Virtuent

WEALTH MANAGEMENT GROUP

of Wells Fargo Advisors

FIRST QUARTER 2020

2019 RECAP & 2020 OUTLOOK

As is customary this time of year, we spend a lot of time with clients, friends and colleagues recapping the previous year's market movements as well as discussing next year's outlook. While we are reaching out systematically to everyone to have more individualized conversations, we thought we would provide you with a quick summary of where we stand.

2019's market performance was certainly exemplary. We saw nearly all asset classes yield positive returns. In some respect, this was to be expected, considering that 2018 was the first year since 1972 that all asset classes yielded negative returns (Source: Wells Fargo Investment Institute). But with many of the stock indices returning in excess of 20%, performance was surprisingly better than one might expect from the normal "bounce" after a loss. Despite plenty of newsworthy events, volatility in the markets was relatively tame. There wasn't a single 10% correction all year.

For 2020 we would expect market behavior to be the opposite. Instead of a high return, low volatility market like 2019, we expect more of a high volatility, low return market. The good news is that we do still see positive returns for 2020. When polling our research providers like Wells Fargo Investment Institute, Credit Suisse, Goldman Sachs, and FactSet's consensus, most are calling for upward movement in the mid-single digits. But again, the road to get there may be a bit bumpy. It would not be unusual to see one or more corrections during the year. These corrections should not come as a shock, rather, they should be expected.

Last summer in our newsletters and client calls we began talking about our geopolitical concerns for the market as opposed to structural/fundamental concerns. In particular, we introduced 1) China Trade / China Debt 2) Brexit 3) Fed Policy 4) Iran and 5) North Korea as the major issues threatening the U.S. economy and market stability. We also said that barring a major negative shift in these geopolitical issues, the fundamentals of the U.S. economy remained fairly strong, strong enough to put us in the camp of "no recession for 12 months."

Currently inflation, debt, unemployment and valuations all remain reasonable, so again, structurally we see no reason to call for recession in the next 12 months. And we will double down on our call that shocks to our outlook would primarily come from the exogenous, geopolitical events mentioned above. We just have a couple adjustments to make. Iran was less of a concern last year, but obviously, it has taken the top spot among our list of concerns at the moment. We would also add to our geopolitical list the election cycle. As political rhetoric begins to ramp up in a few months, this too will tend to weigh on markets. Nonetheless, excluding any major shocks from our (now six) geopolitical concerns, we see a slow growing economy with modest markets returns. Just buckle your seatbelts. 2020 might be a little bumpy.

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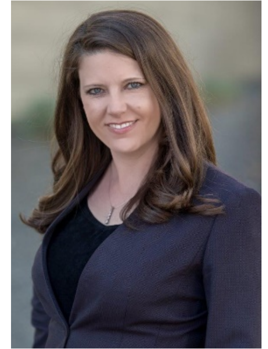
The Secure Act

By Meghan McGuire, Associate Vice President – Investment Officer



Since we *love* to talk in acronyms in the finance industry, I'd like to introduce to you a new one. It pertains to the SECURE Act, this is short for Setting Every Community Up for Retirement Enhancement Act. There is a lot to explain and unfortunately acronyms are hard to avoid here. I'll do my best to explain the Act but all joking aside, there is a lot of financial jargon associated with the Act and I apologize in advance.

The Act was a bipartisan effort signed into law on December 20th 2019. Basically, the US has a retirement crisis on hand. In 2018 the US Bureau of Labor Statistics published a report that stated only 55% of the adult population participate in a workplace retirement plan. And, of those who do participate, most are behind schedule in saving for retirement. Vanguard published a report that stated that the median 401(k) balance for those 65 or older is $58,035. Ouch! Bottom line: Social Security is not providing a sufficient income stream to retirees. Pensions are becoming like the dinosaur, extinct. Some pension plans, such as Illinois and Kentucky, are significantly underfunded. Which means it's up to **you** to save for **your** retirement. Unfortunately, the majority of Americans aren't saving like they should to maintain their lifestyle in retirement. This is why the Act was supported by both parties. It's an attempt to solve the problem.

There is a lot of changes associated with this Act and to summarize a 125 page document with 30 provisions in 1,000 words or less is difficult at best. I'll highlight two of the major provisions below. I invite you to tune into our quarterly call for more details.

Modifying the Required Minimum Distribution (RMD) in all Individual Retirement Accounts (IRA) and Qualified Retirement Plan (QRP) from 70 ½ to 72. (Who came up with 70 ½ anyway? Most people stopped counting their age by ½ years at the age of 10…). This pertains to people who have not turned 70 ½ on or before December 31, 2019. Pay attention here, this is a magical date that keeps coming up. The new law states that if you are 72 and are still working you can still make contributions into your IRA/401(k) as long as you don't own 5% or more of the company. You are still required to take a RMD but you can still contribute as long as you have earned income. **For example**: Sam (75) enjoys working. He is still required to take his RMD from his IRA. But he is allowed to contribute $7,000 of his earned income from his part-time job into his IRA.

An inherited IRA must be depleted by the 10th calendar year after the death of the account owner. This eliminates the use of a stretch IRA's. The change is effective to IRA account holders who pass after December 31, 2019. This does not apply to "eligible designated beneficiaries" defined as a spouse, minor children, one who is disabled or chronically ill. When the minor child reaches majority age then the 10 year rule kicks in. If the beneficiary is less than 10 years younger than the account holder the rule does not apply and reverts to the old law. Under the old law if you inherited an IRA account you are required to take RMD's based on a life expectancy table published by the Internal Revenue Service (IRS) based on your age. With the new law, there is no formula for how much

one needs to take out each year as long as the account balance is zero by the end of the 10th anniversary of the passing of the IRA account holder. Roth IRA's and trusts as beneficiaries are also subject to this new rule. The IRS is going to *love* this one! Why? It created an estimated **$15.8 BILLION** in tax revenue over the next 10 years. **For example**: Matt, age 80, passes his IRA to his two sisters, Julie (75) and Janice (65).

Because Julie is less than 10 years younger than Matt she is an eligible designated beneficiary and she can take the RMD from his IRA based on her life expectancy (old law). Because Janice is more than 10 years younger than Matt, she not an eligible designated beneficiary and therefore has to deplete her IRA account before the 10th anniversary of Matt's passing (new law). **For example**: Joe passes at the age of 75 and his wife, Ann (50) is the beneficiary. Because she is Joe's spouse she is an eligible designated beneficiary and can transfer the IRA into her name and she doesn't have to take an RMD until she turns 72. **For example**: Christa, age 50, passes and leaves her IRA to her two minor children, Dean (15) and Dave (12). Each will receive ½ of Christa's IRA. As soon as Dean turns 18 he will be required to deplete his ½ over the next 10 years. Same for Dave as soon as he turns 18.

Wow… I know! A LOT of information. I get that this can be confusing. If this topic should spark any questions or concerns please reach out; I am more than happy to explain in greater detail. BTW, if you were counting the correct answer to how many acronyms were used it was 5. Sorry, I couldn't resist throwing in another one.
BTW = by the way.

Questions, Comments, Suggestions?

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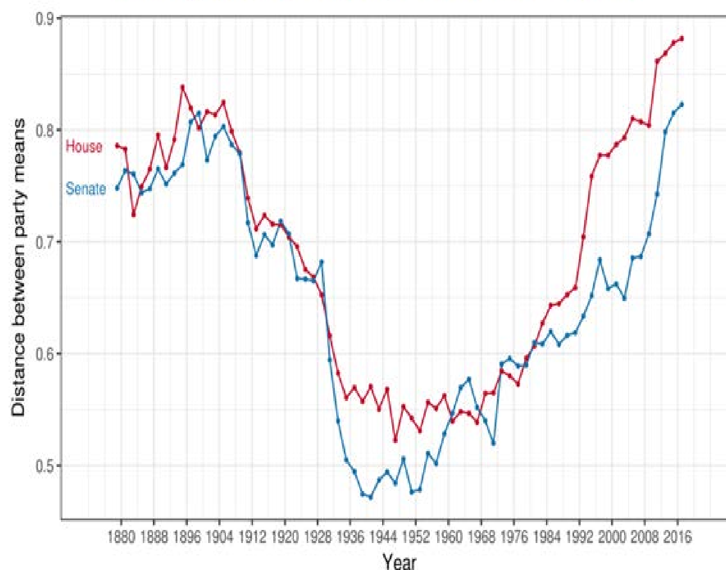
Don't Vote with Your Money

By T.H. Williams, Managing Director - Investments

According to research by the political scientists Keith Poole and Howard Rosenthal, partisanship has never been as high in congress as it is today. In the chart to the right, the higher the score the higher the level of partisanship for both the Senate and the House of Representatives.



(Source: Rosenthal and Poole)

This deep political divide permeates the news we consume and the opinions we form. So naturally, when we are talking with our clients about their plans, goals and investment objectives, it is not unusual for conversation to pivot to politics. These conversations become even more frequent during presidential election years. After all, you would assume that the choice for President of the United States would have a great effect on the stock market. And yet, you would be wrong to think so!

First a quick sidebar. Naturally, I have my political leanings and opinions, as do all of the team members of the Virtuent Wealth Management Group. However, we deliver all of our advice, and approach our investment process, in a completely apolitical manner. That's not to be confused with bipartisan. We take a non-political approach. Not only does this help us uphold our fiduciary responsibility, but it is also how all financial advisors should approach their advice. As I will discuss below, political bias (particularly presidential bias) is not helpful when it comes to financial advice and investments.

I remember Wednesday, November 9th 2016 very well. I was sitting at my desk in our Colorado Springs office a little before the 7:30 AM market open. Donald Trump had just shocked the world. Several hours earlier, around midnight, the Dow futures plummeted over 750 points in anticipation of a Hillary Clinton loss. But now they were beginning to reverse up (By the end of the day the Dow closed 312 points higher). Over the next hour I would field no less than seven phone calls from some of our more politically involved clients. Four were Democrats, three were Republicans. The Republican calls were easy. They ranged from asking me to add money to the market, to discussions about sectors and stocks we should invest in to take advantage of this momentous win. The Democrats were a different story. There was a lot of hand-holding and "talking people off the ledge."

I had to convince those four, plus several others over the course of the next few weeks, not to go to cash, not to put it all into gold, not to buy treasuries, etc.

After the initial wave of calls ended and the dust had settled, the market traded up through the end of the year with a 9.54% gain for the S&P 500 (Source: Factset). Democrats rationalized it was the calm before the storm and Republicans were perfectly smug in seeing this rally as the market's validation of their vote. Both were wrong.

The pullback in the markets leading up to the 2016 election and the rally thereafter are patterns we see in most elections. In 2020 once again we may see a similar pullback in the weeks leading up to the election, followed by a "relief rally" after the election. And you know what? It won't matter whether a Democrat or Republican is elected. This is a pattern that is intrinsic to elections, not political parties (Source: Goldman Sachs).

In general, whether a Democrat or Republican president is in the oval office matters less to the performance of markets than you might think. That is not to say that politics do not matter. They do. But history shows us that the choice of president alone, Democrat or Republican, doesn't have much impact on market performance (Source: Goldman Sachs). Every presidential election cycle our research providers, like the ones mentioned above, generate plenty of analysis discussing how markets behave under Democrat and Republican Presidents. This year will be no different. And I will be happy to share that analysis as it is updated for this election cycle. But let me give you the punch line first… One study will use one time period and show that there is slightly better market performance under a Democrat. Another study will use a different time period and give a slight edge to the Republican. However, BOTH will conclude that these small differences in performance are within the margin of error and statistically insignificant. In short, the wild claims that "If <Insert Candidate> wins, the markets and the economy are going to tank!" are simply untrue and not based on history or fact.

Politics do matter. And yes, the choice of president matters. But it is a combination of the president with the make-up of the house and senate where you really start to see differences in policy and performance, not the president alone. Along these lines, I would expect some real interesting analyses to be forthcoming. In the meantime, I want to drive home the point that while elections matter, the choice of president matters less to market performance than you might think. So in this hyper partisan environment, I encourage you all to read and educate yourself on the issues. Most of all, get out and vote! It is the most American thing you can do. Just don't vote with your money!

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