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THE ADVISOR

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Market May Keep Building Up, Blowing Off 'Froth' for Some Time

July could be a pivotal month in the coronavirus crisis for many reasons. With the infection rate spiking in several states as June ended, we'll find out whether these outbreaks can be contained without a major setback to reopening efforts nationwide. By mid-August, we should also see the release of corporate earnings reports, second quarter GDP numbers, and other data that will give us a clearer picture of the true economic impact of the crisis so far. How the financial markets respond to these developments will be telling — although we believe the shaky holding pattern the stock market has been in may continue for some time.

As you know, Wall Street has done a good job so far of staying laser-focused on good news while shrugging off bad news. As a result, the stock market was able to rebound from its initial drop of nearly 40% and has remained down by only about 10% for most of the pandemic. However, its hold on that relatively slight drop has been tenuous at times. That's typical when a market is overvalued and experiencing a blow-off top rally, which is what we believe is happening. This is a period of irrational growth that occurs without the economic fundamentals to support it, and we believe in this case it also is occurring despite a lot of socio-economic uncertainty.

In truth, we believe this market was already in a blow-off top period before the coronavirus hit. The pandemic has simply made the market's top "frothier" and more vulnerable to getting blown-off, as was clearly demonstrated last month. When the labor department reported in early June that the unemployment rate decreased slightly in May rather than increased as most analysts predicted, the Dow Jones Industrial Average quickly shot up 800 points.[1] Never mind that the real unemployment rate for the country still stands at close to 19%; just because the job news for May was slightly less bad than expected, Wall Street went crazy!

It went crazy again when the commerce department reported that retail sales rose by a record 18% in May.[2] Never mind that sales had shrunk by a

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The SECURE Act and Stretch IRAs

In the past, beneficiaries could take distributions from an inherited IRA over their lifetimes, often referred to as a stretch IRA. However, the SECURE Act, which is effective as of January 1, 2020, drastically changed those rules. Now, for individuals dying after December 31, 2019, designated beneficiaries (humans with a life expectancy) must withdraw all funds within 10 years. However, eligible designated beneficiaries can still withdraw funds over their life expectancy:

- Surviving spouses
- Minor children
- Disabled or chronically ill individuals
- Individuals who are not more than 10 years younger than the deceased IRA owner

Once a minor child reaches the age of majority, the remainder of the distributions must be taken within 10 years. Withdrawals do not have to be taken out in equal installments over the 10-year period. The only requirement is that the entire balance must be withdrawn by the end of the 10-year period. This provision is expected to significantly increase tax revenue from inherited IRA distributions. It may be a particular problem for children who inherit parents' IRAs and are in their peak earning years.

Some strategies to consider include:

Charitable Beneficiary

If you are already planning to give money to a charity, it will be more tax-efficient to leave taxable

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Market May Keep

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record 16.5% in April, or that second quarter GDP shrinkage is now expected to exceed 50%.[3] Wall Street focused only on the good news, and the Dow added another 600 points.

Healthy Dose of Caution

Just as quickly as froth can build up during a blow-off top rally, it can be blown off. This happened only a week after the jobs report spike when Federal Reserve Chairman Jerome Powell said some things that were already obvious to most economists, namely that this recovery is likely to be slow, and that unemployment may still stand at between 8 and 10% by the end of the year. With that, the Dow dropped 1,800 points, its biggest drop since March.[4]

This rapid change also illustrates why a blow-off top period can be so volatile. Big money investors don't really care whether a market spike is supported by economic fundamentals. Most are short-term traders and they just want in on the spike so they can make money. However, they also keep one finger on the trigger, ready to pull out whenever the next big selloff starts. That's exactly what we saw in mid-June, and it's probably what we will continue to see as reopening efforts proceed and more data emerges about the pandemic's impact on every sector of the economy.

Ultimately, we believe that dramatic 1,800-point blow-off in June was a good thing because it brought a dose of healthy skepticism and caution back to the markets. There was little of that throughout April and May, and the lack of it may have put some everyday investors at risk of falling prey to the psychological trap of "FOMO" — or "fear of missing out" — and buying back into the market at a dangerous time. FOMO is always a danger during a blow-off top period, which is why it's so important to keep things in perspective. Yes, the stock market has shown remarkable resilience during the coronavirus crisis so far, and there are some analysts who continue to believe the worst is already over for Wall Street. But considering all the potential setbacks to reopening, and the fact that we still don't have a coronavirus vaccine, I'm not that optimistic — nor are most economists.

A Narrow Range

What's more, even if a vaccine is discovered soon and virus spikes are quickly contained, the systemic damage already done to the economy may be more extensive than we realize. That's why the next six weeks could be so pivotal, since second quarter earnings and GDP figures will help make that picture clearer. Either way, we believe we will continue to see more weeks like we saw in mid-June, with froth building up and blowing off in an ongoing cycle. As a result, we believe the market should continue to trade in a fairly narrow range. Where it goes when it breaks out of that range will depend on how the pandemic plays out in the coming months. If a lot of things go right (the outbreaks subside, we get a vaccine, etc.) it could go up. If just one thing goes wrong, however, it could go down significantly again.

As we discussed in last month's newsletter, the next downturn may not be as precipitous as the first, but it may return the market to bear territory and possibly test its low point from March. The important thing for everyday investors to do during this period is to keep things in the right perspective, stay focused on asset protection, and be aware of the potential dangers of "FOMO" whenever the market's blow-off top is building up froth again.

[1] "May Sees Biggest Jobs Increase Ever of 2.5 Million," CNBC, June 5, 2020

[2] "US Retail Sales Rose Record 18% in May," Wall Street Journal, June 16, 2020

[3] "GDP is Now Projected to Fall Nearly 53% in the Second Quarter," CNBC, June 3, 2020

[4] "US Stocks End Sharply Lower as Coronavirus Worries Return," Wall Street Journal, June 11, 2020

Estate Planning for Complicated Family Situations

Divorce, remarriage, blended families, and children with disabilities are all situations where protecting your loved ones will give you peace of mind.

Divorce

If you divorce, you should update your beneficiaries, will, trusts, durable power of attorney, and healthcare proxy as soon as possible. If you have minor children, you will need to decide on a guardian if something happens to you or both of you.

In terms of financial assets, you can name your children as beneficiaries on life insurance, annuities, retirement accounts, and health savings accounts. However, your children cannot usually receive these funds until they turn 18. The surviving parent or an appointed guardian will need to manage these funds until your children are adults.

If You Remarry

If you remarry and both of you have children from previous marriages, you and your spouse will need to determine the best way to split assets. Unless you have a prenuptial agreement, your current spouse is entitled to half your estate. If you want your children from your previous marriage to receive assets, you should consider setting up a trust that provides for your current spouse but also ensures your children will receive the assets you designate for them.

If You Have a Special Needs Child

With a special needs child, the two most important things to consider are protecting his/her eligibility for Medicaid and providing assets for his/her financial future. This is a delicate balance because an inheritance could disqualify your child from essential benefits from Medicaid. The best solution is to set up a special-needs trust, which will ensure he/she qualifies for Medicaid benefits while preserving assets for his/her future.

The SECURE Act

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assets to your individual beneficiary and the IRA assets to a charity. The charity will receive the funds as a tax-exempt organization, meaning they will owe no taxes on the distribution.

Choose Beneficiaries Carefully

The idea is to try to reduce the income tax burden from the inheritance. That could mean naming younger or more lightly taxed beneficiaries to receive the IRA. For instance, if your children don't have a need for the IRA, you may want to give it to your grandchildren instead. You can also name more beneficiaries so that each receives less taxable income.

Life Insurance

You can buy life insurance to help beneficiaries fund the taxes from the inherited IRA distributions. Since life insurance proceeds are income-tax-free, your beneficiary will receive the proceeds of the life insurance policy without having to pay taxes.

Convert to a Roth IRA

If you convert your traditional IRA to a Roth IRA, your beneficiary will receive the funds free from income tax. The distributions still need to be taken within a 10-year period, but at least no taxes will be due on those distributions. A Roth IRA conversion involves taking funds from a traditional IRA, paying tax on any previously untaxed funds, and then putting the funds in a Roth IRA so that distributions can be taken income-tax-free. Most experts recommend using cash to pay the tax on conversion to avoid depleting your retirement savings. Paying the taxes with cash is especially critical if you are under age 59½, because if you use money from your IRA to pay the tax, you'll owe a 10% penalty on the amount that's not rolled over into the Roth IRA.

Please call if you'd like to discuss the implications of the SECURE Act on your retirement accounts.

Estate Planning Tips for Baby Boomers

As the baby boomer generation gradually makes the transition from their working years to retirement, it's time for them to get serious about estate planning. For a variety of reasons, many boomers have put off this essential task. These tips can help get back on track with estate planning.

1. Know what your kids expect — and what you plan to give them. By and large, boomers' parents were conservative savers. They came of age in the Great Depression, and that formative experience often led them to be cautious with their money. Many of them accumulated far more than they ever spent, and they passed that wealth on to their boomer children. But many baby boomers aren't taking the same approach. Even boomers who've saved a lot may end up spending much of what they've accumulated, since retirements are likely to be longer and healthcare costs expensive. But there's also an attitude difference. Active boomers may be planning on spending much of their hard-earned money on themselves. They believe they've done a lot for their children already. That's fine, but if this is your plan, you may want to let your children know.

2. Have a plan for the end of your life. Many, if not most, boomers are still leading busy lifestyles, and they plan to keep doing so for some time. Boomers who value staying fit and healthy may not consider what will happen when the inevitabilities of aging finally do catch up. While taking steps to live a healthy lifestyle is important to enjoying a great retirement, boomers shouldn't assume they'll be healthy forever. Sickness and disability can happen, and it will be easier for you and your family to deal with if you have a plan. Not only should you think about long-term care and how you'll pay for it, you should also make sure you have end-of-life planning documents in place.

3. Make sure your estate plan is up-to-date. Many boomers have estate plans they created decades ago. The primary goal of those estate plans may have been to ensure their children and surviving spouse were protected in the event of unexpected death. But as you get older, your estate planning needs change. If your kids are independent adults, providing for them is no longer as critical. You may have grandchildren who you want to receive part of your estate or new property that should be incorporated into your will. Or your family composition might have changed. You may even have received a health diagnosis that is affecting your estate-planning goals. For all these reasons and more, boomers need to sit down and review their estate plans to make sure they are properly conveying all their wishes.

4. Decide if, and how, you want to leave a legacy. Successful boomers often want to find a way to leave a lasting impact on the world and to support the causes and organizations closest to their hearts. If you count yourself among those for whom leaving a legacy is important, now is the time to start thinking seriously about how to turn those legacy dreams into reality. If your goals are ambitious — like starting a foundation or charity or endowing a scholarship — you should start planning now. The more lofty your goals, the more important it is that you take clear, concrete steps to turn your dreams into reality — like meeting with the leaders of the organization you support and finding out how you can best help them. After all, you won't be able to do this work after you are gone.

Not sure how to put these estate-planning tips into action? Please call if you'd like to discuss this topic in more detail.

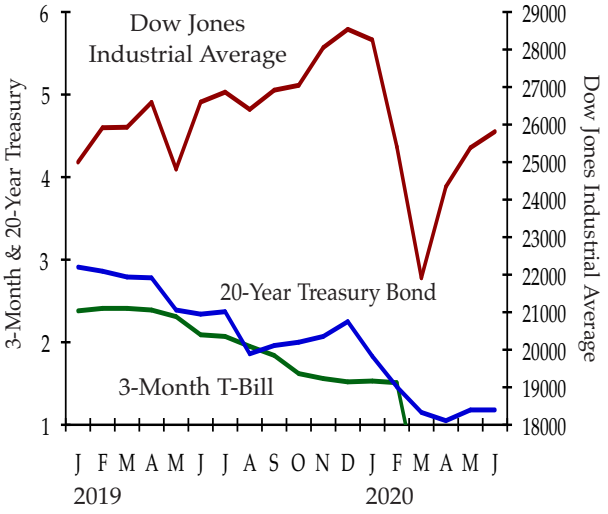
Business Data

Indicator	Month-end Apr-20	May-20	Jun-20	Dec-19	Jun-19
Prime rate	3.25	3.25	3.25	4.75	5.50
3-month T-bill yield	0.12	0.13	0.15	1.52	2.09
10-year T-note yield	0.64	0.65	0.66	1.92	2.05
20-year T-bond yield	1.05	1.18	1.18	2.25	2.34
Dow Jones Corp.	2.72	2.63	2.50	2.84	3.22
GDP (adj. annual rate)#	+2.10	+2.10	-5.00	+2.10	+3.10

Indicator	Month-end Apr-20	May-20	Jun-20	% Change YTD	12 Mon
Dow Jones Industrials	24345.72	25383.11	25812.88	-9.6%	-3.0%
Standard & Poor's 500	2912.43	3044.31	3100.29	-4.0%	5.4%
Nasdaq Composite	8889.55	9489.87	10058.77	12.1%	25.6%
Gold	1702.75	1728.70	1768.10	16.1%	25.5%
Unemployment rate@	4.40	14.70	13.30	280.0%	269.4%
Consumer price index@	258.12	256.39	256.39	-0.3%	0.1%

— 3rd, 4th, 1st quarter @ — Mar, Apr, May Sources: *Barron's, Wall Street Journal*
Past performance is not a guarantee of future results.

18-Month Summary of Dow Jones Industrial Average, 3-Month T-Bill & 20-Year Treasury Bond Yield
January 2019 to June 2020



Should You Serve as a Guardian?

When asked to serve as the guardian of someone's minor children in the event of his/her death, it is usually meant as a compliment that the person trusts you to serve in this important role. While you may fear that you'll hurt your relationship with that person by saying no, don't accept this role without giving it serious thought. Consider the following:

- **Are your lifestyles compatible?** Go over all details involved in raising the children. Will the children move in with you? If so, will that mean relocating them far from their current home? What are the parents' preferences regarding education, religion, lifestyle, and other factors? How well does your family get along with their children? Consider the impact on your children, including the fact that you will probably have less time available for them.
- **How much financial support will be available?** This involves more than making sure money is available for college and other expenses directly attributable to the children. Additional children in your house will increase many of your bills. Your house may now be too small, requiring an addition to your current home or moving to a larger home.
- **Are you comfortable taking on responsibility for the children's finances?** Just because you agree to take physical custody of the children does not mean you have to handle their finances. You may feel more comfortable with another person involved.
- **Has a contingent guardian been named?** Find out if a contingent guardian has been named in case you cannot serve. However, don't use this as an excuse to say yes when you really want to decline. It is better to indicate that you do not want to take on this responsibility now, so another guardian can be chosen and has the opportunity to go over all these details. Also, if your situation changes in the future, inform the parents immediately.

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