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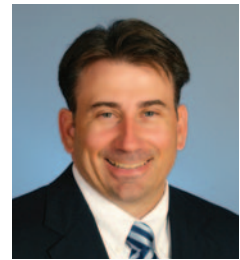

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# Financial Outlook

**SUMMER 2020**

## Avoid These Investor Mistakes

Avoid these common mistakes when making investment portfolio decisions:

❍ **Chasing performance.** Investors often pull out of sectors that are not performing well, moving that money to high performing investments. But the market is cyclical, and often those high performers are poised to underperform, while the sectors just sold are ready to outperform. A classic example is technology stocks in early 2000. Many investors rushed to purchase technology stocks just as they reached their peak and were headed for a long slide down. Rather than trying to guess which sector is going to outperform, broadly diversify your portfolio across a range of investment sectors.

❍ **Looking for get-rich-quick investments.** When your expectations are too high, you have a tendency to chase after high-risk investments. Your goal should be to earn reasonable returns over the long term, investing in high-quality investments.

❍ **Avoiding the sale of an investment with a loss.** When selling a stock with a loss, an investor has to admit that he/she made a mistake, which is psychologically difficult to do. When evaluating your investments, objectively review the prospects of each one, making decisions to hold or sell on that basis rather than on whether the investment has a gain or loss.

❍ **Selecting investments that don't add diversification benefits to your portfolio.** Diversification helps reduce your portfolio's volatility, since various investments respond differently to economic events and market factors. Yet it's common for investors to keep adding investments that are similar in

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## Basics of the SECURE Act

Signed into law by President Trump on December 20, 2019, the Setting Every Community Up for Retirement Enhancement Act, also known as the SECURE Act, is intended to increase access to tax-advantaged retirement accounts, helping older Americans in retirement and encouraging employers to offer 401(k) plans.

The new act, which went into effect on January 1, 2020, will affect IRAs, 401(k) plans, and other retirement accounts.

### What Has Changed

The SECURE Act has made several changes related to tax-advantaged accounts:

❍ Increasing the cap for small businesses to automatically enroll workers in safe harbor retirement plans from 10% of wages to 15%.

❍ Providing a $500 tax credit per year to employers who create a 401(k) or SIMPLE IRA plan with automatic enrollment.

❍ Allowing businesses to enroll part-time employees who have worked 1,000 hours throughout the year or 500 hours for three consecutive years.

❍ Encouraging plan sponsors to offer annuities in their 401(k) plans by reducing their liability if the insurer can't meet its financial obligations, and also not requiring them to choose the lowest-cost plan.

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# Investor Mistakes

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nature. This does not add much in the way of diversification, while making the portfolio more difficult to monitor.

- **Not checking your portfolio's performance periodically.** While everyone likes to think their portfolio is beating the market, many investors simply don't know for sure. So analyze your portfolio's performance periodically. Compare your actual return to your targeted return. If you aren't achieving your targeted return, you risk not achieving your financial goals. Now honestly assess how well your portfolio is performing. Are major changes needed to get it back in shape?
- **Letting market predictions cause inaction.** No one has shown a consistent ability to predict where the market is headed in the future. So don't pay attention to gloomy or optimistic predictions. Instead, approach investing with a formal plan so you can make informed decisions with confidence.
- **Expecting the market to continue in its current direction.** Investors tend to make investment decisions based on current trends in the market. Thus, if the stock market has been performing well for a period of time, investors tend to move more and more funds into that area. However, when the markets have an extended period of above or below average returns, they have a tendency to revert back to the average return. For instance, following an extended period of above-average returns in the 1990s, the stock market experienced a significant downturn, helping to bring the averages back in line.
- **Not understanding that saving and investing are two different concepts.** Saving involves not spending current income, while investing requires you to take those savings and do something with them to earn a return. Saving often becomes easier when separated from the choice of where to invest. Find ways to make saving as automatic as possible, then take your time to research and select specific investments.
- **Considering only pretax returns.** One of the most significant expenses that can erode your portfolio's value is income taxes. Thus, don't just consider your pretax returns, but look at after-tax returns. If too much of your portfolio is going to pay taxes, implement strategies that can help reduce those taxes.
- **Not realizing that help is only a phone call away.** The investment world has become very complex, with a vast assortment of investment vehicles now available. If you need help with your investment decisions, please call. ❍❍❍

# Consider Maturity Dates

All investments seem more volatile these days, including bonds. To help control volatility in your bond portfolio, carefully consider maturity dates before purchase. Bonds can be purchased with maturity dates ranging from several weeks to several decades. Before deciding on a maturity date, review how that date affects investment risk and your ability to pursue your investment goals.

Typically, yield increases as the maturity date lengthens, since you assume more risk by holding a bond for a longer time. Investors are often tempted to purchase bonds with long maturity dates to lock in higher yields, but that strategy should be used with care. If you purchase a long-term bond knowing you'll need to sell before the maturity date, interest rate changes can significantly affect the bond's market value. Two fundamental concepts about bond investing apply:

- **Interest rates and bond prices move in opposite directions.** A bond's price rises when interest rates fall and declines when interest rates rise. The existing bond's price must change to provide the same yield to maturity as an equivalent, newly issued bond with prevailing interest rates. You can eliminate the effects of interest rate changes by holding the bond to maturity, when you will receive the full principal amount.
- **Bonds with longer maturities are more significantly affected by interest rate changes.** Since long-term bonds have a longer stream of interest payments that don't match current interest rates, the bond's price must change more to compensate for the interest rate change.

Although you can't control interest rate changes, you can limit the effects of those changes by selecting bonds with maturity dates close to when you need your principal. In many cases, you may not know exactly when that will be, but you should at least know whether you are investing for the short, intermediate, or long term. Please call if you'd like to discuss bond maturities in more detail. ❍❍❍

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## SECURE Act

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- ❍ Removing the "one bad apple rule" for multiple employer retirement plans, which required that all of the participating small businesses meet the plan requirements or it failed for all of them. Now multiple employer plans will enjoy the economy of scale and be able to provide more plan features.
- ❍ Changing the age of required minimum distributions (RMDs) on retirement accounts from 70½ to 72.
- ❍ Eliminating the maximum age for traditional IRA contributions, which was previously capped at 70½ years old.
- ❍ Allowing a penalty-free withdrawal of $5,000 from 401(k) plans to help with the costs of having or adopting a child.
- ❍ Allowing the use of $10,000 annually from 529 plans to repay student loans.

Another change is the removal of the stretch IRA, which is estimated to raise $15.7 billion in tax revenue. This rule allowed nonspouses who inherited an IRA to stretch the disbursements over their lifetime. With the new rule, nonspouses who inherit an IRA will be required to take a full payout from the account within 10 years of the original account owner's death, beginning with account holders who die in 2020. With the changes to inherited IRAs, it will be important for account owners to review their estate plans and the potential tax consequences.

### The Jury Is Out

While it will take time for the jury to come in on whether the SECURE Act will make positive changes in helping Americans save for retirement, many financial experts appear to be optimistic and believe it is a step in the right direction. As expected, other experts feel it will have a limited impact on saving.

One thing experts can agree on is that Americans are currently not financially prepared for retirement, and changes are needed to put people on the path toward financial security. Hopefully, the SECURE Act is the impetus for that change. Please call if you'd like to discuss this in more detail. ❍❍❍

## When to Use Tax-Advantaged Accounts

Tax-advantaged savings plans, like 401(k) plans and individual retirement accounts (IRAs), help your money grow faster than taxable investments, but they're not always the right place for your savings. Here is a rundown on when one choice or the other might be appropriate.

### Put your money in a tax-advantaged saving plan when:

- ❍ Your employer matches your contribution. It's rare that taking advantage of this free money doesn't make sense.
- ❍ You already have savings equal to at least three months of living expenses and, if you have dependents, adequate life insurance coverage.
- ❍ You already own a home and are comfortably meeting your monthly mortgage payments.
- ❍ You haven't yet met your goal for a retirement nest egg and need the return-enhancing advantage of tax-free compounding to reach it.

### Consider *not* contributing to a tax-advantaged plan when:

- ❍ Either you're already at the limit of your employer's matching contribution or your employer doesn't offer one. (Though even in these cases it may still make sense to contribute to your 401(k), as long as the plan's fees and expenses are low and it offers sufficient diversification.)
- ❍ The investment choices in your employer's plan charge high annual expense fees. The pre-tax advantage of contributing to a 401(k) plan can be eroded by fees.
- ❍ You're in a high tax bracket and want to invest in individual equities for long-term capital gains. Rates on long-term gains are well below the highest federal income tax bracket, and unless you contribute to a Roth IRA or Roth 401(k) plan, you'll have to pay ordinary income taxes on the gains on stocks in a traditional IRA or 401(k) plan.
- ❍ You want to diversify beyond the choices available in an employer's retirement plan. If this is the case, you may still want to contribute to an IRA, but through an account with sufficient diversification options.
- ❍ You want municipal bonds to be part of your portfolio. If you hold municipal bonds in a traditional IRA or 401(k) plan, any interest income, even tax-exempt income, will be taxed at ordinary income rates when withdrawn. It is better to hold municipal bonds in taxable accounts so the tax-exempt interest income is not taxable. ❍❍❍

## Financial Data

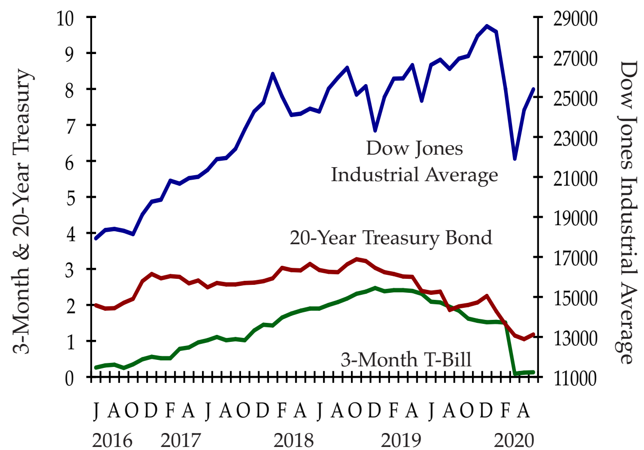
| Indicator | Mar-20 | Apr-20 | May-20 | Dec-19 | May-19 |
|---|---|---|---|---|---|
| | Month-end | | | | |
| Prime rate | 3.25 | 3.25 | 3.25 | 4.75 | 5.50 |
| Money market rate | 0.34 | 0.31 | 0.29 | 0.58 | 0.72 |
| 3-month T-bill yield | 0.09 | 0.12 | 0.13 | 1.52 | 2.31 |
| 20-year T-bond yield | 1.15 | 1.05 | 1.18 | 2.25 | 2.39 |
| Dow Jones Corp. | 3.81 | 2.72 | 2.63 | 2.84 | 3.63 |
| 30-year fixed mortgage | 2.41 | 2.36 | 2.28 | 3.31 | 3.44 |
| GDP (adj. annual rate)# | +2.10 | +2.10 | -5.00 | +2.10 | +3.10 |

| Indicator | Mar-20 | Apr-20 | May-20 | YTD | 12 Mon |
|---|---|---|---|---|---|
| | Month-end | | | % Change | |
| Dow Jones Industrials | 21917.16 | 24345.72 | 25383.11 | -11.1% | 2.3% |
| Standard & Poor's 500 | 2584.59 | 2912.43 | 3044.31 | -5.8% | 10.6% |
| Nasdaq Composite | 7700.10 | 8889.55 | 9489.87 | 5.8% | 27.3% |
| Gold | 1608.95 | 1702.75 | 1728.70 | 13.5% | 33.4% |
| Consumer price index@ | 258.68 | 258.12 | 256.39 | -0.3% | 0.3% |
| Unemployment rate@ | 3.50 | 4.40 | 14.70 | 320.0% | 308.3% |

# — 3rd, 4th, 1st quarter @ — Feb, Mar, Apr Sources: *Barron's, Wall Street Journal*

### 4-Year Summary of Dow Jones Industrial Average, 3-Month T-Bill & 20-Year Treasury Bond Yield

June 2016 to May 2020




Past performance is not a guarantee of future results.

# Planning Year Round

Many people confuse tax planning with tax preparation and only think about it when preparing their annual tax return. However, there is little you can do to actually lower your tax bill when preparing your return. If your goal is to reduce income taxes, you need to be aware of tax planning opportunities throughout the year.

Take time early in the year, perhaps as part of the tax preparation process, to assess your tax situation, looking for ways to reduce your tax bill. Consider a host of items, such as the types of debt you owe, how you're saving for retirement and college, which investments you own, and what tax-deductible expenses you incur. It often helps to discuss these items with a professional who can review strategies you might not have considered.

During the year, consider the tax consequences before making important financial decisions. This will prevent you from finding out later that there was a better way to handle the transaction for tax purposes.

Look at your tax situation again in the fall, which gives you plenty of time before year-end to implement any additional tax planning strategies. At that point, you'll also have a better idea of your expected income and expenses for the year. You may then want to use strategies you hadn't considered earlier in the year, such as selling investments at a loss to offset capital gains. ❍❍❍

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