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INVESTMENT NEWSLETTER

> Focusing on what you can control can lead to a better investment experience.

KEY QUESTIONS FOR THE LONG-TERM INVESTOR

NOVEMBER 2017
Dimensional Fund Advisors

Whether you've been investing for decades or are just getting started, at some point on your investment journey you'll likely ask yourself some of the questions below. Trying to answer these questions may be intimidating, but know that you're not alone. Your financial advisor is here to help. While this is not intended to be an exhaustive list it will hopefully shed light on a few key principles, using data and reasoning, that may help improve investors' odds of investment success in the long run.

1. What sort of competition do I face as an investor?

The market is an effective information-processing machine. Millions of market participants buy and sell securities every day and the real-time information they bring helps set prices. This means competition is stiff and trying to outguess market prices is difficult for anyone, even professional money managers (see question 2 for more on this). This is good news for investors though. Rather than basing an investment strategy on trying to find securities that are priced "incorrectly," investors can instead rely on the information in market prices to help build their portfolios (see question 5 for more on this).

World Equity Trading in 2016 (daily average)

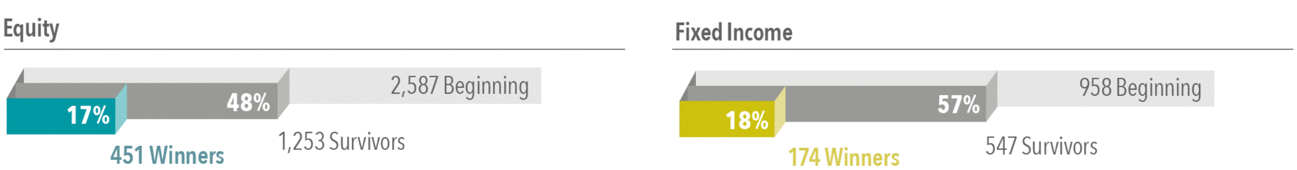
Number of Trades	Dollar Volume
82.7 MILLION	$346.4 BILLION

Source: World Federation of Exchanges members, affiliates, correspondents, and non-members. Trade data from the global electronic order book. Daily averages were computed using year-to-date totals as of December 31, 2016, divided by 250 as an approximate number of annual trading days.

2. What are my chances of picking an investment fund that survives and outperforms?

Flip a coin and your odds of getting heads or tails are 50/50. Historically, the odds of selecting an investment fund that was still around 15 years later are about the same. Regarding outperformance, the odds are worse. The market's pricing power works against fund managers who try to outperform through stock picking or market timing. One needn't look further than real-world results to see this. Based on research*, only 17% of US equity mutual funds and 18% of fixed income funds have survived and outperformed their benchmarks over the past 15 years.

US-Based Mutual Fund Performance, 2002–2016



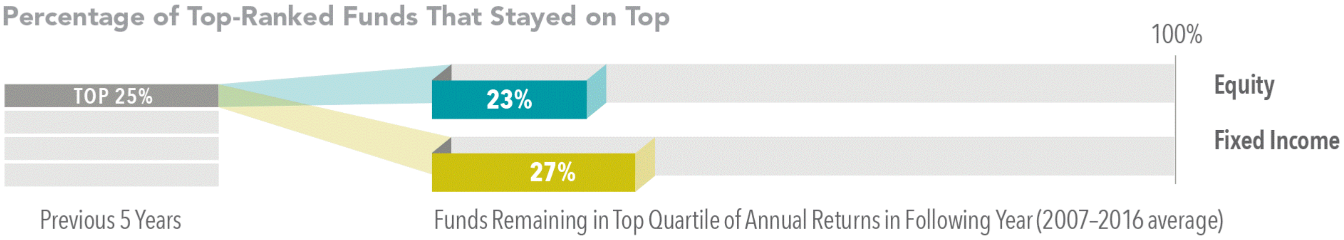
Source: *Mutual Fund Landscape 2017, Dimensional Fund Advisors. See Appendix for important details on the study. Past performance is no guarantee of future results.

Canandaigua National Bank & Trust

3. If I choose a fund because of strong past performance, does that mean it will do well in the future?

Some investors select mutual funds based on past returns. However, research shows that most funds in the top quartile (25%) of previous five-year returns did not maintain a top-quartile ranking in the following year. In other words, past performance offers little insight into a fund's future returns.

Percentage of Top-Ranked Funds That Stayed on Top

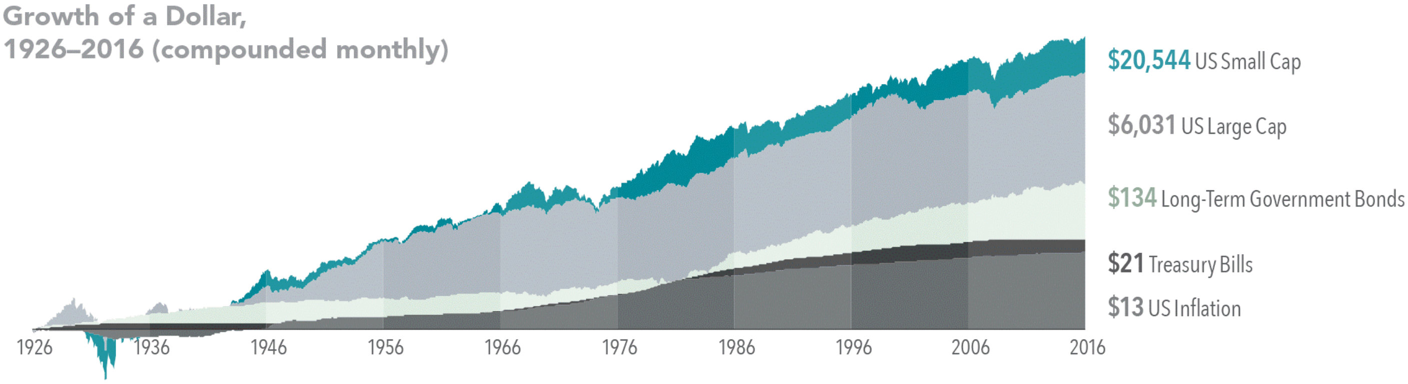


Source: *Mutual Fund Landscape 2017, Dimensional Fund Advisors. See Appendix for important details on the study. Past performance is no guarantee of future results.

4. Do I have to outsmart the market to be a successful investor?

Financial markets have rewarded long-term investors. People expect a positive return on the capital they invest, and historically, the equity and bond markets have provided growth of wealth that has more than offset inflation. Instead of fighting markets, let them work for you.

Growth of a Dollar, 1926–2016 (compounded monthly)

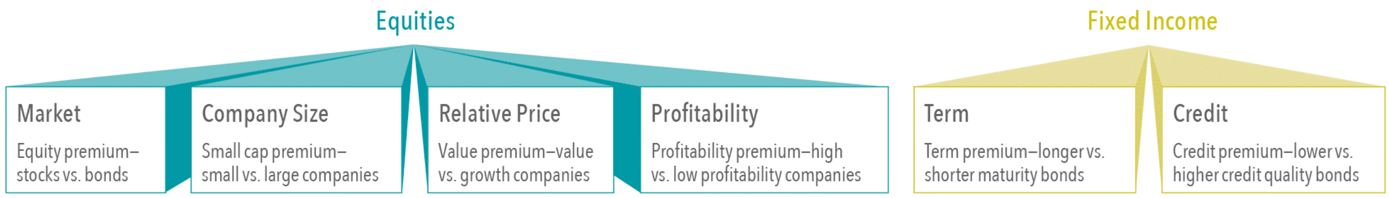


US Small Cap is the CRSP 6–10 Index. US Large Cap is the S&P 500 Index. Long-Term Government Bonds is the IA SBBI US LT Govt TR USD, provided by Ibbotson Associates via Morningstar Direct. Treasury Bills is the IA SBBI US 30 Day TBill TR USD, provided by Ibbotson Associates via Morningstar Direct. US Inflation is measured as changes in the US Consumer Price Index. US Consumer Price Index data is provided by the US Department of Labor Bureau of Labor Statistics. CRSP data is provided by the Center for Research in Security Prices, University of Chicago. The S&P data is provided by Standard & Poor's Index Services Group. Indices are not available for direct investment. Index performance does not reflect the expenses associated with the management of an actual portfolio. Past performance is no guarantee of future results.

5. Is there a better way to build a portfolio?

Academic research has identified these equity and fixed income dimensions, which point to differences in expected returns among securities. Instead of attempting to outguess market prices, investors can instead pursue higher expected returns by structuring their portfolio around these dimensions.

Dimensions of Expected Returns



Relative price is measured by the price-to-book ratio; value stocks are those with lower price-to-book ratios. Profitability is a measure of current profitability based on information from individual companies' income statements.

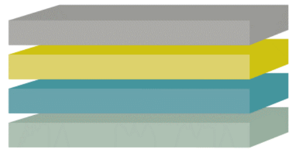
6. Is international investing for me?

Diversification helps reduce risks that have no expected return, but diversifying only within your home market may not be enough. Instead, global diversification can broaden your investment opportunity set. By holding a globally diversified portfolio, investors are well positioned to seek returns wherever they occur.

Home Market Index Portfolio

S&P 500 Index
1 Country, 500 stocks

Global Market Index Portfolio



MSCI ACWI
Investable Market Index (IMI)
46 countries, 8,628 stocks

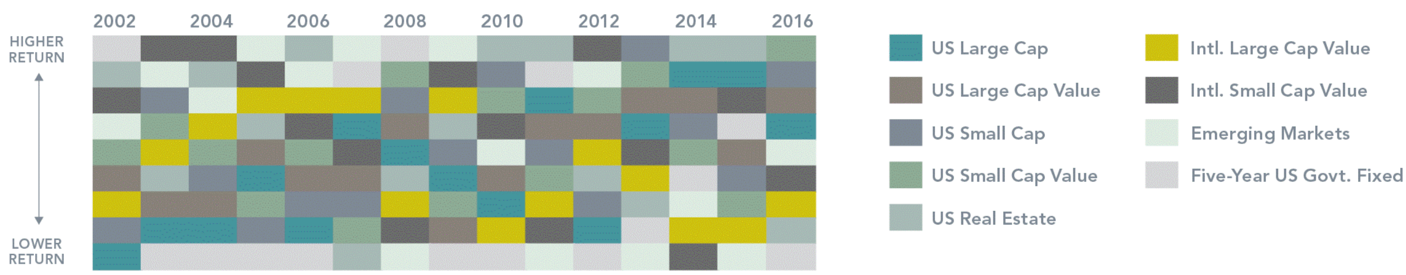
Number of holdings and countries for the S&P 500 Index and MSCI ACWI (All Country World Index) Investable Market Index (IMI) as of December 31, 2016. The S&P data is provided by Standard & Poor's Index Services Group. MSCI data ©MSCI 2017, all rights reserved. International investing involves special risks such as currency fluctuation and political stability. Investing in emerging markets may accentuate those risks. Diversification does not eliminate the risk of market loss. Indices are not available for direct investment

7. Will making frequent changes to my portfolio help me achieve investment success?

It's tough, if not impossible, to know which market segments will outperform from period to period.

Accordingly, it's better to avoid market timing calls and other unnecessary changes that can be costly. Allowing emotions or opinions about short-term market conditions to impact long-term investment decisions can lead to disappointing results.

Annual Returns by Market Index



US Large Cap is the S&P 500 Index. US Large Cap Value is the Russell 1000 Value Index. US Small Cap is the Russell 2000 Index. US Small Cap Value is the Russell 2000 Value Index. US Real Estate is the Dow Jones US Select REIT Index. International Large Cap Value is the MSCI World ex USA Value Index (net dividends). International Small Cap Value is the MSCI World ex USA Small Cap Value Index (net dividends). Emerging Markets is the MSCI Emerging Markets Index (net dividends). Five-Year US Government Fixed is the Bloomberg Barclays US TIPS Index 1–5 Years. The S&P data is provided by Standard & Poor's Index Services Group. Frank Russell Company is the source and owner of the trademarks, service marks, and copyrights related to the Russell Indexes. Dow Jones data provided by Dow Jones Indices. MSCI data ©MSCI 2017, all rights reserved. Bloomberg Barclays data provided by Bloomberg. Indices are not available for direct investment. Index performance does not reflect the expenses associated with the management of an actual portfolio. Past performance is no guarantee of future results.

8. Should I make changes to my portfolio based on what I'm hearing in the news?

Daily market news and commentary can challenge your investment discipline. Some messages stir anxiety about the future, while others tempt you to chase the latest investment fad. If headlines are unsettling, consider the source and try to maintain a long-term perspective.

9. **So, what should I be doing?**

Work closely with a financial advisor who can offer expertise and guidance to help you focus on actions that add value. Focusing on what you can control can lead to a better investment experience.

- Create an investment plan to fit your needs and risk tolerance.
- Structure a portfolio along the dimensions of expected returns.
- Diversify globally.
- Manage expenses, turnover, and taxes.
- Stay disciplined through market dips and swings.

APPENDIX

Question 2: The sample includes US-based funds at the beginning of the 15-year period ending December 31, 2016. Each fund is evaluated relative to the Morningstar benchmark assigned to the fund's category at the start of the evaluation period. Surviving funds are those with return observations for every month of the sample period. Winner funds are those that survived and whose cumulative net return over the period exceeded that of their respective Morningstar category benchmark.

Question 3: At the end of each year, funds are sorted within their category based on their five-year total return. Funds in the top quartile (25%) of returns are evaluated again in the following year based on one-year performance in order to determine the percentage of funds that maintained a top-quartile ranking. The analysis is repeated each year from 2007–2016. The chart shows average persistence of top-quartile funds during the 10-year period.

Questions 2 and 3: US-domiciled open-end mutual fund data is from Morningstar and Center for Research in Security Prices (CRSP) from the University of Chicago. Index funds and fund-of-funds are excluded from the sample. Equity fund sample includes the Morningstar historical categories: Diversified Emerging Markets, Europe Stock, Foreign Large Blend, Foreign Large Growth, Foreign Large Value, Foreign Small/Mid Blend, Foreign Small/Mid Growth, Foreign Small/Mid Value, Japan Stock, Large Blend, Large Growth, Large Value, Mid- Cap Blend, Mid-Cap Value, Miscellaneous Region, Pacific ex-Japan Stock, Small Blend, Small Growth, Small Value, and World Stock. Fixed income fund sample includes the Morningstar historical categories: Corporate Bond, Inflation-Protected Bond, Intermediate Government, Intermediate-Term Bond, Muni California Intermediate, Muni National Intermediate, Muni National Short, Muni New York Intermediate, Muni Single State Short, Short Government, Short-Term Bond, Ultrashort Bond, and World Bond. For additional information regarding the Morningstar historical categories, please see "The Morningstar Category Classifications" at morningstardirect.morningstar.com/ clientcomm/ Morningstar_Categories_US_April_2016.pdf. See Dimensional's "Mutual Fund Landscape 2017" for more detail. Benchmark data provided by Bloomberg Barclays, MSCI, Russell, Citigroup, and S&P. Bloomberg Barclays data provided by Bloomberg. MSCI data © MSCI 2017, all rights reserved. Frank Russell Company is the source and owner of the trademarks, service marks, and copyrights related to the Russell Indexes. Citi fixed income indices © 2017 by Citigroup. The S&P data is provided by Standard & Poor's Index Services Group.

Source: Dimensional Fund Advisors LP.

Indices are not available for direct investment. Their performance does not reflect the expenses associated with the management of an actual portfolio. Past performance is not a guarantee of future results. Diversification does not eliminate the risk of market loss.

There is no guarantee investment strategies will be successful. Investing involves risks including possible loss of principal. Investors should talk to their financial advisor prior to making any investment decision.

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CATCHPHRASE INVESTING

NOVEMBER 2017
Dimensional Fund Advisors

The financial media is drawn to catchphrases, acronyms, and buzzwords that can be sold as the new thing. FAANG (Facebook, Apple, Amazon, Netflix, and Google) is the latest of these. But does this constitute an investment strategy?

For journalists, commentators, and marketers, acronyms like FAANG are useful. They fit easily into headlines and they appeal to a feeling among some investors that their portfolios should match the "zeitgeist" or spirit of the age.

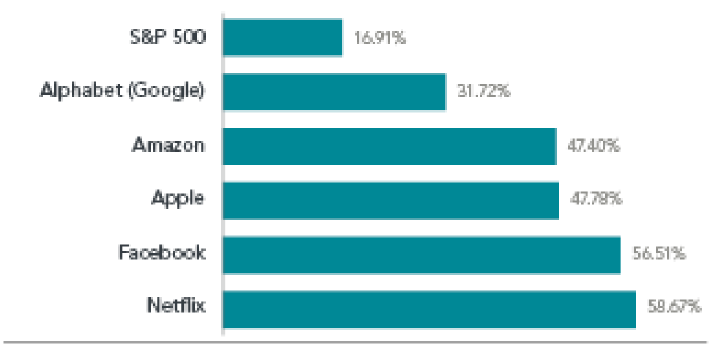
But as we'll see, investment trends tend to come and go. This is not to downplay the transformative nature of new technologies and the possibilities they present. But as an investor, it is wise to recall that all those hopes and expectations are already built into prices.

The FAANG acronym has become particularly popular in 2017 as returns from the five members of the unofficial club have far outpaced the wider market. Exhibit 1 shows the total year-to-date returns of the FAANG members compared to the S&P 500.

Such is the public interest in the tech giants that the parent company of the New York Stock Exchange recently launched the NYSE FANG+TM Index that includes the quarterly futures contracts of the FAANG members apart from Apple (hence only one "A"), plus another five actively traded technology growth stocks.

Exhibit 1: Total Returns

Year to date as of October 31, 2017



So, does this mean, as some media gurus suggest, that you should reweight your portfolio around these tech names? After all, these companies have fundamentally reshaped traditional sectors like newspapers, television, advertising, music, and retailing.

For investors, there are a few ways of answering that question, none of which involve denying the significant influence Facebook, Amazon, Apple, Netflix, Google, and other technology names are having on our lives.

Firstly, market leadership is constantly changing based on a myriad of influences, including shifts in the structure of the global economy, commodities, technology, demographics, consumer tastes, and supply factors. Trying to build an investment strategy by anticipating these forces is like trying to catch lightning in a bottle.

In the 1960s, the then often-quoted Nifty Fifty of solid, buy-and-hold blue-chips included such names as Xerox, Eastman Kodak, IBM, and Polaroid, all of which were disrupted in one way or another by newer, more nimble competitors in the following decades.

By the late 1990s, the media was full of stories about the dot-coms, companies that were building new businesses using the transformative power of the internet. A handful of those companies (Amazon, for instance) fulfilled their promise. Many others (retailer Boo.com, prototype social network TheGlobe.com, and pet supplies firm Pets.com were just three examples) crashed and burned.

In the mid-2000s, the focus turned to companies with a large exposure to the so-called BRIC economies, an acronym based on the fast-growing emerging economies of Brazil, Russia, India, and China.

Several financial services companies even set up BRIC products, with mixed degrees of success. One investment bank, having argued that the superior growth for emerging economies justified a bias to stocks exposed to these markets, ending up closing its BRIC fund in late 2015 after years of poor returns.[1]

1 "Goldman Closes BRIC Fund," The Wall Street Journal, November 9, 2015.
2 The "All stocks" portfolio consists of all eligible stocks in all eligible developed and emerging markets. The portfolio for January to December of year t includes stocks whose free float market capitalization as of December t-1 is greater than $10MM in developed markets and $50MM in emerging markets and with non-missing price returns for December of year t-1. Annual portfolio returns are value-weighted averages of the annual returns on the included securities. The portfolios "Excluding the top 10%" and "Excluding the top 25%" are constructed similarly. Individual security data are obtained from Bloomberg, London Share Price Database, and Centre for Research in Finance. The eligible countries are: Australia, Austria, Belgium, Brazil, Canada, Chile, China, Colombia, Czech Republic, Denmark, Egypt, Finland, France, Germany, Greece, Hong Kong, Hungary, India, Indonesia, Ireland, Israel, Italy, Japan, Republic of Korea, Malaysia, Mexico, Netherlands, New Zealand, Norway, Peru, Philippines, Poland, Portugal, Russia, Singapore, South Africa, Spain, Sweden, Switzerland, Taiwan, Thailand, Turkey, United Kingdom, and the United States. Diversification does not eliminate the risk of market loss. Past performance is no guarantee of future results.

So, while individual sectors each can have their time in the sun, it is not clear that weighting your portfolio toward an industry currently in favor is a sustainable long-term strategy.

A second way of looking at this issue is that accepting it is difficult to pick winning sectors does not mean you should exclude these zeitgeist stocks in a diversified marketwide portfolio. You can still own them, but you do so by casting a much wider net.

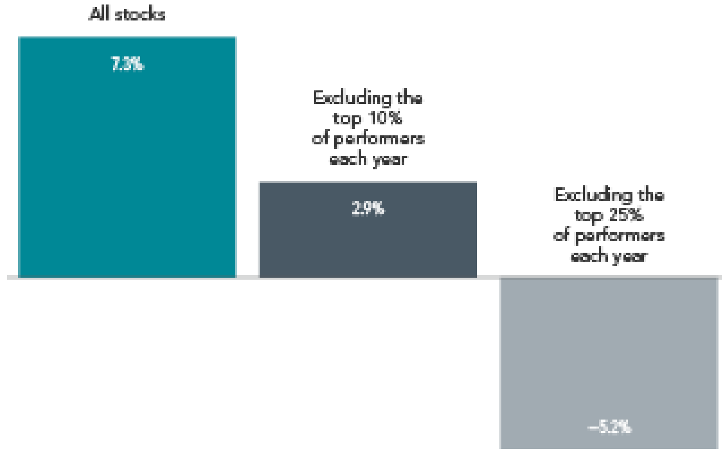
The more concentrated the portfolio, the more you are exposed to idiosyncratic forces related to individual stocks or sectors. Being highly diversified means you can still benefit from the broad trends driving technology or whatever is leading the market at any one time, but you are doing so in a more prudent manner.

Put another way, by diversifying you are not only reducing the risk of placing too much of a bet on one sector, you are improving the odds of holding the best performers. Look at Exhibit 2, which shows what would have happened if you had excluded the top 10% and top 25% of market performers in a global portfolio from 1994–2016.

We've seen that even professional investors can find it tough to pick which sector will lead the market from year to year.

Exhibit 2: Diversification May Prevent You From Missing Opportunity[2]

Compound average annual returns: 1994–2016



It's true that technology companies like Amazon and Facebook have performed well recently. But it is worth recalling that current prices already contain future expectations about those companies. We don't know what future prices will be because these will reflect information we haven't received yet. Because no one has a reliable crystal ball, a better approach is to diversify. That way we increase the odds of being positioned in the next big winning sector without chasing hot trends or latching on to cute-sounding acronyms.

Source: Dimensional Fund Advisors LP.

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HOW YOUR INVESTMENT INCOME IS TAXED

TIMOTHY STRAUTS
MORNINGSTAR

While this is by no means an exhaustive list, it covers some of the main categories of income-producing investments and how the income they produce is generally treated by the IRS at tax time.

Please note, though, that because every investor's tax situation is unique, you should consult your accountant for verification of your tax status and tax treatment of any investment product mentioned below. Also, we won't go into capital gains taxes in this article because the tax treatment of them is largely the same regardless of asset class.

STOCKS WITH QUALIFIED DIVIDENDS

For most stocks that pay qualified dividends, the tax treatment is pretty straightforward: Investors would report the income on a 1099-DIV in the Qualified Dividends box. Investors in the 10% and 15% brackets will have a zero tax rate on dividends. For individuals in income tax brackets greater than 15% but less than 39.6%, qualified dividends are taxed at 15%. Individuals in the 39.6% tax bracket are subject to a 20% tax on dividends. Higher-income taxpayers are also subject to a 3.8% Medicare surtax on investment income.

In order to be a 'qualified dividend,' the dividend must be issued by a U.S. corporation or a foreign company that either trades on a U.S. exchange, such as an ADR, or is eligible for benefits under a U.S. tax treaty.

Note that in order for the dividend to be 'qualified,' you must have owned the investment for at least 60 days of the 121-day period that begins 60 days before the ex-dividend date, or the day the stock trades without the dividend priced in.

FOREIGN STOCKS WITH NONQUALIFIED DIVIDENDS

If you're considering a foreign stock for a taxable account, do your homework on whether the company's dividends are qualified. You can find out more about this by consulting IRS Publication 17.

PREFERRED STOCK

In many (but not all) cases, preferred-stock dividends are treated as qualified dividend income for tax purposes, even though they have many bondlike characteristics, such as a stated par value and fixed coupon.

Some dividends paid by U.S. companies are not eligible for lower tax rates, however. Here are a few examples:

REITS

Real estate investment trusts do not pay income taxes at the corporate level, but they are required to pay annually at least 90% of their taxable income in the form of shareholder dividends, which is one reason they pay out such large dividends.

Different types of REIT payments are taxed at different rates. In the majority of cases, REIT dividends are considered nonqualified and taxed at ordinary income rates; therefore, they are probably best held in a tax-advantaged account. But there are other types of income payments, such as those distributed from taxable REIT subsidiaries or out of long-term capital gains, which could be subject to lower tax rates; investors should consult with their tax advisors in these cases.

MLPS

Master limited partnerships are partnerships that trade on a public exchange. They may offer certain tax benefits but also some tax complexity. Unlike with REITs, however, it is best to hold MLPs in a taxable account, because owning them in a tax-deferred account can result in something called unrelated business taxable income, which then requires the account to pay taxes.

MLPs pass through their taxable income to unitholders, who then pay taxes on that income at their own marginal tax rates, often only when the units are sold. These can be a little complicated at tax time, owing to the fact that you don't use a 1099 form to report the distributions but instead have to use a K-1.

Another interesting feature of MLPs is that cash distributions are not directly taxable: The IRS looks at them as returns of capital, so it reduces the investor's cost basis in the MLP. In practical terms, that means that the investor will have to pay taxes on the spread between a lower cost basis and the MLP's price at the time of the sale, but most of the income the MLP distributes from year to year is effectively tax-deferred.

Exchange-traded products can sometimes sidestep tax-reporting complexities but oftentimes at the expense of the tax benefits one would get if the MLPs were held directly.

TAXABLE BONDS

Bond income is generally taxed at investors' ordinary income tax rates in the year it was received. The income is taxable at the federal level in all cases, but Treasury bonds are not subject to state and local income taxes.

TIPS BONDS

As with Treasury bonds, interest payments from Treasury Inflation-Protected Securities, and increases in the principal of TIPS, are subject to federal tax but exempt from state and local income taxes. One additional thing to remember about TIPS, however, is that the amount by which the principal of your TIPS increased because of inflation is taxable for the year in which it occurs, even if your TIPS hasn't matured (in other words, before you would receive an actual payment of principal).

MUNICIPAL BONDS

Muni bonds are issued by state and local governments to finance public projects. In the vast majority of cases, the income paid out by these bonds is not taxed at the federal level. In some instances (particularly if the bond is issued by a state or municipality in which you reside), munis' income is not taxed at the state or local level, either. It is also worth noting that income from private-active munis is subject to the Alternative Minimum Tax.

COMMODITIES

There are typically no dividend or interest payments paid to investors who get exposure to commodities through exchange-traded-note (which are unsecured debt obligation) or grantor trust (which often hold physical commodities) structures. However, if you bought a commodity-futures-based ETN, you might have to report income using a Schedule K-1.

This article was contributed by Karen Wallace, Senior Editor with Morningstar.

Disclosure: Returns and principal invested in stocks are not guaranteed. Government bonds and Treasury bills are guaranteed by the full faith and credit of the United States government as to the timely payment of principal and interest. Bonds in a portfolio are typically intended to provide income and/or diversification. U.S. government bonds may be exempt from state taxes, and income is taxed as ordinary income in the year received. With government bonds, the investor is a creditor of the government. Only insured municipal bonds are guaranteed as to the timely payment of principal and interest by issuer. However, insurance does not eliminate market risk. A municipal-bond investor is a creditor of the issuing municipality, and the bond is subject to default risk. Municipal bonds may be subject to the alternative minimum tax and state and local taxes, and federal taxes would apply to any capital gains distributions. International investments involve special risks such as fluctuations in currency, foreign taxation, economic and political risks, liquidity risks, and differences in accounting and financial standards. Gold/commodity investments will be subject to the risks of investing in physical commodities, including regulatory, economic and political developments, weather events, natural disasters, and market disruptions. Exposure to the commodities markets may subject the investment to greater volatility than investments in more-traditional securities, such as stocks and bonds. Funds in a Traditional IRA grow tax-deferred and are taxed at ordinary income tax rates when withdrawn. Contributions to a Roth IRA are not tax-deductible, but funds grow tax-free and can be withdrawn tax-free if assets are held for five years. A 10% federal tax penalty may apply for withdrawals prior to age 59 1/2. Please consult with a financial or tax professional for advice specific to your situation. Holders of preferred stock are usually guaranteed a dividend payment, and their dividends are always paid out before dividends on common stock. In event that the company fails, there's a priority list for a company's obligations, and obligations to preferred stockholders must be met before those to common stockholders. On the other hand, preferred stockholders are lower on the list of investors to be reimbursed than bondholders are.

Tax law is ever-changing and can be quite complex. It is highly recommended that you consult with a legal, tax, or financial professional with any questions or concerns.

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