2019 YEAR-END FINANCIAL NEWSLETTER

At the turn of the decade, we feel very thankful to have you as clients and friends.
"Nothing can stand up to gratitude. There's no negative emotion – not fear, not self-doubt, not sadness, and certainly not anger – that can survive exposure to the radiance of gratitude." – Nick Murray

MARKET OBSERVATIONS

• The year 2019 was, in important ways, the mirror image of 2018. Indeed, 2018 was a dramatically outstanding one for the American economy and for corporate earnings and dividends; however, this great advance in the economy was completely unreflected by the equity market which ended on a terrific downbeat with a 19.8% peak-to-trough decline through Christmas. In 2019 the situation was exactly the opposite -- the market was up 29%, even though the economy slowed somewhat, manufacturing appeared to be stalling out, and the S&P 500's full-year *earnings* almost certainly trailed those of 2018. This advance in the market was a reward for our disciplined long-term approach of keeping the equity part of our portfolios fully invested and minimizing turnover (except for rebalancing and ongoing tax-saving strategies).

• The market's course this past year was a sequence of three important forays into new high ground. Of particular interest is the consolidation after the first advance through April (which made up all of 2018's drawdown). The drop in May only lasted about a month and took the S&P 500 down about 7% (not even close to 10% to be classified a "correction"). What captures our attention is the *way* investors reacted to this relatively brief, relatively shallow decrease. Simply stated, net ***liquidations*** of U.S. equity mutual funds and ETFs—especially contrasted with bond fund ***inflows***—soared to levels not seen since the Great Recession of 2008. It's worth repeating: a one-month, 7% drawdown set off a flight from equities consonant with the greatest financial crisis of recent time!

• Indeed, although the liquidation figures are incomplete as we write, 2019 saw one of the greatest equity fund/ETF net liquidations on record going back to 1992, according to the data provider Refinitiv/Lipper. This, mind you, after 10-plus years of 16% compound annual returns for the S&P 500. It is difficult for us to regard these data as anything but a powerfully suggestive contrary indicator.

Thus, we can only offer one summary opinion. (Note: an opinion, ***not a prediction***.) Assuming history is any guide—and it's the only guide we've ever had, or needed:
If you think the equity market is "too high" now, wait 'til you see it 20 years from now.

SECURE ACT: KEY TAKE-AWAYS

In the waning days of 2019, congress passed sweeping retirement reforms in the form of the SECURE Act. It was passed in the House this past summer, and eventually made its way through the Senate and was signed into law by the President. The legislation will have substantial repercussions for our retirements in the years to come. We note three key take-aways:

1) Unfortunately, inherited IRAs must now be distributed in the first 10 years after your heirs receive them, rather than over their lifetimes (except for spouses). ***Although little noted in the financial media, this now makes Roth conversions more valuable than ever,*** because otherwise, the larger, accelerated distributions of traditional IRAs are fully taxable to your heirs as ordinary income.

2) On the flip side, we now have until age 72 (instead of 70½) before the start of required minimum distributions (RMDs) from IRAs. ***This expands what we call the "Golden Window" between retirement and the start of RMDs for optimized tax-bracket topping with Roth conversions.*** The full effect can be calculated with more sophisticated financial planning programs and makes a surprising impact on your retirement income, as well as tax savings for your heirs.

3) One other provision also caught our attention for small business owners. Specifically, the people most in need of retirement savings rarely opt to have savings regularly deducted from their pay-check. For this group, their retirement income is usually just Social Security and it most likely will not be sufficient. ***Now there is a tax credit for companies who set up <u>automatic</u> enrollment into their 401k plans.*** For their part, new employees can fill out the paperwork to un-enroll, but the easiest course is to just remain in the 401k plan. We are really pleased there are now incentives in place for companies to adopt auto-enrollment, since we think this will have a significant impact on this widespread, growing problem.

A readable summary of some of the other provisions of the Secure Act can be found here:
https://www.kiplinger.com/slideshow/retirement/T047-S001-how-the-secure-act-will-impact-retirement-savings/index.html

GENERAL PRINCIPLES

• While this letter is primarily focused on the year just past, we feel it's worth appending our overall principle of investment advice. It is goal-focused and planning-driven, as sharply distinguished from an approach that is market-focused and current-events-driven. Long-term investment success comes from ***continuously acting on a plan***. Investment failure proceeds from ***continually reacting to current events in the economy and the markets***.

• Since we accept that the equity market cannot be consistently timed by us or anyone (even Warren Buffett unequivocally states this), we believe that the only way to be sure of capturing the full premium return of equities is to ride out their frequent, but ultimately temporary, declines in a well-balanced equity portfolio.

• By our count, there have been 15 "bear markets" in equities since the end of World War II—an average of one every five years or so. The average depth of these declines was around 30%. ***However, historically, the permeant advance of equities has triumphed over temporary declines.*** In September 1945 the S&P 500-Stock Index was about 16[1] whereas the Index ended this past year at 3,231 -- ***a gain of over 200 times (and that without counting dividend income)!***

With best wishes for the New Year!

[1] *Source: "S&P 500 at your fingertips" tab of www.politicalcalculations.com. The data are Nobel laureate Robert Shiller's.*
Content adapted in part from January 2020 Nick Murray ©