Quarterly Playbook
1st Quarter 2020

Current Financial Planning and Investment Themes
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"Roaring into the 20's"

We closed out 2019 with a lot of roaring momentum in both the US economy and the financial markets. With last year's two main challenges (Federal Reserve and China Trade) being taken off the threat list, good times should keep on rollin'! But unlike the Gatsby party that was 2019, we think this year will be more like your cousin's birthday party. Still fun, but nothing to brag about…

US Economics

It appears that we will record a 2.4% GDP growth rate for the full year 2019 based on the final report of 2.1% for the 3rd quarter and preliminary GDP now estimates of 2.3% for 4th quarter growth. Not bad considering all of the trade war fears and that everyone was talking about recession for most of the year! Especially since the Federal Reserve only believe that the long run potential GDP growth to be between 1.7-2.2%. We would argue that even though it wasn't the highest GDP growth year we have seen in a while; the underlying ingredients are at the strongest levels in a few decades. With the official (U-3) unemployment rate of 3.5% that is the lowest measure since 1969 or 50 years. Furthermore, the U-6 unemployment rate (broader definition including part-time) which began to be measured in 1994 is at its lowest level in history, 6.9%. Meanwhile, the labor participation rate is unchanged at 63.2%, which is meaningfully off the 2015 lows of 62.4%. This bodes very well for continued "above range" economic growth.

US Equity Markets

The US stock market roared to a finish in 2019. The S&P 500 posted its second-best year since 1997! Looking forward into 2020, however, we expect a much more average scenario. Not to say that we see any problems in the market, we don't. US stocks are trading at reasonable valuations, economic growth looks to continue to be above long-term expectations, with earnings and balance sheets looking to remain strong. Several factors that helped 2019 returns such as rebounding from an unwarranted 4th quarter sell-off in 2018, the easing of yield curve worries, and solidifying a trades truce with China are not in play for 2020. A nuance that is likely to appear is the shift to politics as the source of volatility. Our expectation is that most of the year will be sideways and a little choppy but should finish higher after the uncertainty of the elections are past. In this scenario, though, all eyes will be on earnings and margins.

US Fixed Income

Wow, 2019 was quite a year for fixed income! We experienced stock market like returns from boring old bonds! However, we expect 2020 to be a year of back to clipping coupons. Unlike the last 18 months of remarkable volatility in bonds, we believe that pricing pressures should remain roughly balanced causing relatively stable prices. Ultra-low or negative global yields should be offset by a stronger economic outlook. So, collecting income will account for the majority of returns in fixed income. We look for returns ranging from 3% - 7% from Government bonds to High Yield bonds & Preferred Stocks, respectively.

International Markets

Even though international economies are still experiencing sluggish growth, it appears that there could be further opportunity in international equities. Both developed and emerging markets are positioned for a relative rebound versus U.S. stocks in 2020. Should both global growth and emerging-market earnings accelerate in the year ahead, as we believe they could, this would likely be well received by the markets. The real tailwind though is the synchronized easing by 23 global central banks that has taken place since the middle of last year.

Real Estate

The outlook for REITs in 2020 remains favorable. Strong cash flows, pricing power, low interest rates, and overall favorable economic conditions remain in place going into the year. Furthermore, real estate markets enjoy low vacancy rates and a balance of new supply and growing demand, supporting rent growth and REIT earnings in the year ahead.

Interest Rates & the Fed

What a relief, the Fed is back to being boring – for now. For the last several meetings, the Fed has stated that they plan to leave the Fed Funds rate at 1.5% to 1.75% for the entire length of 2020. We believe them, given that they were called out for making such an embarrassing policy error in 2019 it's no wonder they want to stay out of the spotlight. Additionally, PCE inflation remains persistently below their minimum target of 2% which calls for more accommodative measures. We also think that the Fed (correctly) feels that too much focus is put on the Fed funds rate. Seemingly for the last decade, the Fed funds rate was THE biggest data point focused on by investors. There is even one analyst who predicted the Fed funds rates will remain intact for the next 5 years! We are not so certain, as our belief that the restlessness of committees won't allow them to sit still for that long. However, we believe that they will use the other "tool" in their toolbox, the Fed balance sheet, which is much less focused on in the general public view.

Legislative Affairs

Even though the House of Representatives has voted to send articles of impeachment to the Senate, almost everyone, including markets, have already dismissed the proceedings as a "political sideshow" that has no chance of taking effect as it was a partisan vote in the House with no republicans voting to impeach and getting the required 2/3rds supermajority in the Republican controlled Senate is next to impossible. Nonetheless, it is a high stakes distraction that may carry lasting repercussions – if trying to impeach the winner of every presidential election continues. But much like the market has gotten used to government shutdowns and other political stunts, this too is becoming seen as "business as usual" – unfortunately. So, we do not expect market volatility stemming from that front. We do, however, believe that as the presidential race heats up, campaign proposals and agendas will cause some choppiness in the markets. One issue that has popped up is the heightened tensions with Iran, which if they intensify, are likely to cause a mild flight to safety among markets. To be clear, Iran is economically insignificant, but markets will infer the possibility of other major world powers – China and/or Russia – aligning themselves with Iran, however this is very unlikely. Lastly, amongst the craziness in Washington, there actually have been some major accomplishments recently. The biggest legislative item has been the passage of the SECURE Act that bolsters retirement savings abilities. Please read our financial planning section for the details. Not far behind is the announced phase one trade deal with China expected to be signed on January 15th. This is likely to put markets at ease and we expect that phase two to be picked up after the elections. Interestingly, both of these are somewhat surprising accomplishments given the impeachment pursuit.

Financial Planning Corner

Legislative Updates

THE SECURE ACT:

The passing of the SECURE Act brings the most impactful changes to retirement and tax planning we've seen since the Tax Cuts and Jobs Act. Here's a closer look at the more impactful changes:

- Inherited IRA 10-year Rule - Elimination of the "Stretch" IRA forcing the entire account balance to be distributed by the end of the 10th year after the original IRA owner's death barring some exclusions
- Required Minimum Distributions (RMDs) Pushed to Age 72 rather than 70 ½,
- Traditional IRA Contributions No Longer Prohibited At and Beyond Age 70 ½
- No 10% Withdrawal Penalty for Childbirth and Adoption
- Annuities Are a More Viable Retirement Plan Investment Choice For 401k
- Bigger (up to $5,000) in Tax Credits for Small Businesses Who Establish Retirement Plans
- Part-time Employees work over 1,000 hours in a year OR at least 500 hours in at least 3 consecutive years will gain access to Employer Retirement Plans
- Multi-Employer Retirement Plans More Viable for Small Businesses looking to pair up with others
- Qualified 529 Expenses Now Include $10,000 of Student Loans and Apprenticeships

The Affordable Care Act's "Cadillac Tax" Officially Repealed

The "Cadillac Tax" was a 40% excise tax (to employers) on employer group health plans that paid more than $10,200/year for self-only coverage and $27,500/year for more than self-only coverage (spouse or family) for its employees. The repeal will more than likely bring more choices for employees with employer healthcare since employers will maintain flexibility in the types of plans and coverage levels they can offer (without fear of the Cadillac Tax on the horizon). There is a growing consensus that High Deductible Health Plans paired with HSAs will maintain popularity in the coming years.

Medicare Changes:

2020 Premium and Deductible Changes: The Medicare Part B premium went from $135.50 to $144.60 per month (this is the amount paid every month to cover the government portion of Original Medicare, and is likely automatically deducted from your Social Security payment). The Income Related Adjustment Premiums (for higher income brackets) went up slightly as well adding an additional $57.80 to $347 monthly surcharge, depending on tax bracket.

The Part B (outpatient) annual deductible rose from $185 to $198. If you have a plan F or C Supplement, or a Medicare Advantage plan, this deductible change would not affect you.

The Part A (inpatient) deductible and copays went up as well, but the only way these increases typically affect you is if you do not have a Medicare Supplement or a Medicare Advantage plan.

Side Note: If you're married and planning on going onto Medicare within the next few years, make it known to your CPA or tax preparer. Express to them that you would like to keep that in mind when determining whether to file Joint vs. Married and Separate. Married and Separate has substantially less favorable income brackets that determine your Medicare premium rates. If you have any questions, just ask us.

State of Ohio Business Income Deduction

The Ohio General Assembly elected to maintain the preferential state income tax treatment of business income allowing sole proprietors, partnerships, and LLCs to continue to deduct the first $250,000 of income, and paying a flat 3% tax rate on any income earned above that amount. They did, however, eliminate the deduction and 3% tax rate altogether for Lobbyists and Attorneys. These changes take effect for taxable years beginning January 1, 2020 or after.

Reduced Ohio State Income Tax:

On July 17th, 2019 the Ohio General Assembly finalized the operating budget for fiscal years 2020 and 2021. One of the most notable changes was the reduction of Ohio income tax across the board for all brackets. Here's a closer look at the changes (All filing statuses are the same bracket):

For taxable years beginning in 2019:

Ohio Taxable Income	Tax Calculation
0 - $21,750	0.000%
$21,751 - $43,450	$310.47 + 2.850% of excess over $21,750
$43,450 - $86,900	$928.92 + 3.326% of excess over $43,450
$86,900 - $108,700	$2,374.07 + 3.802% of excess over $86,900
$108,700 - $217,400	$3,202.91 + 4.413% of excess over $108,700
more than $217,400	$7,999.84 + 4.797% of excess over $217,400

Source: https://www.tax.ohio.gov/ohio_individual/individual/annual_tax_rates.aspx

What this ultimately equates to is a **4% reduction on your overall Ohio state income tax liability beginning for taxable year 2019**. Here's an example of how 2019 rates compare to 2018 rates for different income levels (not including any tax credits you may qualify for):

Taxable Income	2018 Tax Due	2019 Tax Due	Percent Change
$150,000	$5,235.06	$5,025.48	-4.00%
$250,000	$9,962.46	$9,563.66	-4.00%
$350,000	$14,959.46	$14,360.66	-4.00%

We're here to help. If you have questions about these or any other topics, don't hesitate to call us at (855) AFS-4545.