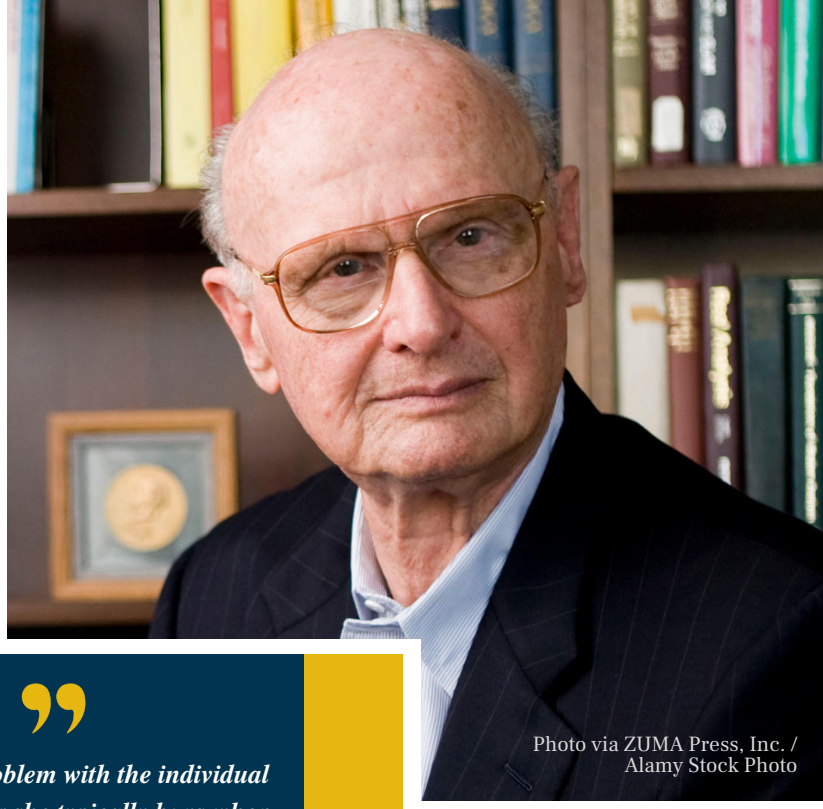


Photo via ZUMA Press, Inc. / Alamy Stock Photo

> ***"The chief problem with the individual investor: He or she typically buys when the market is high and thinks it's going to go up, and sells when the market is low and thinks it's going to go down."***
>
> ***- Harry Markowitz***

THE PERMANENT PORTFOLIO

In the 1980s, wealth advisor and two-time Libertarian presidential candidate Harry Browne took the 60/40 allocation a step further. While he agreed that stocks had a place in his portfolio for periods of prosperity and long-term bonds for periods of deflation, he wanted to come up with a balance of assets that would perform well during all phases of the economic cycle. Since both stocks and bonds tend to fall during recessions (especially in what he called "tight-money recessions" caused by the central bank raising interest rates in a weak economy) and during periods of inflation, he added two asset classes.

[4] "A Brief History and Outlook for Traditional 60/40 Investment Portfolios," (tfafunds.com).

His Permanent Portfolio (*Chart 2*, **below**) as put forward in his book *Fail-Safe Investing* consists of 25% domestic stocks by way of a diversified index fund, 25% long-term Treasury bonds with maturities of 25 to 30 years, 25% physical gold for inflationary periods and 25% cash (Treasury bills) for tight-money recessions. He recommended buying the assets all at once to avoid the pitfalls of market timing and using Treasuries and index funds to maximize tax efficiency while minimizing selection and default risk.

He also expected gold to outperform in times of political uncertainty, currency crisis and negative real interest rates. Cash could do double duty to buffer investors from having to sell assets in down markets and to assist in rebalancing the portfolio—which he recommended whenever any of the four asset classes rose above 35% or fell below 15%. It's probably a good thing that the cash had more than one job to do since, after a certain overall funding level, there would be a lot of it.

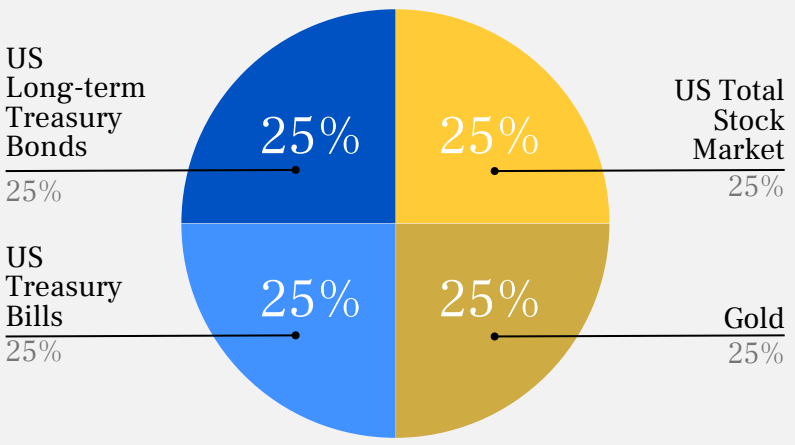


Chart 2. Harry Browne's Permanent Portfolio.
Source: Craig Rowland and J.M. Lawson, *The Permanent Portfolio: Harry Browne's Long-Term Investment Strategy.*


Photo via quotesgram.com

"When you know you're capable of dealing with whatever comes, you have the only security the world has to offer."

- Harry Browne

THE ALL WEATHER PORTFOLIO

Hedge fund billionaire and historian Ray Dalio and his team at Bridgewater Associates approached the problem of portfolio construction from the perspective of risk.[5] They determined that: Return = Cash + Beta + Alpha. The Cash rate is determined by the central bank and so is out of the investor's control; Beta (the returns of an asset class) rises over time relative to Cash; and Alpha (the returns of individual securities within an asset class) is a zero-sum game in that when some securities within an asset class outperform, others must underperform to an equal extent.

Since his All Weather Portfolio was originally intended for his family trust assets, it was designed to rely entirely on Beta for growth. The conundrum was how to control risk in order to achieve the best net positive return for Beta relative to Cash over time.

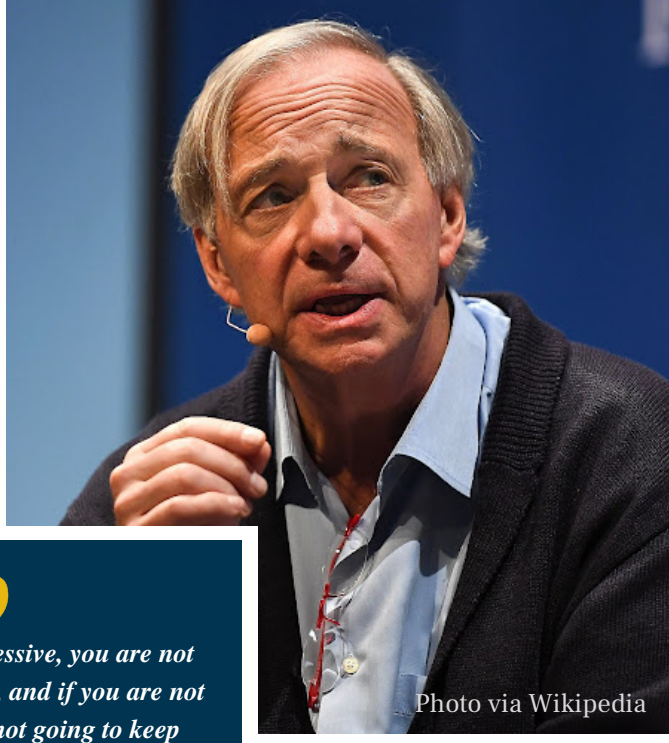


Photo via Wikipedia

> ***"If you are not aggressive, you are not going to make money, and if you are not defensive, you are not going to keep money."***
>
> ***— Ray Dalio***

Dalio identified the two main drivers of economic risk as the volume of economic growth, and inflation (the pricing of that growth). He then assessed which asset classes do well as growth and inflation rise or fall relative to expectations (*Chart 3*, **below**). These four quadrants of economic risk correspond closely to the four economic conditions identified by Harry Browne.

	GROWTH	INFLATION
RISING ↑	Higher than expected economic growth	Higher than expected inflation
FALLING ↓	Lower than expected economic growth	Lower than expected inflation

Chart 3: Ray Dalio's Four Risk Environments.
Source: Tony Robbins, *The End of the Bull Market.*

[5] "The All Weather Strategy," (Bridgewater Associates, 4Q, 2009).

In analyzing the 60/40 portfolio, Dalio concluded that nearly all of the portfolio's risk came from the 60% allocation to stocks. Part of the reason is because most corporations carry a hefty burden of debt, so that investing in them amounts to buying a leveraged asset. He found that by leveraging long bonds, he could give them a similar risk/reward profile to equities for the purpose of risk management.

In 1996, the All Weather Portfolio finally took shape after 25 years of development.[6] The asset allocation Dalio recommends to successfully ride out the four periods of economic risk is significantly more complex than either the 60/40 allocation or the Permanent Portfolio. It also relies on sophisticated financial instruments not available to the average investor in addition to hedged and leveraged positions.

Motivational speaker and author Tony Robbins persuaded Dalio to create an unleveraged, retail investor–friendly version of the All Weather Portfolio that is shown in *Chart 4* (**below**). Dalio recommends rebalancing the modified portfolio at least annually.

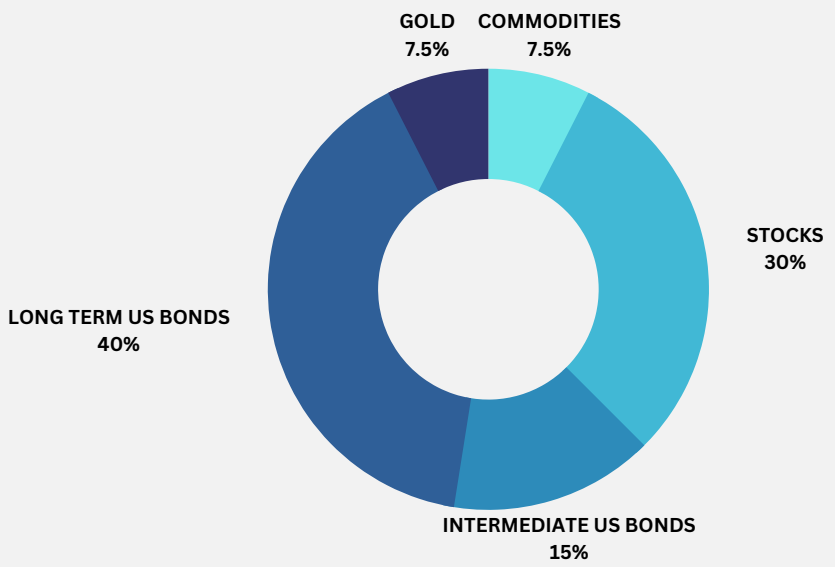
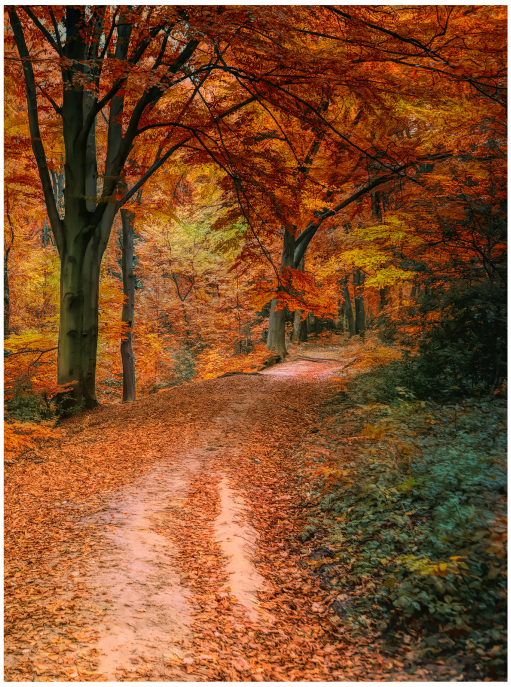


Chart 4: Ray Dalio and Tony Robbin's All Season strategy.
Source: Tony Robbins, *Money: Master the Game.*

Dalio also created a separate Safety Portfolio to which he recommends shifting assets when Bridgewater's Depression Gauge falls below a certain level, as it did in 2008 and 2009. This safety portfolio suggests that in practice he considers the All Weather Portfolio a Most Weather Portfolio not quite suited to all economic conditions.

[6] "The All Weather Story," (bridgewater.com, January 2012).

The All Season Portfolio



Warren Buffet has said: "I never have the faintest idea what the stock market is going to do in the next six months, or the next year, or the next two." Trying to predict the next move in the markets is almost irresistible, but if the greatest investor of our time can't do it, chances are neither can you. Your best bet is to participate in the long-term growth of the economy while protecting against downside risk.

That last bit, "protecting against downside risk," is more important than most people realize. The fact is that you need to achieve a 100% gain to make up for a 50% loss, so avoiding loss through the careful selection and diversification of assets is an essential part of staying ahead of the curve.

BOX: WHAT TO LOOK FOR IN A WEALTH ADVISOR

Wealth is more than money. It is more, even, than the Merriam Webster definition of "an abundance of valuable material possessions or resources." The word's origin provides a clue: "Wealth" comes from the Middle English "wele," meaning "well-being." Well-being can be achieved at almost any level of income or net worth, but not having to worry about money is an important precondition. Because your wealth advisor can have a real and direct influence on your well-being, it's important to choose wisely. Some questions to ask include:

- **Are they a fiduciary?** – Fiduciaries are legally bound to put your interests before their own.
- **Are their fees transparent?** – Your advisor should be forthcoming about how they get paid, with information on fees, commissions and other expenses readily available.
- **Do they have experience?** – Make sure they have the appropriate licenses, certifications and credentials as well as experience with clients whose circumstances are comparable to your own.
- **Are they approachable and communicative?** – Look for someone committed to regular meetings who is responsive to your questions and concerns and will consult you regarding changes to your financial plan.
- **What is their investment approach?** – Your advisor should be able to clearly lay out their investment philosophy and resources.

All of those are important considerations for choosing a wealth advisor. But given that you are entrusting them with your well-being, your financial future and your legacy to your children and grandchildren, you have every reason to expect more than the essentials. To help ensure a superior outcome, choose an advisor who is prepared to:

- **Bring your goals forward** – Much of financial planning is focused on future goals such as retirement, paying for college and wealth transfer. Planning for the future is vital, but not at the expense of neglecting your present needs. Your advisor should be focused on helping you achieve an exceptional "now" as well as a comfortable "later."
- **Get your whole story** – Many advisors are eager to start implementing a plan after a few brief questions and calculations. Look for someone who will listen to your aspirations and concerns and will thoroughly understand your unique circumstances before they start to make recommendations.
- **Provide a cohesive, collaborative team** – No single financial professional, no matter how capable, can craft and implement an effective plan in a vacuum. It takes a team.

  Even when advisors reach out to other professionals such as accountants and attorneys, too often the result is less than a coordinated effort. Having a cohesive team of experts that is used to working together and is unified behind your goals is the best way to make those goals a reality.
- **Make education a part of the process** – Finance should be as fundamental to our educational system as the "three Rs." Sadly, that is not the case. Entrusting your finances to someone without fully comprehending what they are doing is an uncomfortable experience. That's why it's important to find an advisor who makes education an integral part of the planning process. You deserve to understand the tax, estate, income, risk/reward and other implications of your financial plan before it is put into practice.

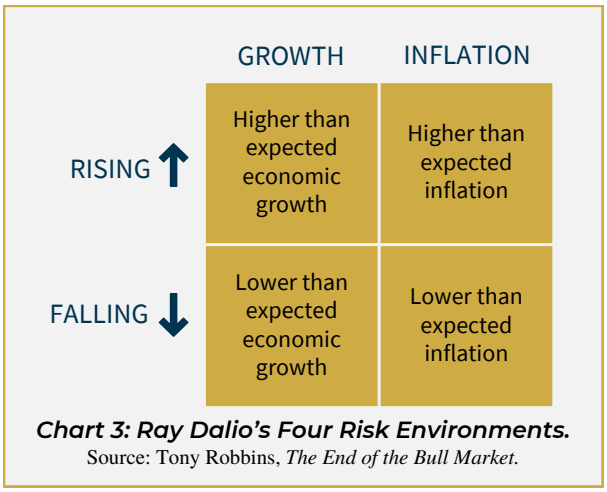
The best financial advisors will work with you in all of the above ways to develop and monitor a comprehensive plan that addresses your financial needs and objectives. That may seem like a lot to ask, but where the security and well-being of you and your family are concerned, you can't afford to settle for less.

GROWTH WITH SAFETY

These two principles—long-term growth and loss reduction—are the foundation of the All Season Portfolio.

Many people believe that both cannot be achieved in the same portfolio, but as we have seen above, they can. The widely accepted maxim that higher risk investments have a higher potential reward neglects to mention that there are many ways to deleverage the risks. For example diversification, especially using uncorrelated assets, can help limit the downside.

Compared to the All Weather Portfolio, and even the Permanent Portfolio, the All Season Portfolio is both simpler and more flexible. The All Season Portfolio takes as its starting point the risk quadrants of the All Weather Portfolio and overlays the asset allocation quadrants of the Permanent Portfolio (*Chart 5*, **below**), but with a broader choice of assets.



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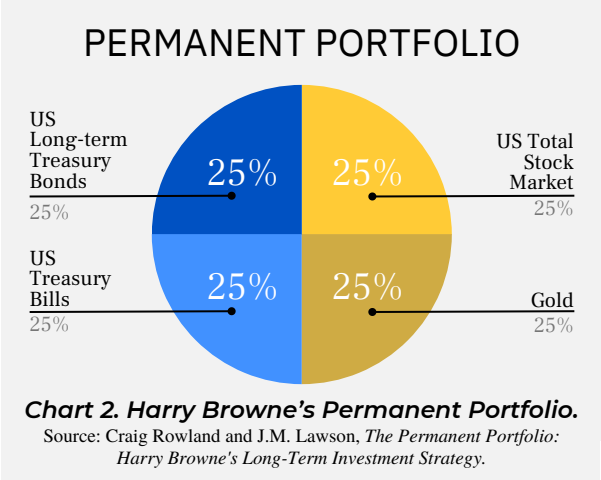

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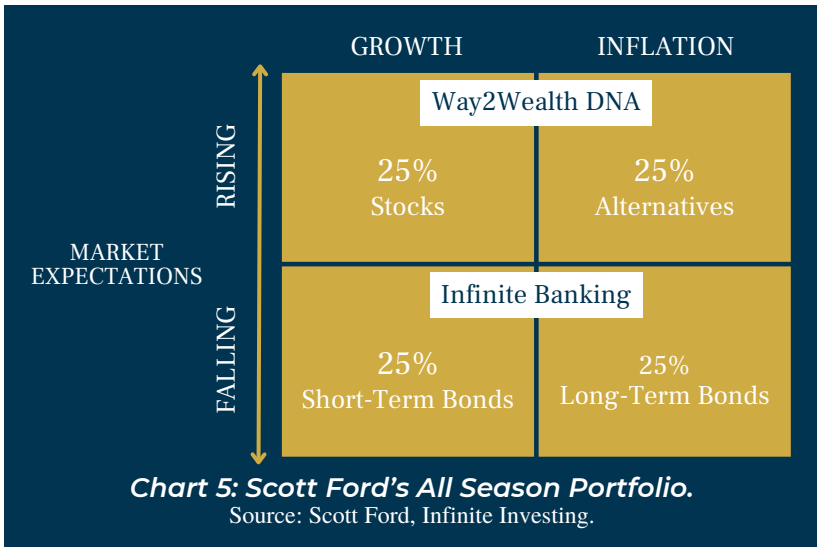

Chart 5: Scott Ford's All Season Portfolio.
Source: Scott Ford, Infinite Investing.

Let's take a closer look at how the All Season Portfolio achieves growth with safety, one risk quadrant and asset class at a time.

SPRING AND SUMMER

We are strong believers in diversification in the interest of maximizing Beta (the growth of an asset class over cash) while minimizing the risks associated with picking individual stocks and assets (Alpha). At its simplest and safest, the upper half of the All Season Portfolio risk chart can be invested in low-cost, broad-based stock funds for the rising growth quadrant (25% Stocks) and low-cost, broad-based commodities funds, real estate investment trust (REIT) funds, Treasury Inflation Protected Securities (TIPS) and gold for the rising inflation quadrant (25% Alternatives).

Way2Wealth DNA

However, we also believe that if you have an area of specialized knowledge or expertise, it can make sense to diversify a portion of the two upper quadrants into assets that reflect your strengths. These allocation decisions are best informed by what we call your "Way2Wealth DNA." It starts with investing in yourself.

Much investment risk comes not so much from the investments themselves as from the investor. Research suggests that individual investors lose 3.8% in returns every year due to aggressive trading in response to market volatility.[7] In other words, the average investor tends to buy high and sell low.

Choosing a first-rate financial advisor (*Box: What to Look for in a Wealth Advisor,* **page 11**) is a giant step toward removing this type of risk. A study by Vanguard shows that working with a wealth advisor can boost your annual investment returns by 3.75%.[8]

Educating yourself about your money is another way to reduce investor risk and provide greater agency over your finances, even when you work with an advisor: Understanding breeds competence. Other ways to invest in yourself include professional education to boost your career, such as attaining advanced certifications and licensing, or investing in your business to make it more efficient and profitable.

A second way to use your Way2Wealth DNA to diversify the rising growth quadrant of your portfolio is to direct at least some of those assets toward attractive investment opportunities that fall within your sphere of capability. Finally, if you know a particular field inside and out, you may want to use your Way2Wealth DNA to acquire direct or participating ownership in promising companies in that field.

[7] Brad M. Barber, et al., "Just How Much Do Individual Investors Lose by Trading?" (*The Review of Financial Studies*, February 2009).
[8] Francis M. Kinniry Jr, CFA et al., "Putting a Value on Your Value: Quantifying Vanguard Advisor Alpha," (advisors.vanguard.com, July 2022).

For higher net worth investors, assigning a portion of your equity allocation to private equity can provide further diversification along with tax advantages and the potential for excess returns. A report by Cambridge Associates indicates that a minimum private equity allocation of 15% is the sweet spot for excess returns and that diversifying among several private equity funds can substantially reduce the risk of capital loss.[9] For clients interested in exploring this option, Carson Wealth can provide access to select private equity platforms.

For the 25% alternatives quadrant, taking advantage of your Way2Wealth DNA can broaden your choices to include, say, land, income-producing real estate or art.

Aligning Your Money With Your Values

It may also make sense to allot some of these "upper half" assets to areas that are important to you for reasons that go beyond the strictly financial. Reaching your goals is priority one, but doing so can be especially satisfying when your investments are aligned with your values. This can matter not only for how you feel about yourself and the world around you, it can also turn out to be a sound investment approach. For example, 88% of impact investors—those who seek investments to optimize a goal other than profit—report that their portfolios meet or exceeded their financial performance expectations.[10] Though money carries no intrinsic set of values, it can be a useful tool for expressing our values. Whatever your convictions and beliefs may be, taking them into account when you weigh your financial decisions provides the opportunity to do well by doing good. Knowing that your investments support your beliefs also makes it easier to sit tight during periods of market volatility.

All of the above stratagems are geared toward the helping you "think like an owner," a signal attribute of successful investors. While your Way2Wealth DNA and aligning your money with your values can expand your asset choices for the 25% stocks and 25% alternatives quadrants (and to some extent for the "lower half" quadrants discussed next), maintaining those asset allocations and diversifying within them remains key.

[9] Maureen Austin, David Thurston, William Prout, "Private Investing for Private Investors: Life Can Be Better After 40(%)," (cambridgeassociates.com, February 2019).
[10] Chen, James, "Impact Investing Explained: Definitions, Types, and Examples," (investopedia.com, July20.2022).

FALL AND WINTER

The lower half of the All Season Portfolio risk/asset allocation chart shows 25% short-term bonds for the falling growth risk quadrant and 25% long-term bonds for the falling inflation (deflation) risk quadrant. These can be satisfied by a combination of short-term and long-term Treasury bonds, short-term and long-term corporate bonds, Treasury or corporate bond funds or laddered CDs, depending on your timeframe, tax situation, objectives and risk tolerance.

While these are excellent asset choices for those quadrants, they serve here as a sort of shorthand for the kinds of assets that should be used.

A recent study by Roger Ibbotson, a Professor at the Yale School of Management best known for his pioneering work on asset allocation, shows that a fixed indexed annuity with a 60% participation rate (share of positive performance of, in this case, the S&P 500 Index) and a 0% floor (the minimum index-linked interest rate you can earn) outperformed long-term bonds in a 60/40 portfolio while providing better downside protection.[11] This offers an alternative to long-term bonds for investors who have a very low risk tolerance. It could even be used to replace a portion of the 25% equity allocation for those who are wary of wading back into a volatile stock market.

Infinite Banking

For most investors, however, experience has taught us that the Infinite Banking Concept (IBC) is the most effective way to satisfy both of the lower-half risk quadrants (*Box: The Infinite Banking Concept*, **page 17**). A study by Wade Pfau, PhD, CFA, and Michael Finke, PhD, CFP, Professor and Dean respectively of the American College of Financial Services, shows that funding a whole life policy results in a better income stream in retirement than "buy term and invest the difference," where the difference is invested in a target date fund within a 401(k).[12]

11 Roger G. Ibbotson, PhD, "Fixed Indexed Annuities: Consider the Alternative," (Zebra Capital Management, LLC, January 2018).
12 Wade D. Pfau, PhD, CFA, and Michael Finke, PhD, CFP, "Integrating Whole Life Insurance into a Retirement Income Plan," (Wealth Building Cornerstones, LLC, April 2019).

Infinite Banking serves the same function as both short-term and long-term bonds, but with several advantages over direct bond ownership. Although more than 75% of the typical mutual life company's portfolio is invested in long-term bonds,[13] with the IBC:

- The cash value of the policy does not decline when interest rates rise.
- It is highly tax efficient.
- Your insurance company receives a steady stream of funds to invest in long- and short-term bonds, reducing interest-rate risk.
- The cash value is non-callable.
- It includes a death benefit.

Just as importantly, the rising cash value of the policy gives you unprecedented control over your money and can serve as your personal bank, one that you own and use as you see fit. Bank loans are far more expensive than the interest rate alone would suggest. Not only do you have to qualify for the loan and go through a lengthy approval process, there are also points, fees and other expenses. And of course, if you don't keep up with your payments, penalties accrue, and your collateral (home, car, etc.) may eventually be foreclosed on to pay back the loan.

When you borrow against the cash value of your policy, by contrast, there are no points, fees or expenses, no approvals, qualifications or appraisals required. In addition, you determine the loan amount, up to the cash value of your policy, as well as the repayment schedule and amounts. Best of all, the cash value that you have borrowed against continues to earn interest and dividends and to increase your death benefit. Some far-sighted individuals extend the advantages of the IBC to their entire families to create a "family bank" as outlined in the next section of this paper.

No less a genius than Albert Einstein said, "Compound interest is the eighth wonder of the world. He who understands it, earns it; he who doesn't, pays it." Nothing torpedoes the magic of compounding like negative returns, or even flat returns. To quote Warren Buffet: "Never forget that anything times zero is zero…. If you do anything that gives you the chance of having a zero in there, it'll all turn to pumpkins and mice." Interrupting the flow of compound returns amounts to the same thing as a zero. A properly structured IBC allows you to continue to earn uninterrupted compound interest on the cash value of your policy at

[13] Robert McMenamin, Anna Paulson, Thanases Plestis, and Richard Rosen, "What Do U.S. Life Insurers Invest in?" (The Federal Reserve Bank of Chicago, *Chicago Fed Letter*, April 2013).

BOX: THE INFINITE BANKING CONCEPT

> *"It never dawns on most financial gurus that you can control the financial environment in which you operate. Perhaps it is caused by lack of imagination, but whatever the cause, learning to control it is the most profitable thing you can do over a lifetime."*
>
> *— Nelson Nash*

Photo via Nelson Nash Institute

Developed by Nelson Nash in the early 1980s, the Infinite Banking Concept (IBC) is an innovative method for using the special tax, savings and growth attributes of high-premium, dividend paying mutual whole life insurance to help you become your own banker while increasing your wealth and ensuring the financial security of your loved ones.

That's a pretty big claim. Here's how it works:

By definition, mutual life insurance companies are owned by their policyholders and can pay tax-free dividends (return of premiums) on the cash value of the policy. By structuring the policy to maximize the cash value rather than the death benefit, and by reinvesting the dividends to buy paid-up additions (PUAs), the cash value can quickly increase to the point that you can use it to fund purchases of consumer goods—or of anything else. Once withdrawals exceed the amount of dividends paid, you can borrow against the cash value of the policy without the hassle and inconvenience, not to mention the points and fees, of getting a loan from a bank. Getting a loan against your cash value is easy because the death benefit of the policy, which is always more than the cash value while the policy is in effect, serves as your collateral. This also means that your house, car or other valuable belongings will never be foreclosed on or repossessed. You are in control of how much you borrow and when you borrow it as well as your repayment schedule and amounts. Try that with a bank or finance company!

If you repay the policy loan at the same rate you would repay an equivalent loan from a bank, your cash value will grow even faster. Soon you will be able to finance bigger purchases, such as cars or even a house, with policy loans. If you own a business, you can also buy fixtures and equipment for it using policy loans and then lease them to your company. If structured properly, such transactions can have significant tax benefits.

In the meantime, as long as you keep up with your premiums and pay back your loans, your policy becomes an increasingly efficient savings vehicle and your tax-free dividends and interest payments on those savings grow ever larger. Of course, because you are accomplishing all of this with a life insurance policy, the death benefit of which also increases with PUAs, you have the peace of mind of knowing that if anything happens to you, your loved ones will be provided for. ∞

the same time that you have access to those funds for other needs or opportunities.

Mutual life companies are also notably safe and well capitalized, some with more than 200 years of continuous operation under their belts. Mutual life companies hold an average of $107 of reserves for every $100 of future obligations.[14]

The Family Bank

At the beginning of World War II. the young John Templeton (later Sir John Templeton), another student of Benjamin Graham's who would become a legendary investor in his own right, saw an opportunity. World markets were hammered by uncertainty, and Templeton, believing that the war would finally pull the U.S. out of the Great Depression, bought 100 shares of all the stocks on the New York and American stock exchanges selling for $1 or less—104 stocks in all. That nearly a third of the underlying companies were in bankruptcy at the time didn't keep him from making a 400% profit on the trade, with an average holding period of just four years.[15]

The well-connected Templeton was able to borrow much of the capital he needed (well over $200,000 in today's money) to jump on this opportunity, but how many of us have had to forego opportunities in our personal, professional, business or investing lives due either to a lack of ready funds or the risk to the security of our families that borrowing them would entail? There has to be a better way—and there is.

Extending the IBC to every member of your family to create a family bank can be a powerful tool for giving you and your loved ones the wherewithal to seize opportunities when they arise. This is not a new idea. The Rothschilds set up a family bank to perpetuate their wealth in the 1700s, and the Rockefellers have used a family bank to help preserve their wealth over seven generations and counting.[16] That countless other well-to-do families have set up family banks is not surprising given that it makes cash flow and capital available to every member of the family without risking the family's financial well-being—and you don't have to be a Rothschild or a Rockefeller to do it.

Establishing a properly structured, dividend-paying mutual whole life policy for each member of your family, then putting a governance structure in place for the use and repayment of the cash flow and the policy loans, are the first steps in setting up your own family bank. Cash flow from the policies and loan repayments can be directed to further capitalize the bank when not required for other needs, and loans against cash value can be used by family members for education, starting or expanding a business, buying a house and myriad other opportunities.

In the meantime, the cash value that serves as collateral on the loans continues to earn dividends and interest, making this a useful strategy for satisfying the Fall and Winter quadrants of the All Season Portfolio. Structuring your family bank within an irrevocable life insurance trust (ILIT) can provide additional tax advantages and protect its assets from creditors.

Cash flow and control are the crux of the lower half of the All Season Portfolio, and a family bank is an excellent vehicle for providing an abundance of both, not only now, but for generations to come.

Once both upper and lower half assets have been apportioned, the allocations should be revisited every year by you and your advisor and rebalanced as appropriate. Annual rebalancing shifts resources from asset classes that have outperformed to those that have underperformed in order to maintain the desired allocation ratio. It has also been shown to decrease volatility and reduce downside risk. [17]

[14] Rachel Marshall, "Infinite Banking, Part7: What Is a Life Insurance Policy Loan?" (themoneyadvantage.com, October 24, 2022).
[15] Fernand, Larissa, "John Templeton: How to be a Bargain Hunter," (morningstar.in, May 9, 2014).
[16] Gunderson, Garrett, "Tips for Setting Up Your Own Family Bank," (forbes.com, July 21, 2020).
[17] Amy C. Arnott, CFA, "Why Rebalancing (Almost Always) Pays Off," (morningstar.com, July 2020).

Conclusion

Uncertain times require creative solutions to wealth management. We have traced the development of portfolio construction over the past hundred years by the economists, historians and investors who have endeavored to come to terms with how best to position assets to prosper throughout the rhyming cycles of economic activity.

Each new portfolio strategy has built on the discoveries of those that came before as the theme of growth with safety has been pursued with increasing sophistication. The All Season Portfolio makes no attempt to reinvent the wheel. Instead, it structures tried-and-true methods for achieving growth with safety using a flexible framework designed to accommodate each individual's financial strengths and requirements.

The All Season Portfolio not only grows and protects your assets, it can also lower your taxes and borrowing costs and put you fully in control of your banking needs. At the same time, it provides the liquidity and flexibility necessary to take advantage of opportunities that arise from your specialized knowledge and skillset. ∞

Afterward: The Way2Wealth

We look at the challenge of growing and protecting your wealth from a slightly different perspective in our The Way2Wealth® program. As part of The Way2Wealth process, we approach the question of asset allocation and diversification using the bucket concept first advanced by wealth manager Harold Evensky in 1985.

In our version, three buckets represent money earmarked for use over three different timeframes (*Chart 5*, **below**)

Chart 5: Scott Ford's Way2Wealth Bucket Strategy.
Source: Scott Ford, The Way2Wealth.

The first bucket represents Savings in the form of safe, liquid assets available to cover at least one year's worth of living expenses. Many investors' eyes glaze over at the mention of savings, which all too often provide low returns that are taxable as income. Yet savings serves as a crucial financial backstop when other sources of income fail, or as a buffer against having to sell other assets when you need cash for unexpected expenses.

As we've seen in this white paper, savings don't need to be boring: They can provide a good compound rate of return that won't get nibbled to death by taxes. Some people mistakenly believe that their investments can function as savings, but savings and investments are not the same thing. What sets savings apart is that they are liquid (readily convertible to cash) and are not subject to loss. Additional funds in the Savings bucket can also serve as a war chest for when opportunity knocks.

The second, Income, bucket represents holdings that produce income sufficient to cover at least some portion of living expenses for ten years—ideally 100% of living expenses for life. This bucket is especially important in retirement, when many people suddenly lose the paycheck they have relied on their entire adult lives. Social security and retirement distributions can only take up so much of the slack. Filling the income bucket is all about maximizing cash flow and control.

Remaining funds fill the third bucket, devoted to Growth assets with a timeframe of ten years or more. Inflation erodes the buying power of your money. You see it in action every time you go to the gas pump or the grocery store. Long-term ownership of assets that can keep up with or, better yet, outpace inflation, such as stocks, real estate and commodities, is the best way to ensure that the money you invest today will continue to grow in real, inflation-adjusted, terms.

The All Season Portfolio is used to determine the asset allocations for implementing the bucket strategy. The Savings bucket is funded by the kinds of assets discussed in the Fall and Winter section of the All Season Portfolio, such as bonds, CDs and the IBC. The Income bucket can be filled either by those lower-half assets, or by upper-half assets such as income-producing real estate, business distributions, annuities and dividend-paying stocks. Assets in the Growth bucket come from the upper half of the chart, informed by your Way2Wealth DNA. Tax-free, tax-deferred and taxable strategies are used to minimize that nemesis of all investor returns: taxes.

While The Way2Wealth uses a different starting point than the All Season Portfolio, the endpoint remains the same: growth with safety. By giving you the tools you need to reach financial independence through financial wisdom, we help take the stress out of investing and make money simple, so that you can focus on living now. ∞

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New York Times bestselling author Scott Ford (RFC) is Managing Director of Carson Wealth, a financial advisory and wealth management firm with dozens of locations nationwide. Scott's teams provide comprehensive wealth management designed to bring clarity and simplicity to the complex issues of financial management using the proprietary Way2Wealth® process.

Scott is also Chairman of the Four Worlds Global Impact Fund of the Four Worlds International Institute, an organization dedicated to sharing the wisdom and knowledge of First Nation Peoples in the service of building a single human family.

He and his wife, Angie, live on a farm in West Virginia where they practice permaculture and beekeeping. They have two grown children and four grandchildren.