FINANCIAL SYNERGIES®
WEALTH ADVISORS

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Quarterly Newsletter

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Risky Goals

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In my 35 years+ of advising clients, step one has always been to determine what they need their money to do for them (their goals). Step two is putting together a portfolio of investment choices that will most likely achieve those goals, while matching their tolerance for market volatility (their risk profile). Holistic Financial Planning is rewarding but can be a tricky business.

According to Michael Kitces, financial expert and author, there are two alternative paths for implementing a client's plan. The first is to take a more "authoritative" approach, where

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the financial advisor is literally "the authority", or expert, whose job is to implement whatever the investor needs to achieve the goal, regardless of their risk tolerance. That advisor then bears the responsibility to help their clients stick with the plan and stay the course and "behaviorally manage" the relationship through the inevitable market downturn.

By contrast, the second option is a more "accommodative" approach, where the financial advisor may educate and make suggestions to the investor about why they need a greater level of risk, make them comfortable with their decisions, and in the end accommodate however the client wishes to invest (since it's their money and their decision in the end, even if it's a path inevitably doomed to failure by generating insufficient returns).

Which approach is better? Should the advisor design a portfolio that is a perfect fit to a client's risk profile, knowing it may not accomplish their goals? Or should the advisor put together a portfolio that will most likely accomplish a client's goals but is riskier than the client's tolerance for volatility? The standard industry approach is to assess a client's ability to withstand risk associated with their portfolio during the (inevitable) market downturns. All investors must ask themselves, "How likely is it that I will stay focused on my goals rather than my account balance during market reversals?"

All advisors struggle with this question when the risk "need" doesn't fit a client's risk tolerance: change the portfolio or change the goal? We know that something has to give. In my opinion, risk tolerance and risk need mismatches often aren't portfolio problems, they are goals problems. Sometimes, it's the goals that are risky. The sensible approach to designing a plan isn't only about finding a client's risk tolerance, it's about identifying a client's goal that is more consistent with their risk tolerance.

The next time we get together to review your portfolio for its risk and performance, let's also visit about your goals – they may carry more risk than your portfolio.

Welcome Brock Hedgecoke!

As part of our commitment to providing the highest level of service to our clients, we've added a new financial advisor to the team – Brock Hedgecoke. Please join us in welcoming Brock to the Financial Synergies Team!

Brock joins our team with experience serving at another well-regarded financial advisory firm in Houston. With his passion to build relationships, he has already hit the ground running and will prove to be a valuable part of the Financial Synergies team.

Brock grew up a Red Raider in the Texas Panhandle and decided to stay true to his roots and attend Texas Tech University. He graduated with a degree in Personal Financial Planning and is working towards obtaining the CERTIFIED FINANCIAL PLANNER™ certification. In his spare time, Brock enjoys serving with his church, Seven Mile Road Houston, hiking, running, and reading at coffee shops.

A trip to Charles Schwab's HQ focuses on best practices and the client experience

In June, our newest hires Lottie Hensley, Steven Ha, and Brock Hedgecoke participated in a two-day intensive customer service training at Charles Schwab's new facilities in Westlake, TX, just outside of Fort Worth. While at Schwab, they focused on how they can help Financial Synergies create better experiences for you, our clients, and picked up new tricks to make paperwork and our services more efficient for you. We are looking forward to implementing some of the things they learned while they were there!

New Tax Law Impacting Charitable Giving?

WILL GOODSON, CFP® | FINANCIAL ADVISOR

At the end of June, *The Wall Street Journal* reported that charitable giving by individuals saw the biggest drop in nearly ten years. According to the article, donations dropped by over 3% after four straight years of increased giving. The article suggests that the biggest reasons for the decline were the changes to the tax law and the sharp market downturn at the end of 2018. The tax laws change went into effect in 2018 and raised the standard deduction for individual and married filers. With fewer people itemizing their deductions, the article notes that individual giving saw a dip.

Whether this is a one-time occurrence or a long-term trend remains to be seen. Many of us in the office recently sat in on a presentation by Schwab Charitable that gave an in-depth overview of charitable giving in the U.S. I was surprised to learn that nearly 70% of all giving is done by individuals. It far surpassed both corporate and foundation giving (5% and 16%, respectively). While the dollar amounts given by corporations and foundations often exceed that of the average person, it's clear that the lion's share of giving is done by individuals.

While changes to the tax code may have eliminated some tax benefits for giving, there remains two great ways to give in a tax-efficient manner:

1) Donor Advised Funds (DAF) –individuals can transfer highly appreciated assets to a DAF and give those funds to a charity of their choosing. You receive a tax deduction equal to the fair market value and you can avoid paying any long-term capital gains. You can give non-cash assets such as real estate or collectibles to a DAF as well. The funds transferred to the DAF can be invested and grants can be given over several years

2) Qualified Charitable Distributions – individuals who save in tax-deferred vehicles like a 401k or IRA must begin taking annual Required Minimum Distributions (RMD) at age 70 ½. You can elect to have a portion of your RMD sent directly to a non-profit. The portion that is given counts toward the RMD requirement but is not considered a taxable distribution. The IRS allows qualified charitable distributions up to $100,000 per year.

The two options are great planning opportunities for those who are charitably inclined and have assets and/or RMD funds available to give. Will individuals continue to give at high levels in in the future despite changes to the tax laws? My guess is, yes, they will.

If you would like to explore either of these charitable opportunities, please contact us to learn more.

Sources:
https://www.wsj.com/articles/charitable-gifts-slip-in-first-year-under-new-tax-law-11560866400?mod=hp_featst_pos2

https://www.schwabcharitable.org/public/charitable/home

Timing Isn't Everything

MIKE MINTER, CFP®, CFS® | SHAREHOLDER, PORTFOLIO MANAGER

Over the course of a summer, it's not unusual for the stock market to be a topic of conversation at barbecues or other social gatherings. In fact, it's pretty common these days!

A neighbor or relative might ask about which investments are good at the moment. The lure of getting in at the right time or avoiding the next downturn may tempt even disciplined, long-term investors. The reality of successfully timing markets, however, isn't as straightforward as it sounds.

OUTGUESSING THE MARKET IS DIFFICULT

Attempting to buy individual stocks or make tactical asset allocation changes at exactly the "right" time presents investors with substantial challenges. First and foremost, markets are fiercely competitive and adept at processing information. During 2018, a daily average of $462.8 billion in equity trading took place around the world. The combined effect of all this buying and selling is that available information, from economic data to investor preferences and so on, is quickly incorporated into market prices. Trying to time the market based on an article from this morning's newspaper or a segment from financial television? It's likely that information is already reflected in prices by the time an investor can react to it.

Dimensional Fund Advisors recently studied the performance of actively managed mutual funds and found that even professional investors have difficulty beating the market: over the last 20 years, 77% of equity funds and 92% of fixed income funds failed to survive and outperform their benchmarks after costs.

Further complicating matters, for investors to have a shot at successfully timing the market, they must make the call to buy or sell stocks correctly not just once, but twice. Professor Robert Merton, a Nobel laureate, said it well in a recent interview:

"Timing markets is the dream of everybody. Suppose I could verify that I'm a .700 hitter in calling market turns. That's pretty good; you'd hire me right away. But to be a good market timer, you've got to do it twice. What if the chances of me getting it right were independent each time? They're not. But if they were, that's 0.7 times 0.7. That's less than 50-50. So, market timing is horribly difficult to do."

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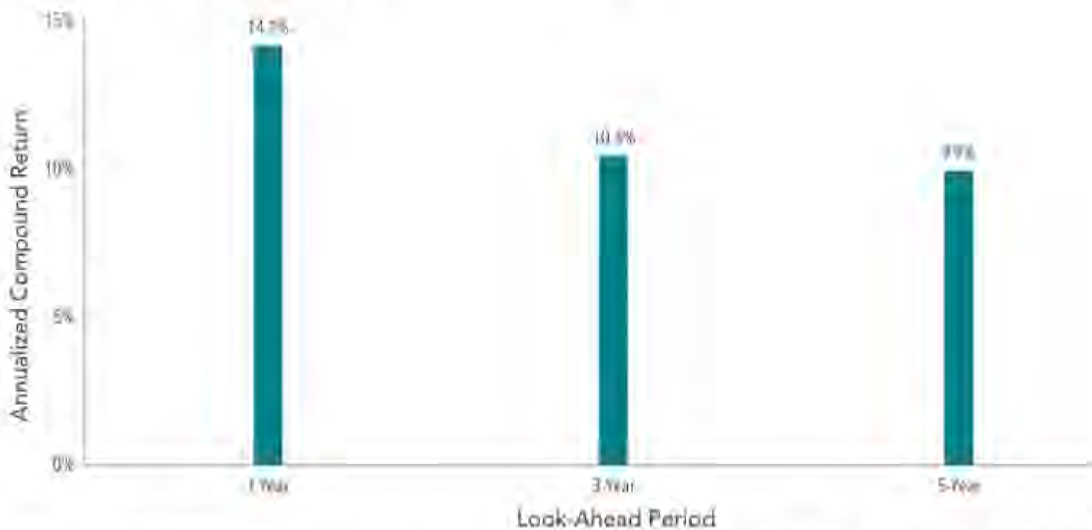
TIME AND THE MARKET

The S&P 500 Index has logged an incredible decade. Should this result impact investors' allocations to equities? Exhibit 1 suggests that new market highs have not been a harbinger of negative returns to come. The S&P 500 went on to provide positive average annualized returns over one, three, and five years following new market highs.

Exhibit 1. **Average Annualized Returns After New Market Highs**
S&P 500, January 1926–December 2018



In US dollars. Past performance is no guarantee of future results. New market highs are defined as months ending with the market above all previous levels for the sample period. Annualized compound returns are computed for the relevant time periods subsequent to new market highs and averaged across all new market high observations. There were 1,115 observation months in the sample. January 1990–present: S&P 500 Total Returns Index. S&P data © 2019 S&P Dow Jones Indices LLC, a division of S&P Global. All rights reserved. January 1926–December 1989; S&P 500 Total Return Index, *Stocks, Bonds, Bills and Inflation Yearbook*™, Ibbotson Associates, Chicago. For illustrative purposes only. Index is not available for direct investment; therefore, its performance does not reflect the expenses associated with the management of an actual portfolio. There is always a risk that an investor may lose money.

CONCLUSION

Outguessing markets is more difficult than many investors might think. While favorable timing is theoretically possible, there isn't much evidence that it can be done reliably, even by professional investors. The positive news is that investors don't need to be able to time markets to have a good investment experience. Over time, capital markets have rewarded investors who have taken a long-term perspective and remained disciplined in the face of short-term noise. By focusing on the things they can control (like having an appropriate asset allocation, diversification, and managing expenses, turnover, and taxes) investors can better position themselves to make the most of what capital markets have to offer.

Source: Dimensional Fund Advisors (DFA)