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# The R Word

*by Mike Booker, CFP®, ChFC®, CFS®*

There has been a fair amount of talk about a possible recession coming to us in the near future. I want to discuss what that means and also give a bit of historical context so that we understand the recession when a recession actually shows up. A recession is a macroeconomic term that refers to a significant decline in general economic activity in a designated region. It is typically defined as two consecutive quarters of economic decline, as reflected by GDP in conjunction with monthly indicators such as a rise in unemployment.

First of all, we investors should not have an excessive fear of recessions. They are a normal component of the business cycle and are unavoidable. In fact, roughly every 4 years since the Great Depression of 1929 and every 5 years since WWII, a recession has occurred in the U. S. The longest period of calm in the economic cycle was during the decade of the 90s when the U. S. economy did not experience a recession at all.

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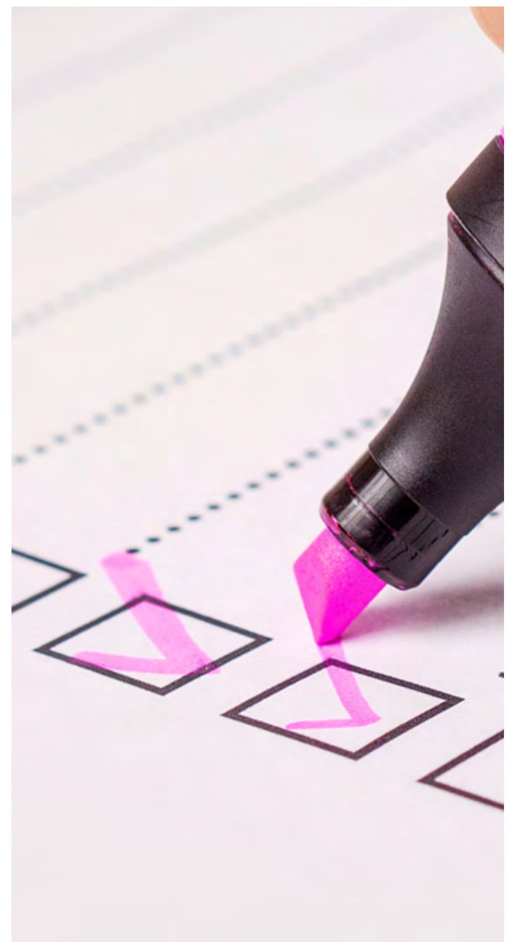
Economies need recessions to take a breather. Financial writer Ben Carlson likens recessions to drivers in a NASCAR race. He writes, "drivers make somewhere between 5-8 pit stops over the course of the 200 laps in the 500-mile race. NASCAR drivers can't push their cars to the extreme for the duration of the race without taking a break. They need to stop and fill up their gas tanks, change their tires and make other adjustments." This is an apt analogy as economic growth cannot uninterrupted forever either.

While recessions are painful in the short term, they also provide investors with lower prices to buy stocks with any cash they have on the sidelines. In my opinion, when recessions create a downward stock market, they wash out all of the short-term speculators in the market. This is a positive in the long run because by the end of a recession, all that is left are the long-term investors who have kept their eye on the investment ball. Those are the investors that will reap the benefits of a new base for the recovery of the market post-recession.



There are two other benefits besides buying stock in a recession that benefit the long-term investor. First, in 4 of the last 9 recessions, stocks actually rose. Likewise, in the year leading up to a recession, stocks were positive 6 out of 9 times, which dispels the myth that the stock market always acts as a leading indicator of economic activity. The second is those post-recession market returns. Now, the average return percent during a recession is -1.5% since 1954, but the returns 1 year after a recession are 15.3%. After 3 years, 40.1% and 5 years later, 78.7%.

Aiming to benefit financially from the correct timing of the end or even the beginning of a recession can be a true fool's errand, however. Remember the Great Recession that began in December of 2007? The economists at the National Bureau of Economic Research, who are basically the official scorekeepers, didn't discover the recession until December 2008 - a year later, and only a few months before the episode ended. The previous recession began in March 2021 - but the NBER didn't call it a recession until November 26 of that year! By amazing coincidence, that was actually the month it ended (as they told us many months later).

We may not get our recession this year, but we can count on one coming home to roost at some point. Remember that you have an investment plan, and it is executed by us every day, recession, or no recession.

# Charitable Giving Strategies

*by Heath Hightower, CFP®*

The task of being a good steward is always top of mind for me. It's an honor to have the opportunity to help our clients make good decisions with their money. Over the years, I've had the privilege of working with some very successful people. But what's even more rewarding is to work with generous people who have a desire to give back. For some, the primary focus is on passing their wealth down to their children and then on to their children's children. And for others, there is more of a charitable focus. Today, I'd like to focus on the latter.

Many of our clients are already contributing to charity in some way. Over the years I've noticed that many people make on-going cash contributions to a church or favorite charity. While these cash contributions may be partially tax-deductible, there may be a more impactful and more tax-efficient way to give. Before making a charitable contribution this year, consider the following:

**Qualified Charitable Contributions (QCD)**

If you're an IRA owner over the age of 70 ½, you can make a tax-free Qualified Charitable Contribution (QCD) of up to $100,000 from your IRA. A QCD can be particularly useful for those who do not itemize their taxes. This is a great way for those who take the standard deduction to benefit from a charitable contribution. It's typically more tax-advantaged to make a QCD from your IRA, than making a cash contribution to a charity.The QCD also counts towards satisfying your Required Minimum Distribution so long as the funds come out before the 12/31 deadline.

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**Qualified Charitable Contributions (QCD), continued**

Just be advised that private foundations and donor advised funds do not qualify as eligible recipients.

**Donor Advised Funds (DAF)**

A donor-advised fund is essentially a giving account that can be setup at most custodians like Charles Schwab & Co., Fidelity, etc... Donors can contribute cash, appreciated stock, real estate, or even an interest in privately owned businesses. DAFs are very cost-effective and can offer better tax advantages than private foundations. But what I like the most about a DAF is its simplicity. They're very easy to establish and administer with no need for a board of directors. Donors can make contributions to multiple qualified charities and the custodian takes care of all administrative requirements.

Unfortunately, the lifespan of a DAF is limited to the original donor's lifetime or the two succeeding generations. Donors are also limited to qualifying charities. Most foundations are not considered to be a qualified charity; however, a foundation is permitted to contribute to, or fully convert to a DAF.

Our clients typically contribute highly appreciated stock to DAFs to shelter the capital gain. Once the stock is in the DAF, the shares can either be held long term or sold tax-free. The donor can then contribute the proceeds to any qualifying 501C(3) organization on the day of his choosing. The tax deduction for stock with a long-term capital gain is limited 30% of AGI (compared to 20% for a private foundation).

**Private Foundations**

Private Foundations are a bit more complex but can also offer some compelling advantages. For instance, a foundation can play a key role in generational planning for higher net worth families (typically funded with a least $5 Mill). They're often setup in perpetuity, providing family members an opportunity to serve on the board to collaborate and do something positive for generations to come. In my opinion, the long-term control and family collaboration are the most attractive aspects of a private foundation. And unlike Donor Advised Funds, a foundation can be used for scholarships, individual grants for travel or study, and can engage in direct charitable activities. You can even pay family members as foundation employees.

Unfortunately, private foundations can be costly and administratively cumbersome. The IRS also requires a 5% payout rate – meaning the foundation must distribute at least 5% of their net investment assets each year.

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A private foundation can be great for someone looking to maintain a high level of control and flexibility. They're typically associated with larger-scale gifts. Those who choose to start a private foundation typically contribute highly appreciated stock or private equity to their foundation to shelter the capital gain. Once the stock is held within the foundation, it can be held for future growth & income.Or it can be sold tax-free and then managed by the appointed board. The tax deduction for stock with a long-term capital gain is limited to 20% of AGI (compared to 30% for a DAF).

**Charitable Trusts (CRT, CLT, etc.)**

Charitable trusts fall into two basic camps, depending on when you want the donations to go to the charity: Charitable Lead Trusts (CLT) and Charitable Remainder Trusts (CRT).

- Charitable lead trusts can be a great option for those who would like to create a stream of income to a charity for a set period of time, but then leave the principal to their heirs.

- Charitable remainder trusts do the exact opposite of a CLT. CRT's provide a stream of income to the donor while living, and the remainder is then left to the charity at the donor's passing.

Charitable trusts come in all shapes and sizes. There are several different variations of CLTs and CRTs so it's important to visit with your estate planning attorney to find the trust that best fits your needs. Charitable trusts are irrevocable, so once you transfer your assets into the trust you no longer own them.

When it comes to charitable giving, the available options can seem daunting. If you'd like to discuss the options in greater detail, feel free to reach out to your financial advisor or estate planning attorney. If you'd like us to recommend an attorney that specializes in charitable giving, we can do that too. We look forward to hearing from you!

# 'Don't Stop 'Til You Get Enough' Estate Planning

*by Adam Lawrence, CPA*

With more than 400 million records sold, 15 Grammys won, and instantly recognizable by billions of fans worldwide, Michael Jackson was a pop culture icon who certainly earned his perennial title, "The King of Pop." Despite grossing close to $2 billion throughout his career, however, no amount of success could prepare him for what was to come posthumously – a very messy estate fight.

The alarming thing is that Jackson already had a will. And not just a will, but a living trust that estate planning attorneys had set up for him while he was alive. What's even more alarming, however, is that up to 60% of Americans haven't even set up a simple will. With Michael Jackson's estate stuck in probate limbo for the last 13 years, even with a will and estate plan in place before his death, are you confident that your estate plan is sounder than his was?

Never fear, estate planning is easy to get out in front of as long as you plan well in advance. You can set up a will at any point in life, but the earlier the better. It's also best to be as specific and detailed as possible and review it from time to time with your attorneys and advisors, to ensure the plan still aligns with your goals and life changes.

Despite Jackson's estate planning shortcomings, one thing that was not up for interpretation was to whom his assets would go, and how much: 40% to his kids, 40% to his mother, and 20% to various charities. Jackson also set up a living trust, legally known as a revocable trust, while he was alive. Creating a revocable living trust establishes a separate legal entity that allows you to transfer all your assets into the trust while you're alive, such that it's protected from lawsuits and the eyes of the public.

Unfortunately, though, the trust did not go far enough in protecting Jackson's assets as intended. First, Jackson did not place all his assets in the trust, and second, the trust left the assets to the beneficiaries outright, making the assets vulnerable to action from lawsuits, creditors, and unforeseen life events. An irrevocable trust, such as Lifetime Asset Protection Trust, could have mitigated this risk by keeping the assets in the trust at the time of Jackson's passing and distributing living expense allowances to each of the beneficiaries as dictated by the estate plan over time. If Jackson had been reviewing his estate plan with his advisors and attorneys, he could have helped shepherd the fate of his estate ahead of time.

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It's important not to overlook the potential emotional and psychological stress that arises when these sometimes-difficult conversations about life and death arise. However, I can promise that you'll definitely sleep better at night knowing that your loved ones will be taken care of with an ironclad estate plan in place. A comprehensive estate plan will also help your loved ones avoid untold amounts of legal costs, effort, and stress that too many have tacked on to what is often already a difficult period.

If you want to avoid these worries that are just 'human nature,' Financial Synergies can connect you with an experienced estate planning attorney who won't leave it up to chance for 'Billie Jean' to decide who "the one" is.

## Save the Date!

Already Gone (Eagles Tribute Band) Concert Event at The Heights Theater 10/26/2022 - More Details to Come!

# Seeing Red

*by Mike Minter, CFP®, CFS®*

The first quarter of 2022 was rough, and your upcoming quarterly statements are not going to be any fun to look at. You'll be seeing red (okay technically we don't use the color red, but negative numbers).

Inflation, interest rates, supply chain issues, and Ukraine have all taken a toll on the markets. It wasn't catastrophic, and certainly we've had WAY worse quarters in the last twenty years, but it was still unsettling for many investors.

One thing in particular that set this quarter apart from other market declines was the performance of bonds. It's not often we see bonds going down when stocks are on the decline. It happens, but it's rare.

Bonds actually declined more than the broad stock market (S&P 500) during Q1. You can see that stocks still lived up to their reputation as the more volatile asset class, but ultimately bonds lost more.

It's no secret why bonds are struggling, as we've discussed this many times recently. One of the key determinants of bond performance is prevailing interest rates –

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bond prices have an inverse relationship with interest rates. Obviously rates are on the rise so prices are on the decline.

January 2022 was one of the worst-performing months for the Bloomberg US Aggregate Bond Index (the Agg) during the past 20 years. Much of the blame can be placed squarely on steadily increasing rates. Yields on the benchmark 10-year US Treasury note spiked from 1.49% at the start of the current year to 2.00% in early February.

But remember, bonds by an overwhelming margin usually go up when stocks hit a rough patch. Let's take a trip down memory lane and revisit some of the worst stock market quarters of the last twenty years.

Bonds Are Usually Positive When Equities Decline

S&P 500 Index Largest Quarterly Losses Since 2001 vs. the Agg (%)

| Quarter | S&P 500 Index | Bloomberg US Aggregate Bond Index |
|---|---|---|
| Q4 2008 | -21.94 | 4.58 |
| Q1 2020 | -19.60 | 3.15 |
| Q3 2002 | -17.28 | 4.58 |
| Q3 2001 | -14.68 | 4.61 |
| Q2 2011 | -13.87 | 3.82 |
| Q4 2018 | -13.52 | 1.64 |
| Q2 2002 | -13.40 | 3.69 |
| Q2 2010 | -11.43 | 3.49 |
| Q1 2001 | -11.86 | 3.03 |
| Q1 2009 | -11.01 | 0.12 |
| Q1 2008 | -9.44 | 2.17 |
| Q3 2008 | -8.37 | -0.49 |
| Q2 2015 | -6.44 | 1.23 |
| Q4 2007 | -3.33 | 3.00 |
| **Average Return** | **-12.65** | **2.74** |

**Past performance does not guarantee future results.** As of 1/31/22. Indices are unmanaged and not available for direct investment. Source: Morningstar Direct.

We were glad to own bonds during these turbulent times for stocks. And even though this past quarter didn't see bonds protecting us as stocks declined, it doesn't negate the long-term benefits of holding bonds in a diversified portfolio.

And we should be careful not to extrapolate these negative bond returns out into the future and just assume that because rates may go up that bonds will continue to lose money forever. That simply has not been the case historically. More often than not, bonds are in positive territory after a period of rate hikes.

One of the more dramatic rate hike periods was from 2004-2006, when the Fed raised rates 17 times in a row!

Bonds were up almost 6% over these two years. And six months after the Fed had raised rates for the 17th time, bonds were up another 5%. *Source: YCharts

Now, I'm not saying that this data guarantees bonds will turn the corner next month and end the year in positive territory. Only that we have to be careful in assuming the worst for bonds going forward.

In the short run, rising interest rates may negatively affect the value of a bond portfolio. However,

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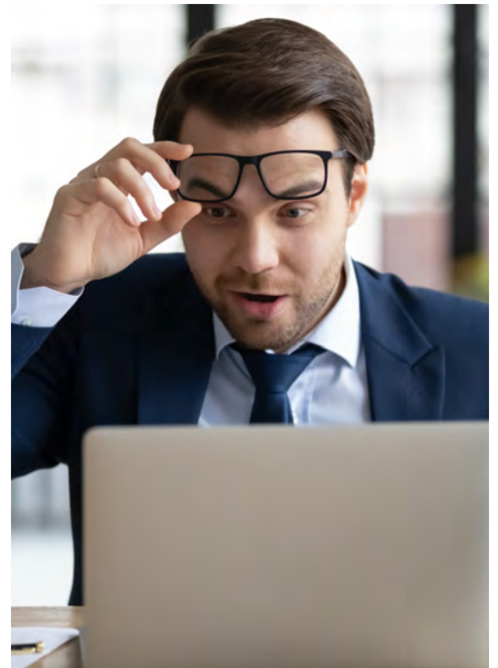
over the long run, rising interest rates can actually increase a bond portfolio's overall return. This is because money from maturing bonds can be reinvested into new bonds with higher yields.



At the end of the day, bonds are still the ultimate shock absorber against a stock market downturn. And this relationship will revert to its mean eventually.

**CONCLUSION**

We know seeing your portfolio down in value is not fun, and can be a source of real anxiety. This is not something we take lightly.

We are invested in the same funds and in the same manner as our clients. In other words, "we eat our own cookin'." We also know this won't last forever, and diversification will eventually win the day.

From a strategy standpoint, many of our active bond fund managers have taken the following steps:

- shortened duration (lessened rate sensitivity)
- rotated into sectors with more attractive characteristics during
- rising rates gone into overseas markets when necessary
- entered private markets when optimal from a risk perspective

These shifts take time to play out, but we feel confident in our positioning going forward.

# Welcome Baby Jonah!

We would like to extend our warmest congratulations to Zach Robinson (our Director of Client Service) and his wife Rose Kelly Robinson in welcoming their son Jonah on February 24th.