Volume XXVII
Number 2

Personal Financial Profiles, Inc.
EST. 1989 • FINANCIAL PLANNING…A CRITICAL INVESTMENT IN TIME ™

2nd Quarter
2019

Printed on Recycled Paper

*Frank*ly Speaking©

Welcome to the Q2-2019 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.

Most of all, when you are finished, be ecologically correct and recycle. Share it with a friend. Thank you for your continued support.

In This Issue

Economic and Market Commentary

There have been mixed signals obscuring our view to determine what are the underlying trends in the U.S. economy. The data have been sending conflicting messages, with some indicators suggesting momentum is relentless, while others hint at sharp deceleration, with most falling somewhere in between.

There were delays in the data flow as a result of the government shutdown, further complicating interpretation. Additionally, adverse weather, residual seasonality in some data series and the effects of the shutdown itself may have added to the confusion, temporarily weighing on measured activity early in the year.

As if that weren't enough, financial conditions have swung wildly, tightening sharply in Q4-2018 then reversing course in Q1-2019.

Add in unresolved trade tensions and a weaker, more uncertain backdrop abroad to raise still more questions about the U.S. outlook.

It appears that momentum has likely peaked and the economy seems to have slowed to a more moderate pace, reflecting the effects of weakening fiscal stimulus, tighter financial conditions, trade restrictions and possibly a weaker growth profile abroad.

The good news is the deceleration does not appear to be excessive, nor was it a surprise.

Economists have long felt that these restraining forces would edge the U.S. economy onto a more moderate trajectory and that such a moderation would be welcome, making it less likely that the kinds of excesses and imbalances, such as inflationary overheating and/or private-sector overindulgence, would emerge and kill any chances this expansion could continue.

Soft landings, where the economy glides onto a more sustainable path, curtailing potentially destabilizing excesses without jeopardizing the expansion, are hardly a sure thing and are never easy to pull off.

And like a flight during the descent phase, you can feel a bit queasy, especially if the economy encounters any air pockets or risk factors, of which there are plenty right now.

High on the list are trade tensions. The trade restrictions enacted so far, together with those potentially in the pipeline, have likely taken some toll on activity, in part by increasing uncertainty, weighing on investment plans and contributing to a tightening of financial conditions.

Most of the focus has been on the U.S.-China tiff, but there have been restrictions enacted on other fronts and potentially more to come. There are risks of more tariffs on European cars and even the renegotiated NAFTA deal isn't assured of legislative approval, although it remains likely.

Trade conflict is especially untimely when global activity is already unsteady. Momentum in Europe remains sluggish and uncertainty is prevalent in China.

All told, global drags could wash up a bit more powerfully onto U.S. shores than we had envisioned.

On the plus side, though, partial resolution of U.S.-China trade conflict may be coming soon, which would be enough to forestall any further tariffs and possibly reverse some of the restrictions already enacted.

Though it won't likely resolve all areas of contention between the U.S. and China, an agreement would reduce risks of an escalating trade war.

Closer to home, the end of the government shutdown removed another source of uncertainty. Still, it will take a while for the data backlog to clear, and for the mild drag from the shutdown to dissipate. Additionally, the shutdown may be indicative of a broader political dysfunction that raises questions about how the government will handle issues like raising the debt ceiling, which will need to be done later this year.

And then there are developments in financial markets. In Q4-2018, a combination of heightened volatility, sharp declines in equity and commodity prices, wider credit spreads and lower interest rates on government securities suggested that markets had not only downgraded their base-case expectations for economic growth, but increased their assessment of downside risks and the compensation they require for bearing those risks, not just in the U.S., but around world.

In 2019, a completely different narrative seems to have taken hold, with sentiment reversing sharply.

The question arises as what to make of these wild swings? Taking everything into account, U.S. financial conditions have tightened over the past year, enough to take away some incentive from activity, but hardly enough on its own to derail things, especially since many of other economic drivers remain broadly supportive.

Most encouragingly, the private sector still seems largely devoid of the kinds of large-scale excesses and imbalances that caused recessions in the past.

Humbled by the Great Recession, households and businesses, borrowers and lenders, savers and spenders and even regulators have been much more cautious this time around.

The economy also seems less vulnerable to the inflationary overheating that brought on recessions in past cycles, in part by provoking aggressive tightening by the Fed.

Labor markets are tight and wage pressures have been building, but recent indications suggest that the labor market may have a bit more running room or at least may not be tightening far beyond full employment, as some had feared.

Moreover, labor costs continue to pick up only modestly, to levels consistent with, but not threatening to surpass the Fed's inflation target.

Well-anchored inflation expectations, a more attenuated responsiveness of inflation to slack and temporary restraint from the stronger dollar and declines in commodity prices should also help prevent a material inflation overshoot and enable the Fed to tread carefully, avoiding the over-tightening that doomed past expansions.

All told, we think markets got strained late last year about the economic outlook. We still see activity slowing, but we don't see a recession in the near-term.

On the contrary, this expansion is apt to persist, becoming the longest ever by this summer and continuing even beyond that. In fact, if some of the near-term risks dissipate, the economy may even regain some strength, at least temporarily this spring and summer.

In short, even though soft landings are rare, they have happened before and for the reasons outlined above, the U.S. seems to have better odds of achieving one this time.

Fed policymakers are being patience right now, especially with an increasingly uncertain backdrop due to of signs of a possible slowing.

Policymakers are taking a prudent wait-and-see course to put interest rates on hold for now and wait for more clarity on how recent developments evolve and shape the outlook.

Inflation appears not to be in any danger of material overshoot and there is a growing recognition that they have already raised the funds rate a cumulative 225 basis points and have set the balance sheet on a path of decline.

We still believe that the Fed may eventually need to nudge the economy onto a more sustainable path with additional rate hikes, but not in the near future, and nothing until late 2019 or early 2020, at the earliest.

The Fed would likely require clear evidence that the downside risks have diminished, labor markets have resumed tightening and inflation is at least at target.

Where policy goes will depend on how the outlook evolves, but the range of probable outcomes is wider than it has been in recent years, because the outlook is cloudier and policy no longer so clearly accommodative and in need of an adjustment.

The funds rate will be the primary tool used to adjust policy stance and the balance sheet will be more of a secondary tool.

Barring any major shocks to the outlook, the size of the balance sheet will be dictated largely by technical considerations such as when reserves are enough to enable the Fed to control short-term interest rates.

Although there's uncertainty about just what that optimal level of reserve may be and when it might be reached, it is expected to be sometime between late 2019 and Spring 2020, when the cumulative reduction of Fed security holdings will reach their target.

Policymakers may opt to slow the pace of runoff as the end approaches to get more clarity on just where optimal reserve levels may lie.

After the runoff, Mortgage Backed Securities will likely continue to dwindle, replaced by Treasuries and the Fed may shift toward a somewhat shorter duration of Treasury holdings. But barring a renewed shock, the balance sheet will not likely be used as an active tool of policy.

Financial markets were on quite a wild roller coaster ride in Q4-2018 sparking a steep correction.

This was brought on by sharply increased anxiety as markets worried about slowing global growth, trade tensions, political dysfunction, perceptions of overly aggressive monetary policy and how difficult it will be for the U.S. to sustain its recent run.

More recently, many of these fears have receded and sentiment has recovered, albeit still not quite completely.

It is understandable why people grew more cautious. There was no shortage of things to worry about on the global front and, closer to home, we were concerned that markets might come to doubt the sustainability of the good news for the U.S. economic cycle.

The longer growth stayed above potential, the tighter labor markets became and the more the Fed hiked, the greater the risk that investors might turn persistently more cautious, increasingly aware that the most favorable phase of the economic cycle for financial assets may be behind us.

We believe that the recovery in Q1-2019 proved the worries late last year were totally overdone and we still see the overall macro backdrop with no recession on the horizon, no material inflation overshoot and a moderation to a more sustainable pace that enables the Fed to slow down, as broadly supportive of risk assets.

Mortgage Rates Had Biggest One-Week Drop in a Decade

MCLEAN, VA, March 28, 2019) - Freddie Mac (OTCQB: FMCC) today released the results of its Primary Mortgage Market Survey® (PMMS®), showing that the average 30-year fixed-rate mortgage dropped 22 basis points.

The 30-year fixed-rate mortgage (FRM) averaged 4.06% with an average 0.5 point for the week ending March 28, 2019, down from the previous week when it averaged 4.28%. A year ago, at this time, the 30-year FRM averaged 4.40%.

The 15-year FRM averaged 3.57% with an average 0.4 point, down from the previous week when it averaged 3.71%. A year ago, at this time, the 15-year FRM averaged 3.90%.

The 5-year Treasury-indexed hybrid adjustable-rate mortgage (ARM) averaged 3.75% with an average 0.3 point, down from the previous week when it averaged 3.84%. A year ago, the 5-year ARM averaged 3.66%.

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, not included in the survey.)

Sam Khater, Freddie Mac's chief economist, reported that the Federal Reserve's concern about the prospects for slowing economic growth caused investor jitters to drive down mortgage rates by the largest amount in over ten years.

He noted that, despite negative outlooks by some, the economy has continued to churn out jobs, which is great for housing demand.

He added that home sales have started to recover with the rate drop and were expected to continue rising with the additional purchase demand.

Roth IRAs & The New Tax Cuts & Jobs Act

The new Tax Cuts and Jobs Act (TCJA) makes Roth IRAs even more attractive and they can provide insurance against future tax rate increases.

Here's what you need to know about Roth IRAs and especially Roth IRA conversions in the post-TCJA world.

Roth IRAs have two big tax advantages. Qualified withdrawals are tax-free and you are exempt from rules to begin taking annual required minimum distributions (RMDs) after reaching age 70½.

You can leave your Roth account(s) untouched for as long as you live. This important privilege makes your Roth IRA a great asset to leave to your heirs

Qualified Roth IRA withdrawals are federal-income-tax-free and usually state-income-tax-free too. A qualified withdrawal is one that is taken after you, as the Roth account owner, have met two requirements. You've had at least one Roth IRA open for over five years and you have reached age 59½, become disabled or died.

The five-year requirement begins on the first day of the tax year for which you make your initial contribution to your first Roth account and can be a regular annual contribution or a conversion contribution.

Annual Roth contributions make the most sense for those who believe they will pay the same or higher tax rates during retirement.

The downside is you get no deductions for making Roth contributions.

If you expect to pay lower tax rates during retirement, you might be better off making deductible traditional IRA contributions because the current deductions may be worth more to you than future tax-free withdrawals.

Another scenario for annual Roth contributions is when you have maxed out on deductible retirement plan contributions. For example, you've contributed the maximum possible amount to your 401(k) plan at work. In that case, making Roth contributions is basically a no-brainer.

The absolute maximum amount you can contribute to a Roth account for any tax year is the lesser of: (1) your earned income for the year or (2) the annual contribution limit for the year.

Basically, earned income means wage and salary income, including bonuses, self-employment income, and alimony received that is included in your gross income.

If you are married, you can add your spouse's earned income to the total. For 2019, the limits are increased to $6,000 and $7,000, respectively.

The annual contribution privilege is phased out at higher incomes. For 2019, eligibility to make annual Roth contributions is phased out between modified adjusted gross income (MAGI) of $122,000 and $137,000 for unmarried individuals. For married joint filers, the 2019 phase-out range is between MAGI of $193,000 and $203,000.

The deadline for making annual Roth contributions is the original due date of your return, the same as the deadline for annual traditional IRA contributions.

After reaching age 70½, you can still make annual Roth IRA contributions, assuming there are no problems with the earned income limitation or the income-based phase-out rule. You cannot make any more contributions to traditional IRAs after you reach age 70½.

The quickest way to get a significant sum into a Roth IRA is by converting a traditional IRA to Roth status.

The conversion is treated as a taxable distribution from your traditional IRA, because you're deemed to receive a payout from the traditional account with the money then going into the new Roth account.

Doing so before year-end could trigger a bigger federal and state income tax bill for the current year.

If you convert in 2019, you will pay today's lower tax rates on the extra income triggered by the conversion and completely avoid the potential for higher future rates on all the post-conversion income that will be earned in your Roth account.

To be clear, the best candidates for the Roth conversion strategy are people who believe that their tax rates during retirement will be the same or higher than their current tax rates.

You could consider a multi-year conversion strategy where you can spread out a larger conversion amount over multiple years so all the extra income from converting could be taxed at a lower rate.

Low current tax cost for converting plus a potential insurance against higher tax rates in future years on income that will accumulate in your Roth account make sense for a Roth conversion strategy.

We recommend you speak to your tax adviser before making any decisions to confirm you've considered all relevant factors.

The Incredible Edible Car

There is an unintended consequence of going "Green" in the automobile industry. Cars just taste way too good!

Personal Financial Profiles, Inc.
EST. 1989 • FINANCIAL PLANNING... A CRITICAL INVESTMENT IN TIME ™

2801 University Drive
Suite 201B
Coral Springs, FL 33065
Phone: 954.755.8647
Fax: 954.755.6863
Email: fpugliese@pfprofiles.com

1415 Panther Lane
Suite 356
Naples, FL 34109
Phone: 239.598.9141
Fax: 239.598.9121
Email: dmaggio@pfprofiles.com

VISIT US ONLINE @ WWW.PFPROFILES.COM

Automobiles are sustaining substantial damage caused by rodents. Specifically, electrical wiring harnesses, air conditioning and heating ducts, seat cushions, trunks, SUV storage areas and carpeting.

Why does this happen? It can be understood by looking at the composition of the materials that are eaten and discover they contain soy, rice husks, wood, sugars, sweet smelling substances like vanilla, peanut oil and straw.

In the past, automotive Original Equipment Manufacturers (OEMs) made almost everything in the car from metal, glass and plastic which was made from petroleum, none of which were particularly tasty or suitable for nest building by rodents.

Then in the mid-1980's, Euro politicians passed regulations that a vehicle manufacturer bears responsibility for their vehicle from the time it is made to the time it is retired from service and disassembled so that the materials can be easily recycled, which sent OEMs on a "Green" binge.

The first attempt at this "Green" correctness was by on the 1991-95 Mercedes-Benz, where they started to use "bio-degradable wiring harness".

No rodents necessary, only heat and time causing wiring insulation to deteriorate, crack and ultimately fall off, causing infinite combinations of wiring shorts.

This did not happen until the vehicles were out of warranty with almost a 100% failure rate by year 12. Call it engineered obsolescence, like the rust buckets of the 50s and 60s.

OEMs started replacing components with untested natural materials in place of petroleum in plastics.

Now we introduce an inexpensive, readily available alternative, soy, which starts being utilized in just about anything from wiring harness covers, insulation, seat cushion foam to interior carpeting.

Understanding why rodents gnaw on wires, and other components, is also important in finding ways to prevent it.

Contrary to the common belief, they do not eat wiring for food. Rodents gnaw constantly, to sharpen and keep the length of their teeth in check. Unlike most mammals, the teeth of a rodent grow rapidly, throughout their life.

All that said, if you were a rodent would you prefer to chew on some toxic foam rubber made from petroleum or a vanilla smelling one made from Soy?

Here are some suggestions to proactively protect your vehicle. Don't let your car sit unused for more than a couple of days.

You can secure your garage by plugging holes with stainless steel mesh, sheet metal or aluminum flashing.

Snowbirds, if you are storing your vehicle for the season, invest in a drive-in bag or capsule that completely seals your car.

To keep vermin away use taste deterrents like bitter apple spray, sold in most pet stores, peppermint oil, Pine-Sol, mothballs, red pepper and laundry dryer sheets.

Get a couple of cheap snap traps and bait them with peanut butter. Put one under your car and one on your engine. It works every time. Nobody has invented a better mouse trap.

Frankly Funny

The owner of a small deli was being questioned by an IRS agent about his tax return.

He had reported a net profit of $80,000 for the year.

"Why don't you people leave me alone?" the deli owner said. "I work like a dog, everyone in my family helps out, the place is only closed three days a year. And you want to know how I made $80,000?"

"It's not your income that bothers us," the agent said. "It's these deductions. You listed six trips to Bermuda for you and your wife."

"Oh, that," the owner said smiling. "Did I forget to mention, we also deliver."