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*Frank*ly Speaking©

Welcome to the Q4-2019 issue of *Frank*lySpeaking©, now in its 27th year. The purpose of this newsletter is to keep you informed of current issues and global events that could impact your finances. Please feel free to share your thoughts with us, as we welcome your comments.

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In This Issue

Economic and Market Commentary

Economic growth remains relatively firm but is expected to slow to 2%. While the US economy continues to stand on relatively firm ground compared to many other large economies, GDP growth is moving towards its long-run trend of 2%.

Factors influencing economic growth include slightly softer but still solid consumption and job growth trends, weakening business investment, a pick-up in residential investment and continued monetary easing.

Consumer spending is also expected to slow slightly in the coming quarters, compared to an especially strong second quarter, but will continue to support economic growth.

On the other hand, job growth remains on a slowing trend, but is still growing fast enough to further tighten the labor market. The unemployment rate now stands at a fifty-year low.

Despite robust consumer confidence, business confidence continues to weaken and will negatively impact investment.

Manufacturing sentiment weakened again in September with the Purchasing Managers' Index dropping further into contractionary territory. This weakness now appears to be spreading into the services sector with the most recent non-manufacturing Purchasing Managers' Index reporting softer though it remained strong.

Following sluggish residential investment numbers in 2018 and early 2019, recent data on housing permits and starts suggests that a strengthening trend may be ahead. This improvement should help offset some of the softening in consumer spending or nonresidential business investment.

Following two rate cuts earlier this year markets are now expecting further easing by year-end. The Federal Reserve is expected to ease by one additional 25 bps in 4Q19 to stimulate the economy via lower-cost business loans and mortgages.

Financial markets have had a good run. The labor markets in the US and parts of Europe are very strong along with solid corporate earnings.

Companies have solid balance sheets, loan defaults remain rare, oil is affordable and there's no risk of interest-rate hikes.

So far, so good, but there are an array of disturbing warning lights flashing in front of us.

The most glaring of the warning lights is that the US yield curve has inverted, which in the past has usually signaled an approaching recession.

The U.S. Federal Reserve (the Fed) is clearly nervous and has already implemented preemptive interest-rate cuts.

In Europe, meanwhile, the European Central Bank (ECB) will probably adopt a whole new package of monetary measures and new calls for fiscal stimulus are on the table.

Investors are struggling to reconcile the apparently good economy with the many warning signs. Complicating things still further is that many don't have to think back very far to remember some very costly mistakes.

Those who took heed of the warning signals in the past and got out of the equity market quickly, lost out because every setback since 2009 has proven just a brief pause in the enduring rally.

This makes everyone more cautious now about predicting recession or saying the bull market is over, but even the bulls themselves are not suggesting that recessions have been banished forever.

The troubling gap between the happy economy and the anxious mood is perhaps most powerfully demonstrated by the yield curve. This has happened nine times in the U.S. since 1956 and recession has tended to follow, within two years.

There are many reasons to be concerned about the medium term, but we believe that it is too early to talk about an imminent crisis because there is too much positive data.

One reason for that may be the steadily growing service sector, which does not have inventory and invest-ment cycles as large as those of the manufacturing sector. In addition, the good labor markets mean consumers are still spending heavily.

Finally, the expected slight economic slowdown reduces the risk of overheating and means central banks have again softened their policies.

Mortgage Rates Remain Steady

MCLEAN, VA, October 3, 2019 (Globe Newswire) - Freddie Mac (OTCQB: FMCC) today released the results of its Primary Mortgage Market Survey® (PMMS®), showing that the average 30-year fixed-rate mortgage averaged 3.65%.

The 30-year fixed-rate mortgage (FRM) averaged 3.65% with an average 0.6 point for the week ending October 3, 2019, slightly up from the previous week when it averaged 3.64%. A year ago, at this time, the 30-year FRM averaged 4.71%.

The 15-year FRM averaged 3.14% with an average 0.5 point, down from the previous week when it averaged 3.16%. A year ago, at this time, the 15-year FRM averaged 4.15%.

The 5-year Treasury-indexed hybrid adjustable-rate mortgage (ARM) averaged 3.38% with an average 0.4 point, unchanged from the previous week. A year ago, the 5-year ARM averaged 4.01%.

As of January 1, 2016, the PMMS no longer provides results for the 1-year ARM.

(Average commitment rates should be reported along with average fees and points to reflect the total cost of obtaining the mortgage. Borrowers may still pay closing costs which are not included in the survey.)

Sam Khater, Freddie Mac's chief economist, reported that even though mortgage rates generally held steady, overall mortgage demand remained very strong, rising over 50% from a year ago thanks to increases in both refinance and purchase mortgage applications.

He also noted that as economic growth decelerates, low mortgage rates will continue to support the mortgage market and is expected to persist for the remainder of the year.

Tax Rules When Selling Your Home

How the gains from the sale of a primary residence are taxed has changed in recent years.

If you have recently sold your home, or are considering doing so, you may want to be aware of these new rules.

If you owned and lived in your home for two of the last five years prior to the sale, then up to $250,000 of profit may be exempt from federal income taxes. If you are married and file a joint return, then it doubles to $500,000.

To qualify for this exemption, you cannot have excluded the gain on the sale of any other home within two years prior to this sale.

Any profit would be excluded from your taxable income. In fact, the sale may not need to be reported unless you receive a Form 1099-S or do not meet the above requirements.

Unfortunately, you can't deduct any loss if you sold your home at a loss.

There are certain exceptions where you may qualify for this exclusion even if you do not meet the requirements discussed above.

If you receive the house in a divorce settlement, you are able to count short-term absences as time lived in the house or if you are a surviving spouse, who has not remarried, you can count the time that the deceased spouse lived in the house.

The five-year test period can also be suspended for up to ten years in cases where any spouse has served on qualified official extended duty as a member of the military, foreign service, or federal intelligence agencies.

Even if you don't pass the five-year rule test, a reduced exclusion may be available if you have a change in employment or health, or because of unforeseen circumstances, such as divorce or multiple births from a single pregnancy.

We recommend that you consult a professional with tax expertise regarding your individual situation.

Your "Will" Power

Only 45% of adults have a will or other estate documents in place, which may not be entirely surprising.

No one wants to be reminded of their own mortality or spend too much time thinking about what might happen once they're gone.

A will is an instrument of power. Creating one gives you control over the distribution of your assets.

If you die without a will, the state decides what becomes of your property, without regard to your priorities.

A will is a legal document by which an individual or a couple, identify their wishes regarding the distribution of their assets after death. A will can typically be broken down into four main parts.

Executors - Most wills begin by naming an executor. Executors are responsible for carrying out the wishes outlined in a will.

This involves assessing the value of the estate, gathering the assets, paying inheritance tax and other debts, if necessary, and distributing assets among beneficiaries.

It is recommended that you name at least two executors in case your first choice is unable to fulfill the obligation.

Guardians - A will allows you to designate a guardian for your minor children. Whomever you appoint, you will want to make sure beforehand that the individual is able and willing to assume the responsibility.

For many people, this is the most important part of a will since, if you die without naming a guardian, the court will decide who takes care of your children.

Gifts - This section enables you to identify people or organizations to whom you wish to give gifts of money or specific possessions, such as jewelry or a car.

You can also specify conditional gifts, such as a sum of money to a young daughter, but only when she reaches a certain age.

Estate - Your estate encompasses everything you own, including real property, financial investments, cash, and personal possessions.

Once you have identified specific gifts you would like to distribute, you can apportion

the rest of your estate in equal shares among your heirs, or you can split it into percentages. For example, you may decide to give 45% each to two children and the remaining 10% to a sibling.

The law does not require that a will be drawn up by a professional, and some people choose to create their own wills at home. But where wills are concerned, there is little room for error.

You will not be around when the will is read to correct technical errors or clear up confusion.

When you draft a will, consider enlisting the help of a legal or financial professional, especially if you have a large estate or complex family situation.

Preparing for the eventual distribution of your assets may not sound enticing. But remember, a will puts the power in your hands.

You have worked hard to create a legacy for your loved ones and you deserve to decide what becomes of it.

History of Estate Taxes

Federal estate taxes have been a source of funding for the federal government almost since the U.S. was founded.

In 1797, Congress instituted a system of federal stamps that were required on all wills offered for probate when property such as land and homes was transferred from one generation to the next.

The revenue from these stamps was used to build the navy for an undeclared war with France, which had begun in 1794. When the crisis ended in 1802, the tax was repealed.

Estate taxes returned in the build-up to the Civil War. The Revenue Act of 1862 included an inheritance tax, which applied to transfers of personal assets. In 1864, Congress amended the Revenue Act, added a tax on transfers of real estate, and increased the rates for inheritance taxes. As before, once the war ended the Act was repealed.

Fast Fact: Between 2016 and 2025, the estate tax will generate about $246 billion in revenues..

In 1898, a federal legacy tax was proposed to raise revenue for the Spanish-American War. This served as a precursor to modern estate taxes. It instituted tax rates that were graduated by the size of the estate. The end of the war came in 1902, and the legacy tax was repealed later that same year.

The 16th Amendment to the Constitution was ratified in 1913 which gives Congress the right to "lay and collect taxes on incomes, from whatever source derived."

The Revenue Act of 1916 established an estate tax, and in one way or another, it's been part of U.S. history since then.

In 2010, the estate tax briefly expired, however in December 2010, Congress passed the Tax Relief Act of 2010 and the new law retroactively imposed tax legislation on all estates settled in 2010.

In 2012, the American Tax Relief Act made the estate tax a permanent part of the tax code.

As part of the 2017 Tax Cuts and Jobs Act, estate tax rules were again adjusted. The estate tax exemption was raised to $11.2 million, a doubling of the $5.6 million that previously existed. Married couples may be able to pass as much as $22.4 million to their heirs.

The 2017 Act is set to expire in 2025, so it's possible the estate tax law may be adjusted at least once during the next few years.

If you're uncertain about your estate strategy, it may be a good time to review the approach you currently have in place.

News Versus Noise

One of our tasks for making prudent investment decisions is to identify geopolitical disruption that really matters for the economy and markets and ignore the events that are just background noise.

In today's electronic communications world, there are three major headlines that can be classified as news versus noise in relation to their potential longer-term impact on the markets. A possible impeachment in the US, the ongoing Brexit saga and the US-China trade situation.

The US House of Representatives has begun an impeachment inquiry into President Donald Trump following the revelation of a whistleblower report related to national security.

The report alleges that Trump utilized his position to attempt to pressure the president of Ukraine to investigate his political rival, former Vice President Joseph Biden.

While this is a serious allegation, this development has little relevance to both the economy and markets. Stocks barely responded to the headlines.

If, at the end of the inquiry, something dramatic were to happen, there could be more volatility and even a sell-off. However, nothing in the timeline of the next few months suggests developments that could heighten economic policy uncertainty.

In an extremely unlikely worst-case scenario in which the president was to actually be impeached, he would be replaced by a vice president who is part of his administration and would likely continue with all the same policies. Additionally, the Fed would likely remain very accommodative, which should also be supportive of equities.

The Brexit drama continues and this is relevant for the economy and markets because it has been creating a high level of economic policy uncertainty, which has historically deterred business investment.

Recent developments have served to increase optimism that the UK will avoid a no-deal Brexit.

Nevertheless, there is also a recognition that the economy has already come under pressure because of a major rise in economic policy uncertainty, which has deterred business investment and that this damage is likely to continue even if the UK does not crash out of the European Union (EU).

A member of the Bank of England's Monetary Policy Committee emphasized this point by saying that persistently high uncertainty, even if the UK reaches a deal with the EU, will likely make it appropriate for the Bank of England to maintain an accommodative monetary policy stance and possibly cut rates further.

This ongoing Brexit drama could substantively impact the economy as well as UK equities, gilts, and the British pound, at least in the short to medium term.

The US-China trade situation matters for the economy for the same reason that Brexit matters for the economy. It can significantly increase the level of economic policy uncertainty, which can deter busi-

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ness investment and other spending.

However, we caution any overreaction. We believe the US will become increasingly desirous of reaching a trade agreement as we move closer to the 2020 presidential election.

There will be additional similar reports or threats that are likely to become more routine given the impeachment inquiry, as well as the presidential election and they are likely to be disregarded as well.

We will remain cautious because if any such threat were to be carried out, it would dramatically elevate the level of economic policy uncertainty with economic and market consequences.

It is worth noting that China is not taking a similar, more protectionist stance in response. Chinese regulators have recently made significant actions to demonstrate that the government is taking steps toward financial market liberalization by removing impediments to foreign institutional investments into China.

Beijing recently removed a $300 billion cap on foreign investments to onshore Chinese equities. While the US may continue to threaten more protectionist policies with China, it still seems unlikely that the US will embark on a financial decoupling from China. One reason is that too many US businesses are dependent on business in China to help fuel their growth.

We will be prepared for almost anything to be reported, given a growing interest by the US in reaching a deal with China as well as the administration's desire to take attention off impeachment proceedings.

Geopolitical disruption is expected to continue for the near term and could become more unpredictable.

In the case of trade developments, it could lead to increased volatility for stocks and Treasuries.

We expect such volatility and view it as a reminder of the importance of broad diversification to mitigate risk.

Additionally, we will take advantage of opportunities created by downward volatility in order to acquire oversold assets.

Benefits of Working In Retirement

Retirement has been considered an ending, the exit from your years in the workplace. The rules are shifting. Participation for those aged 65-74 is predicted to reach 32% by 2022, up from just 20% today.

As the Boomer generation ages, more people are viewing retirement as an opportunity to enjoy the rewards of work in a whole new way. Working during retirement helps maintain mental agility as you learn new skills and staying engaged can lessen the risk of developing dementia and is crucial for continued health.

Studies have shown that a sense of purpose has been found to lengthen lifespan and quality of life.

Besides the obvious extra income, working during retirement may allow you to delay taking Social Security benefits, allowing them to increase 8% annually.

Working on something you care about, starting a new business, or mentoring others in the workplace can ward off depression and provide a healthy sense of fulfillment and direction in your later years.

Working with others reduces this risk, giving you a chance to build connections and enjoy meaningful interactions.

Frankly Funny

An avid football fan on his way to the Sunday NFL game called the Miami Police Department to report a break-in.

He had inadvertently left two Miami Dolphin tickets on the front seat of his SUV and went into a grocery store for some tailgate treats.

When he came out, someone had smashed in his window and left two more tickets.