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Financial Perspectives

Spring 2017

Market Sunshine Causes Investment Portfolios to Grow

Tips to Prune Portfolios Sprouting with Recent Market Performance

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Just as we are seeing the green buds of spring flowers start to emerge thanks to some early warm weather, the sun has been shining on many investments as well. Even in the past few weeks, many indexes continue to hit new highs. While it can be tempting to stay inside and leave everything on autopilot, bull markets present more for the savvy investor than just the chance for higher account balances.

Dig up your asset allocation. When investment values change disproportionately, it can cause your asset allocation to get out of balance. Is the mix between your equity and fixed income investments still appropriate? What about your various equity positions? For example, in 2016 small and mid-cap asset classes outperformed international investments. Consequently, your allocation to these categories may have grown out of balance with your small and mid-sized companies outgrowing your international investments. Take a look at all of your investments and make sure you have good diversification and a mix that is still in line with your investment objectives and risk tolerance. If what you need to reposition is at a large gain in your taxable portfolio, consider making those changes in your tax-deferred portfolio – such as within your IRA accounts – to minimize taxes.

Protect your portfolio from an early frost. Especially as you approach retirement or other goals, consider whether now is a good time to shift your balance from growth oriented investments to those that are better suited to meet near-term goals such as fixed income. By repositioning during market highs, you will be capturing those elevated values as you move into a more appropriate balance.

Don't be too quick to turn over a new lifestyle leaf. While it can be tempting to want to accelerate purchases when we see our account balances at higher levels, it isn't always the best financial decision. Take a longer-term approach and don't be too quick to adjust your spending goals based on near term appreciated values.

Plant the seeds of giving by using appreciated stock. When stock values are high, it is an especially good time to consider making charitable gifts using stock rather than cash to lock in those appreciated values. The higher the value of your gift, the larger the charitable deduction. Moreover, the charity can sell the stock and not face any tax on the appreciation. You can make these gifts directly to a charity or through other vehicles – such as a donor advised fund – which allow you to get a charitable deduction upfront for making future gifts to the charities of your choice.

Prune any overgrowth of hardy plants. If you have concentrated equity positions that comprise a large percentage of your portfolio, consider cutting them back. Prudent investment standards suggest holding no more than 15% of your overall mix in any one security.

Make sure you have set aside ample cash to weather any market storms. An appropriate cash balance guideline is an amount equal to 3-6 months of living expenses.

Pull some weeds. Do you hold positions that you aren't in love with, but didn't want to sell because the value was too low? Maybe you received them as a result of a spin-off or a merger. Consider whether now is a good time to do some necessary portfolio clean-up work.

Spring Cleaning for Other Areas of Your Financial Life

Just like your home can use a good scrubbing every year around this time, spring presents a great opportunity to get things in order in your financial house as well. And while it's good to focus on your investment portfolio – as described above – there are other areas of the "house" that you should take a good look at as well.

Banking

The basics: Consolidate multiple accounts into one place, where possible; streamline your flows with electronic statements and online bill pay; throw out old statements and checks.

The details: Particularly if you've moved once or twice, you may find that you have more than one bank account – which also means you have mulitple statements coming in each month. Bank accounts are easy to keep open, but you might be incurring fees for those, and you can easily avoid them. It may be tempting to use different accounts for different reasons, piling up benefits and perks along the way. But most people can benefit by consolidating with a single financial institution.

Credit Cards/Debt

The basics: Check your credit report; shop for lower interest rates; develop a payment strategy.

The details: A change of 100 or even 50 points in your credit score can mean the difference between great loan terms and awful ones; inaccuracies in your credit report can drop your score down at least that much. You can check your scores from the three credit bureaus – free of charge – each year at www.annualcreditreport.com. If you see a problem, you can dispute it (in writing) and you'll usually have a resolution within a month. Once you have an accurate credit report, check the interest rate you're paying on any credit card balances and compare that rate with the many other cards available; you may find some instant savings or better benefits elsewhere. Credit card companies aren't shy about raising your rate, but even if they haven't, sometimes you can negotiate a better deal. If you do have any outstanding balances you've been meaning to take care of, tackle high-interest credit card debt first to get the biggest bang for your buck.

Estate Planning

The basics: Create or update a will or trust if you don't have one; consider a living will and financial power of attorney; clean out old documents you don't need any more.

The details: If you don't have a will or trust, you should take the time now establish one. Not only will it give you peace of mind having your financial affairs in order, it can also provide for your beneficiaries and prevent them from having to figure out your estate should something happen to you. Any property at all – your home, a car, a flat-screen TV, or even jewelry (which can have sentimental as well as real value) can be accounted for in your will or trust, and this will assure distributions make it to the right person upon your passing. Now is also a good time to think about a power of attorney, which specifies someone trustworthy to handle your finances if you become too ill to take care of them yourself. Once you've had these drawn up, don't just shelve them and forget about them; annual reviews are important, because as you experience changes in life your estate documents may need to be updated accordingly. And make sure to get rid of old documents as you update to new ones; this will elimnate any confusion as to your intent.

Retirement Accounts

The basics: Consolidate accounts; rebalance; update beneficiaries.

The details: Building the wealth to allow you to retire comfortably requires diligent saving and good investment decisions. But you can also get tied up in too many details and accounts. If you've changed jobs several times, and have multiple accounts, you may consider consolidating any old 401(k) accounts into the one at your current job, or into an IRA. An advisor can help you decide what's best. It's also important to rebalance regularly, to mitigate the effects of market volatility, and make sure beneficiaries are current as well.

Insurance

The basics: Get new quotes for car, home and life insurance policies; update your beneficiaries.

The details: Make sure you're fully covered in case of an unfortuante event. In some areas of the country, auto and homeowners insurance rates have gone down in recent years and shopping around could save you money. Major life events need to be taken into consideration, as they could require increased coverage (for a new baby) or beneficiary changes (death or divorce) as well.

Permanent Life Insurance as an Asset Class

For many people, it may be hard to imagine any type of insurance premium as an asset rather than a liability. Most types of insurance such as auto, home, and health will simply reimburse a policyholder for an event that they hoped never would have happened. Not to be morbid, but with permanent life insurance an event is being covered that is certain to occur: death. It's not a matter of if a benefit will be paid, it's a matter of when. So, as long as the proper premium is paid, an income tax-free death benefit will be paid upon the death of the insured(s), resulting in a rate of return calculation that is not available with other types of insurance.

Life Insurance Can Enhance a Legacy

Some people have a surplus of assets and income that will never be needed in retirement. These individuals or couples are often saving and investing to increase their net worth to leave more to their heirs and/or to charity as a legacy. In situations like this, utilizing existing assets to purchase life insurance can be an effective way to enhance a legacy by securing a significantly higher death benefit than the premiums paid into a contract. A permanent life insurance death benefit will offer not only an attractive rate of return, but it will also provide a substantial degree of certainty, and can insure against "mortality risk" (the risk that the insured may not live long enough for their assets to grow to the amount desired to leave their children) and "market risk" (the risk that investments might perform worse than expected). In addition, tax erosion can be avoided with life insurance as death benefits are typically paid without income tax being assessed to the beneficiaries.

To give an example of how this might work, take a look at the table below. The table assumes that a 55-year-old male was able to qualify for a life insurance policy with a $1,000,000 death benefit. If he was in good health and a non-smoker, the lifetime annual premium for this policy might be $13,629. The chart* indicates what the Internal Rate of Return (IRR) would be if he were to die in a specified year. The Pre-Tax Equivalent IRR illustrates the effect of an income tax-free death benefit could have the on the return (assuming a 35% federal tax bracket).

Year	*Age*	*Premium*	*Death Benefit*	*Death Benefit IRR*[1]	*Pre-Tax Equivalent IRR*[2]
5	60	$13,629	$1,000,000	108.21%	166.48%
10	65	$13,629	$1,000,000	34.92%	53.73%
15	70	$13,629	$1,000,000	18.21%	28.02%
20	75	$13,629	$1,000,000	11.23%	17.28%
25	80	$13,629	$1,000,000	7.53%	11.58%
30	85	$13,629	$1,000,000	5.28%	8.12% [LE]
35	90	$13,629	$1,000,000	3.79%	5.84%

*Hypothetical illustration courtesy of The Lincoln National Insurance Company

(1) The Internal Rate of Return (IRR) is the rate at which Outlays up to that year must be compounded each and every year to generate the death benefit. At life expectancy (LE), an alternative investment must have earned 5.28% after-tax to equal the IRR on the death benefit.

(2) Pre-tax Equivalent is the pre-tax rate that an alternate investment must have earned to equal the IRR on death benefit. At LE, an alternative investment must have earned 8.12% pre-tax to equal the IRR on the death benefit (using an assumed tax bracket of 35.00%).

LE: Life expectancy based on the 2008 Valuation Basic Table (2008 VBT), which is published by the Society of Actuaries and appropriate for someone recently underwritten for life insurance. This Table varies by gender and smoker status, but is not tailored to specific underwriting classes. Mortality tables such as 2008 VBT provide a basis for various financial calculations but do not predict any individual's future life span. While these statistics are a useful reference tool, keep in mind longevity is affected by many factors (lifestyle, occupation, health problems, family history of longevity, etc.).

Your Financial Advisor Can Help

Life insurance can play an important role in your financial and legacy plans, and the amount and type of coverage to purchase can vary based on individual circumstances. Contact your advisor to discuss your specific situation and whether or not life insurance might be a good fit for your legacy plans.

A Few Tax-related Deadline Reminders

April 3	Taking required minimum distributions from traditional IRAs if you reached age 70½ in 2016
April 17	Filing 2016 income tax returns Paying first-quarter 2017 estimated taxes Opening and making contributions to traditional IRAs, Roth IRAs and Coverdell Education Savings Accounts for 2016 Establishing and funding SEP IRA plans for sole proprietors and partnerships for 2016 (unless filing under extensions)

Market Recap

Market Summary (As of February 28, 2017)

	Year-to-Date	Trailing 12-Months	3-Year Annualized	5-Year Annualized
DJIA	5.31%	26.00%	8.44%	9.95%
Nasdaq	8.22%	27.81%	10.58%	14.29%
Russell 2000	2.33%	36.11%	6.93%	12.89%
S&P 500	5.57%	22.23%	8.33%	11.60%

Sources: Benjamin F. Edwards & Co. and Bloomberg

	U.S. Treasury Yields
Two-year	1.28%
Five-Year	1.99%
10-year	2.45%
30-Year	3.06%

Source: Bloomberg (as of Mar. 1, 2017)

U.S. Stocks

Performance of S&P 500: Index Price Returns

for Periods Ended Feb. 28, 2017

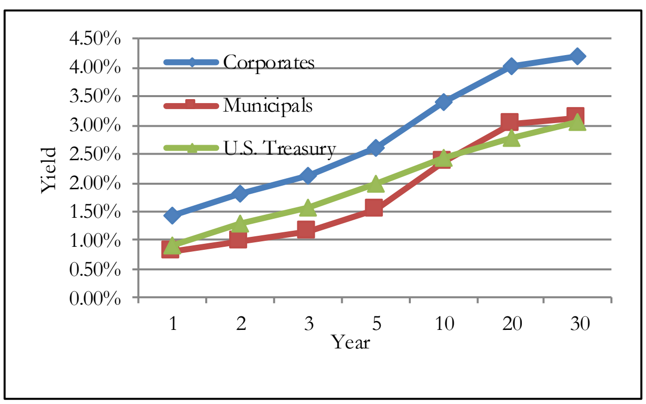
Sector	Weightings	Year-To-Date	Trailing 12-Months	Five-Year Annualized
Info. Technology	21.50%	9.42%	30.85%	13.33%
Financials	14.80%	5.14%	43.29%	15.43%
Health Care	14.10%	8.49%	13.16%	15.65%
Cons Discretionary	12.10%	6.08%	16.44%	15.02%
Industrials	10.20%	4.82%	24.80%	12.02%
Cons Staples	9.40%	6.39%	8.58%	10.64%
Energy	6.60%	-6.27%	22.71%	-1.39%
Utilities	3.20%	5.98%	11.82%	8.22%
Materials	2.80%	5.12%	25.02%	7.01%
Real Estate	2.90%	4.29%	10.81%	7.89%
Tele. Services	2.40%	-3.87%	4.55%	5.59%

Ranked by highest to lowest index weightings; Weightings may not equal 100 due to rounding
Source: S&P®

- Many economists believe the corporate earnings recession has ended. Almost 99% of the companies in the S&P 500 reported fourth quarter 2016 earnings, which may rise about 4.8% overall from a year ago – better than the 2.9% growth during the third quarter. About 65% of companies in S&P 500 reported earnings that exceeded estimates, just short of the five-year average of 67%. S&P is projecting 10.4% earnings per share growth in 2017 for the S&P 500 index ($129.93 versus $117.68 for 2016).
- As of the end of February 2017, the S&P 500 price/earnings multiple based on the 2017 EPS Estimate ($129.93) was 18.19x. The current bull market celebrated its eighth anniversary on March 9, 2017. According to S&P, prior bull markets since World War II recorded a trailing 12-month P/E multiple high of 26x and a low of 9x. Recently, the P/E ratio based on trailing earnings was 23.08x. In addition to higher earnings growth in 2017, investor confidence has been predicated on – and will continue to be impacted by – President Trump's delivery on his campaign promises of tax cuts, regulatory reform, increased infrastructure spending and a successful replacement for the Affordable Care Act. Investors will likely also be sensitive to any level of discord amongst members of the Trump Administration.

Fixed Income

Fixed Income Yield Curves (As of March 1, 2017)



Sources: Bloomberg, Bloomberg US Corporate (A) Fair Value Index, Thomson Reuters MMI

- With the Federal Reserve (FED) completing their only interest rate increase for 2016 in December, all signs are that they are going to move earlier in 2017. The market has currently priced into the short maturity end of the treasury curve a 98% chance that the Federal Open Market Committee will raise rates at the next meeting on March 15th. If the committee does move the Federal Funds Rate will move from 75 bps to 100 bps or 1%. In our last installment, we pointed out that the spread between the 2-year treasury and 30-year treasury was 1.49% that has currently widened out to 1.80%. The average spread over the last 5 years has been 2.48%
- The municipal bond market has rallied back from a sell off we saw in earlier December; a large portion of the strength has been from a supply demand imbalance as municipal issuers have not been coming to the primary market as aggressively. Recently with the imminent rate rise and new issuance starting to pick up we have seen interest rates increase on the longer dated securities.

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