



★ Quarterly ★ Newsletter

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No, Really! It was a Remarkable Decade



MIKE BOOKER, CFP®, CHFC®, CFS®

SHAREHOLDER, FINANCIAL ADVISOR

Don't let anyone tell you the second decade of the 21st Century was a bad period. It was greatest improvement in human living conditions in history. Consider:

- Extreme poverty continued to decline and has dropped to below 10% of the world's population for the first time in history. It was 60% when I was in grade school.
- Global inequality decreased dramatically with African and Asian economies growing faster than Europe and North America
- Famine is virtually extinct
- Malaria, polio and heart disease are all in decline

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- We are using 65% less land to produce a given quantity of food compared to 50 years ago
- Populations of bald eagles, wolves, seals and even tigers are increasing

You may also be surprised to learn that our consumption of “stuff” actually peaked several years ago. We simply are consuming less. Chris Goodall, a researcher and investor in electric vehicles, published research showing that the quantity of usage of resources per person in the UK from 2000 - 2017 fell by about 33%. If this doesn't make sense, think about your smart phone. I use mine instead of a camera, radio, flashlight, compass, map, calendar, watch, CD player, newspaper and pack of cards.

According to Matt Ridley, author of *The Rational Optimist*, “Even in cases when the use of stuff is not falling, it is rising more slowly than predicted. For instance, experts in the 1970s forecast how much water the world would consume in the year 2000. In fact, the total usage that year was half as much as predicted. Not because there were fewer humans, but because human inventiveness allowed more efficient irrigation for agriculture, the biggest user of water.”

There were other ominous predictions that occurred in past decades. For example, the green movement was kicked off by predicting the imminent exhaustion of metals, minerals and fuels. In the 1971 book, *Limits to Growth*, its author predicted that if growth continued, the world would run out of gold, mercury, silver, tin, zinc, copper and lead before 2000. Not only have these metals not become particularly scarce, none of them have risen significantly in price or fallen in volumes of reserves.

As recently as 2012, George Monbiot wrote in the *Guardian* newspaper, “Within as little as 10 years, the world will be faced with a choice: arable farming either continues to feed the world's livestock or it continues to feed the world's people. It cannot do both.” His prediction was breathtakingly off target. Both animals and people are being fed with food left over.

So why write about malaria, famine and bald eagles in an investment newsletter? Because I find predictions, in all their varied forms, consistent in their ineptness. When experts can't even agree on how much farmland or water we might use in the near future, isn't it a bit silly of us to expect stock market prognosticators to correctly forecast something as variable as stocks? Answer: Yes.

Successful investors simply don't play this fool's game that is market prediction. We hope for the best as optimists, but plan for the worst employing a strategy of diversification into assets other than stocks. This is our plan, this is what works.

Thank you for another year of trusting this plan we designed for you. Your trust and confidence mean everything to us.

From all of us at Financial Synergies, we wish you the best and brightest of New Years.



Seeing Clearly in 2020

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

The start of a new year is a time to reflect and plan. For me, this means understanding what's driving the markets and economy, reviewing portfolios and financial goals, and reminding myself of the basic principles of investing. This opportunity to quietly reflect, especially after a year of spectacular investment returns, is a rare gift. After all, we will no doubt be bombarded by day-to-day headlines throughout the year to come. Here's a quote that puts today's "journalism" into perspective.

“Progress is invisible to most people because they don't get their understanding of the world from numbers; they get it from headlines. Journalism by its very nature conceals progress, because it presents sudden events rather than gradual trends. Most things that happen suddenly are bad: a war, a shooting, an epidemic, a scandal, a financial collapse. Most things that are good consist either of nothing happening – like a nation that is free of war or famine – or things that happen gradually but compound over the years, such as declines in poverty, illiteracy and disease.”

-Steven Pinker, *Financial Times*, December 27, 2019

2019 Review

Despite significant market uncertainty punctuated by short periods of volatility, global markets surged in 2019. The positive returns across a breadth of asset classes made 2019 one of the best years of the market cycle. This occurred despite constant worries around the Fed, trade wars, impeachment hearings, Brexit, and more.

Perhaps the most important reason for these returns is that the economy is still healthy. The recession that many investors feared at the end of 2018 didn't occur and few economists now expect a recession in the near future. The unemployment rate of 3.5% across the country is a 50-year low and consumer net worth is at a record high of \$113 trillion.

An equally important reason for these gains is that the Federal Reserve is pouring monetary stimulus into the system. The Fed made a full U-turn from raising rates last December – which slows the economy – to lowering rates in July. In doing so, the Fed effectively makes it cheaper to borrow money which tends to stimulate the economy and the stock market. This excited many investors, resulting in stocks hitting new all-time highs. For now, the Fed is on pause with additional rate cuts, although it continues to use its balance sheet to support the financial system.

Finally, there is a technicality to be aware of that visually inflated last year's stock market return numbers. Because 2018 ended near the market lows, a significant part of 2019's return was simply returning to previous levels. From the 2018 peak to the end of 2019, the U.S. stock market gained 10%. While this is still a terrific return, it's not quite the 28% S&P 500 price return number that will be discussed and remembered.

Seeing Clearly in 2020

The unavoidable truth about investing is that there are always reasons to be worried. All of the recent investment gains happened despite negative headlines and investor concerns all year long. To rephrase Steven Pinker's eloquent quote above, negative headlines capture our attention while positive developments can slip by unnoticed. These negative headlines caused the stock market to temporarily drop three times over the course of 2019.

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Despite this, investors who stayed disciplined were rewarded in the end – especially those who stayed invested at the end of 2018. Thus, an important skill when investing over the long run is to be able to see past short-term news. The fact that the economy stayed healthy and a trade deal, even an interim one, was eventually reached meant that much of the hand wringing by investors during the year was all for naught.

On that note, one challenge we'll all face in 2020 is that media attention will focus on the presidential election. There will be endless speculation and concern over what each candidate will mean for the stock and bond markets. And while elections are incredibly important as citizens, voters and taxpayers, investors should avoid over-reacting or jumping to conclusions based on political preferences.

The reality is that how the stock market responds to elections is very difficult to predict. In fact, investors have feared that just about every presidential candidate in history would spell the end of economic growth and stock returns. In recent times, this was certainly said of both Presidents Obama and Trump.

While economic policies can certainly make a difference over time, investors are usually better off focusing on what affects portfolios in the long run rather than reacting to day-to-day political headlines. In other words, investors should stay invested and save their energy for the polls.

Looking Further Into the Cycle

There are some indisputable facts about the market and economic cycle. In 2020, we will celebrate the 11th anniversary of the bull market and economic expansion – already the longest in history. The economy appears to be growing at a healthy pace of around 2%. Inflation is still benign despite historically low unemployment, although wages are beginning to rise more quickly. Interest rates are also quite low after a tumultuous 2019, during which the yield curve briefly inverted. All of these facts are classic signs of the later stages of the business cycle.

How much longer and further the business cycle goes requires a large degree of speculation. Areas such as manufacturing which have suffered over the past year will have to recover. Global economic growth, dampened by recent trade disputes, will have to rebound as well. Corporate earnings, which are forecast to have grown by only 1% in 2019, will need to accelerate in the next couple of years. The Fed will need to carefully maintain balance in the financial system, and Washington may need to engage in fiscal stimulus and pro-growth policies.

Ultimately, just as many investors were too fearful in 2018, some investors may be too greedy after a historic 2019. With stocks up significantly last year, many may continue to expect similar gains.

While we should be grateful for a strong year, it's important to have realistic expectations. The most important takeaway is that many of the reasons that stocks rose last year, which we discussed above, may be of less help in 2020. Today, very few investors are worried about a recession and the Fed is already stimulating the economy.

Stocks can still do well if the economy is healthy, but we shouldn't expect the U.S. stock market to rise another 30%. Instead, holding a diversified portfolio has always been the best way to benefit from stock market gains while protecting from uncertainty. This will continue to be the case in the decade ahead.

Below are seven charts to help to put the market and economy in perspective:

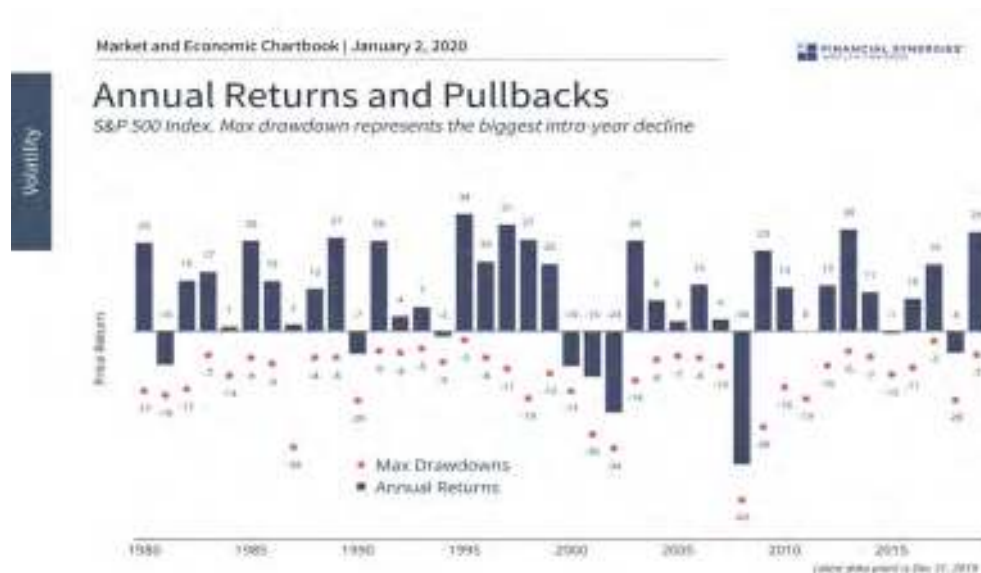
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1. The stock market reached new record highs in 2019



The S&P, NASDAQ and Dow Jones Industrial Average all achieved new record highs near the end of 2019. A combination of factors including the Fed, a healthy economy, and an interim trade deal helps to overcome investor fears.

2. The market was relatively calm throughout the year



Despite daily and weekly market volatility, including three periods of market pullbacks, markets were calm in 2019 by historical standards. The largest decline in the S&P 500 was 7%, only about half of the historical average in any given year.

One principle of investing is that temporary market swings can occur at any time. Investors should have proper expectations and be prepared for volatility in the months ahead by staying the course, not by trying to time the market.

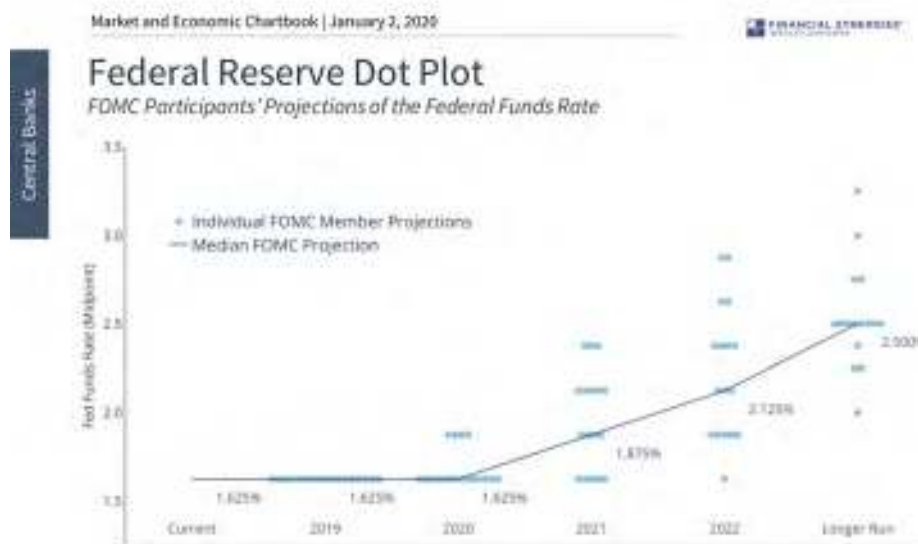
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3. Earnings growth was slow but could speed up in 2020



Unfortunately, earnings growth played little part in the market's record highs. Wall Street consensus estimates are for only 1% earnings growth in 2019 but nearly 9% growth in 2020. Thus, earnings growth will need to re-accelerate to sustain recent levels of returns.

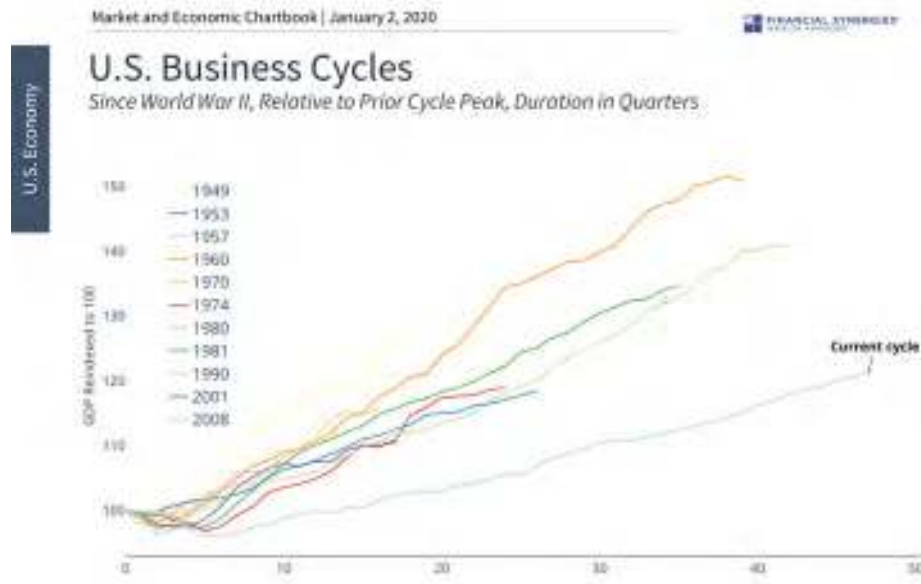
4. The Fed supported markets by cutting rates



The Fed played a large role in boosting investment returns across a variety of asset classes, including stocks and bonds. Not only did the Fed reverse course by cutting interest rates three times, their projections suggest that they expect rates to remain flat into 2021.

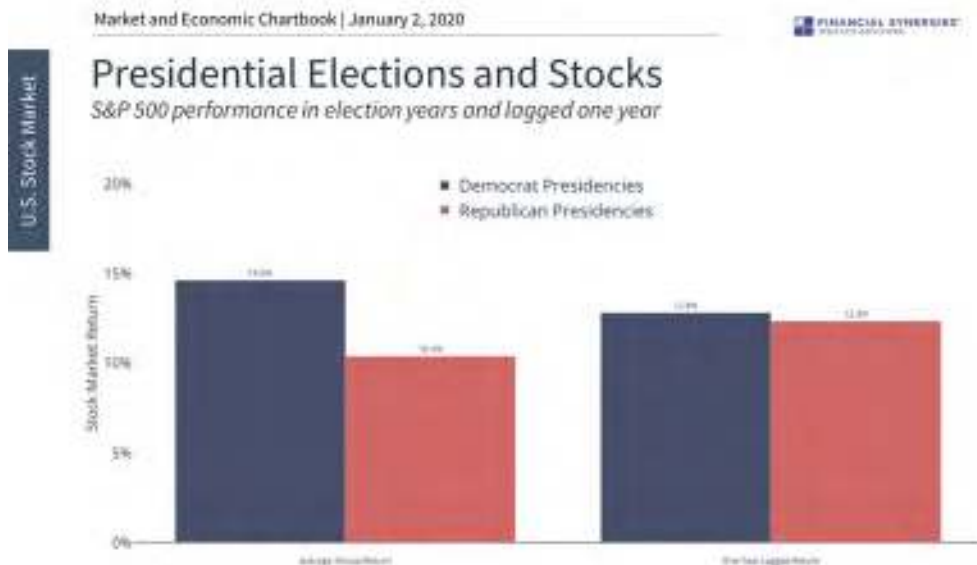
While markets have cheered these Fed moves, it's important to remember that this was in response to global economic risks and a slowing economy. Historically, Fed rate cuts late in a cycle are a negative sign. While this time may be unique for several reasons, it's important to maintain a longer-term perspective.

5. The business cycle hit a historic milestone



At nearly 11 years, this U.S. economic expansion is officially the longest on record. The bad news is that the economy grew at only a fraction of the pace of past business cycles. Still, even slow and steady growth has been enough to push asset prices to record levels.

6. Investors shouldn't over-react to presidential elections

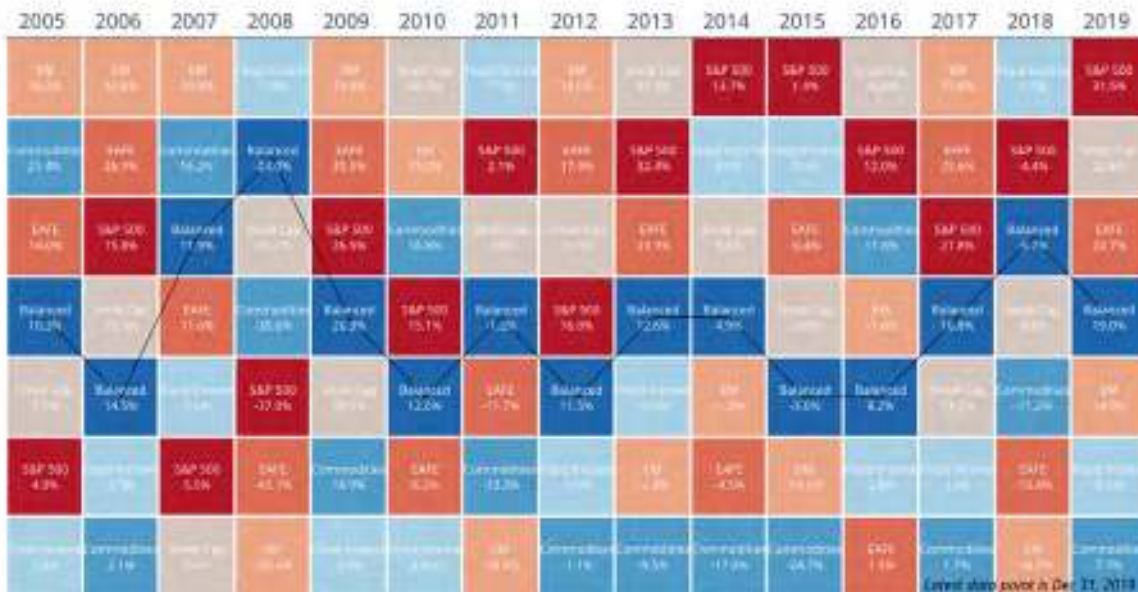


Presidential elections will garner a significant amount of media attention, and rightly so. However, investors should be cautious when reacting to headlines in their portfolios. The reality is that markets have performed well under both political parties, especially when one considers the time it takes for policies to be passed, implemented, and trickle across the economy. For investors, the business cycle is a much more important driving force.

7. Global diversification is key

Asset Class Performance Total Returns

Investing



A breadth of asset classes performed well in 2019, with a hypothetical 60/40 portfolio generating the highest returns since 2009. Both stocks and bonds did well, especially with interest rates falling.

The U.S. stock market outperformed many other regions again in 2019. However, if the global economy can re-accelerate, it will be even more important for investors to diversify globally.

Investors who can see the current market and economic landscape clearly are in a better position to profit in 2020.

Sources: Briefing Investor

Sources for Graph Data:

- 1) Standard & Poor's | 2) Clearnomics, Standard & Poor's | 3) Refinitiv, Standard & Poor's | 4) Federal Reserve | 5) US BEA, NBER | 6) Clearnomics, Standard & Poor's | 7) Clearnomics, Refinitiv

WELCOME DAVID WANJA, JR.!

Please join us in welcoming David Wanja, Jr. to our team! David joined Financial Synergies in December of 2019 as an Associate Financial Advisor. He comes with experience from another reputable advisory firm in the area and currently serves on the Board of Directors for the Financial Planning Association of Houston. He is learning our wealth management business from the ground up, and will no doubt prove to be an invaluable asset to our team and clients for years to come!

When away from the office, David enjoys spending time with his wife Tiffany and their twin boys, Luke and Benjamin. With any remaining spare-time you can find him reading, on a golf course, or on a tennis court. David resides in Huffman and attends North East Houston Baptist Church.



Congress Passes SECURE Act

WILL GOODSON, CFP® | FINANCIAL ADVISOR

Congress recently passed the Setting Every Community Up for Retirement Enhancement, or SECURE Act. The bill marks some of the most significant changes to retirement policy in more than a decade. The bill first made headlines back in the spring when it received bipartisan support in the House of Representatives. Then it stalled in the Senate due to a handful of provisions but remained a priority throughout the rest of the year. The SECURE Act was attached to the year-end Congressional appropriations bill that kept the government funded through the end of 2019.

Lawmakers have remained focused on the need to help improve retirement savings for American workers. The bill makes several significant changes to the current retirement landscape, including:

- Reduces the restrictions for multiple employer plans, or “MEPS,” where small businesses can band together to offer retirement plans, such as 401ks, to their employees and share costs.
- Removes the age cap for Individual Retirement Account (IRA) contributions for workers over the age of 70 ½.
- Non-spouse beneficiaries of tax-deferred retirement plans, like 401ks and IRAs, must distribute all plan assets within a ten-year period and pay all corresponding taxes (eliminates the “stretch” IRA opportunity). The rule also applies to Roth IRAs but those distributions are typically non-taxable.
- Increases the availability of annuity options within retirement plans.
- Increases the Required Minimum Distribution (RMD) age from 70 ½ to 72 (applies to those who turn 70 ½ after December 31, 2019).
- Allows certain long-term part time workers access to company retirement plans.
- Up to \$10,000 of 529 account assets can be used for student loan repayments.
- Parents may take up to a \$5,000 penalty-free distribution from their retirement plan for the birth or adoption of a child (the distribution is still taxable).

Early feedback from the passing of the SECURE Act appears to be mixed. It’s hard to argue against giving more workers the opportunity to save in retirement plans. It’s no big secret that many Americans are facing a shortfall when it comes to their retirement savings. Many small businesses do not offer retirement plans so hopefully these new provisions will help improve that.

Current retirees who have not yet reached the age for mandatory distributions, or RMDs, now have an extra year and a half to allow their assets to grow tax-deferred. The elimination of the stretch IRA for non-spouse beneficiaries may require retirees to reconsider their estate plans. It will likely prompt an increase in Roth conversions for those with large tax-deferred assets.

Roth conversions allow an individual to transfer pre-tax dollars to a Roth IRA and pay the tax on the corresponding amount. The funds then grow tax-free for the remainder of the account owner’s lifetime. Under the new rules, non-spouse beneficiaries of Roth IRAs are now required to distribute those assets over a 10-year period, but those distributions are tax-free. Thus, it has become an effective wealth transfer tactic and its popularity will likely increase in the future.

Like any legislation, it will take time before the potential benefits are realized. For those who are still working, it provides an opportunity to review your current retirement savings strategy to make sure you’re maximizing all available benefits. For retirees, it makes sense to review whether Roth conversions make sense and how the change to the RMD age may impact your wealth distribution strategy. Regardless of whether you’re working or retired, changes like these highlight how financial planning is an ongoing process and it’s important to consistently review your plan to make sure you’re still on track.

If you have any questions about these changes and how they may impact your financial situation, please feel free to contact us. We are ready to help address any questions or concerns you may have.

Sources: “SECURE Act - House Committee on Ways & Means”, “Congress Passes Sweeping Overhaul of Retirement System”, “Advisers weigh in on SECURE Act, approved by House and on way to Senate and the White House”, SECURE Act Provisions Folded Into Congressional Spending Bill Passed By House

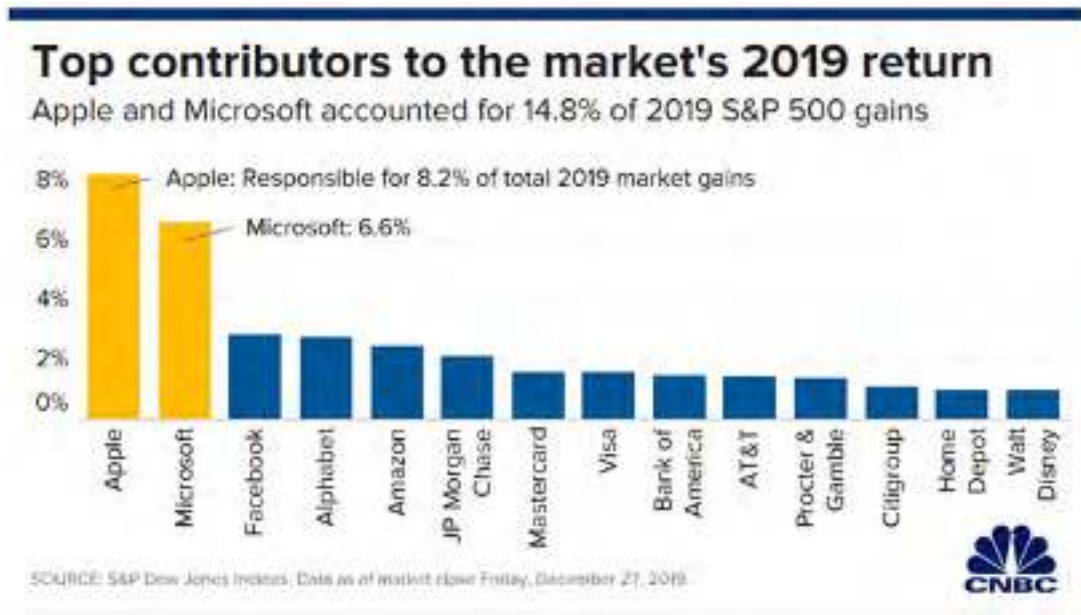


These Two Stocks Dominate the S&P500

HEATH HIGHTOWER, CFP® | SHAREHOLDER, FINANCIAL ADVISOR

Investors seeking broad market exposure often buy S&P 500 index funds as a way of investing in hundreds of US companies all at once. When people buy the S&P 500, they're typically seeking diversification, but 2019 was a friendly reminder that the S&P 500 may not be as diversified as people think it is.

Last year's market performance was one for the record books. The S&P 500 made 28% last year, making it the 2nd best calendar year for the index since the year 2000. (The S&P 500 made 30% in 2013.) Perhaps even more surprising is that over half of the return that investors experienced (nearly 15 percentage points) came from only two stocks: Apple & Microsoft, which gained an impressive 85% and 54%, respectively, for the year. That's more than the next eight biggest contributors combined as reported by CNBC's chart below.



Due to their size, Apple & Microsoft are the two largest holdings in the S&P 500. The S&P 500 is a cap weighted index, which means that the largest companies in the index are more heavily weighted than the smaller ones. So as these companies continue to grow, they will become an even larger percentage of the overall index - a snowball effect. Last year, investors in the S&P 500 celebrated extravagant returns from Apple & Microsoft, but this sword cuts both ways. Losses in these stocks have a more detrimental impact than losses in other (smaller) positions in the index.

In a rally fueled by big tech companies like Apple & Microsoft, the S&P 500 index is a wonderful investment to own. However, it's also important to avoid concentrated stock positions. One way we create diversification in your portfolio is by owning both the S&P 500 and a large cap value fund. This pairing allows us to participate in growth-fueled bull markets like that of 2019 but also hedge our exposure to the largest stocks in the market should they take a dive. As always, feel free to call us if you'd like to discuss your portfolio allocation. In the meantime, here's to continued growth in 2020!