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MARKETWATCH

Deeply Rooted in the Community | Second Quarter 2018

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Current Outlook

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We have now experienced nearly 18 months of the "Trump Effect" on the economy, interest rates, corporate profits, asset markets, and investor psyche. Both consumer and business confidence are at 15-year highs. World economies continue to experience a synchronized growth spurt. Corporate America is seeing improved cash flows as a result of a dramatic cut in its 2018 tax rate. And individuals are seeing improvement in after-tax incomes. But the uncertainty of "what's next" puts a slight damper on all-out euphoria. Questions regarding what the next move on interest rates will be by the Federal Reserve Board and its new Chairman remain somewhat unresolved. Threats of international tensions, as well as the recent "trade war" talk led by the United States cause some to fear a self-inflicted wound to the generally good economic reports we are seeing.

We continue to expect moderate economic growth and relatively low inflation for the foreseeable future. Much has been made of the possible effects of monetary authorities cutting back on the extraordinary easy money of the past decade. At this point the Fed has telegraphed at least three 0.25% short-term interest rate increases this year and another three next year. This suggests that we may be looking at a 3% short-term interest rate by the end of 2019. While the Fed can control short-term interest rates, the longer-term interest rates are determined by market forces. With the 10-year U.S. Treasury Note currently yielding near 3%, and no change in that rate expected near-term due to tame inflation and worldwide demand for U.S. government bonds, we could be looking at a flat or possibly "inverted" yield curve (long-term rates are lower than short-term rates). Seldom has the economy performed well in that circumstance. The threat of a flat or inverted yield curve could prompt the Fed to hold off on any further increases in short-term rates next year. While we are not predicting this will happen, we are ever mindful of the possibility.

Another uncertainty is the path of trade policy. After years of trade policy stability, the Trump administration has taken on a decidedly hawkish approach to our trade imbalance. Not only have tariffs been imposed on selected items, but long-standing trade agreements such as the North American Free Trade Agreement are in the midst of renegotiation. Free trade has been the bedrock of U.S. policy since the end of World War II and has produced much prosperity. Whether or not U.S. policy now prompts widespread retaliation is yet to be known, but it is clear that any disruption could cause both higher inflation and slower growth—"stagflation" anyone?

Finally, we are also watching the political situation both domestically and around the world. As investors we not only track what is happening to the fundamentals of various asset classes, but also their valuation. Valuation depends greatly on the populace's current mood, and that mood generally is dictated by the flow of current events. We are in an election year again in the United States. After the 2016 cycle brought one-party rule to the United States, the mood was decidedly upbeat. The possibility of another divided government after November may cause investors to mark-down asset valuations. Talk of amending the new Tax Bill as well as a return to gridlock is something we must monitor closely. Asset allocations may have to be adjusted going forward to reflect this possible change in investor mood. We maintain our overall positive outlook, but because of persistent uncertainties we will have to remain flexible to the opportunities ahead for wealth creation.

Having "The Talk" With Your Heirs

Hood Craddock, CFA
Director of Family Office Services

Are your children grown? Do they have children or even grandchildren of their own? No matter how much knowledge and experience they have accumulated, inheriting your wealth may be a dramatically different and complex responsibility for them.

How do you plan to pass on your assets? Consider these options -

- How can an Irrevocable Trust protect your heirs and the hopes you have for their future wealth?
- How can elections at death create significant tax differences that impact the ultimate payout?
- How can the design of a trust protect the assets to be inherited when one parent remarries?
- Upon the death of both parents, is it best to create separate trusts for the Next Generation (with multiple heirs) or keep it in one account to benefit all?

These questions and more are ones that families wrestle with every day. The path to the answers all start with one important conversation.

Have the "Inheritance Conversation" sooner rather than later.

Each generation has a way of discussing estate planning and money management with the next one – or alternatively, keeping that information closer to the vest. Only you know your family members and the dynamics between them. Whether or not you disclose the amount of your estate, having a conversation to set expectations in advance generally assures a smoother transition of family assets and provides heirs the opportunity to ask questions directly, gaining clarification about expectations, as well as seeking guidance about how to manage such an inheritance. Understanding your thoughts about the wealth you've accumulated, and how your plans will benefit them and perhaps their community, will be a source of wisdom and insight they will appreciate.

What steps can be taken to assist the Next Generation?

Introduce your heirs to your trusted advisors, so they have an understanding of what they do for you and become familiar with the same fiduciary care and guidance that you have experienced over the years, leading to a less stressful transition of wealth in the future. In addition, help safeguard wealth for the heirs by establishing a Corporate Trustee or Corporate Co-Trustee of the estate. The Corporate Trustee role provides a level of confidence and ongoing advice to heirs to uphold the wishes of the parent generation and manage all fiduciary and tax requirements related to the trust. It also provides a level of protection to assure that the funds are properly managed, and ultimately cultivated and used as they were intended. Corporate Trustees provide a failsafe for the benefit of the heirs — otherwise, depending upon each family's situation, the inheritance can be quickly depleted through tax mistakes, legal battles and lack of financial discipline. Similarly, a Corporate Co-Trustee forms a working partnership with a family member and/or additional trusted advisor to guide and advise, as well as serve as an intermediary to beneficiaries.

It is important to have custom-designed family trust and investment management for you and the generations to follow, taking into account significant life changes, individual circumstances and special needs, business succession, management of special assets, and strategic philanthropy. In addition, ongoing family education and governance helps prepare and inform your children for the responsibilities that come with inherited wealth.

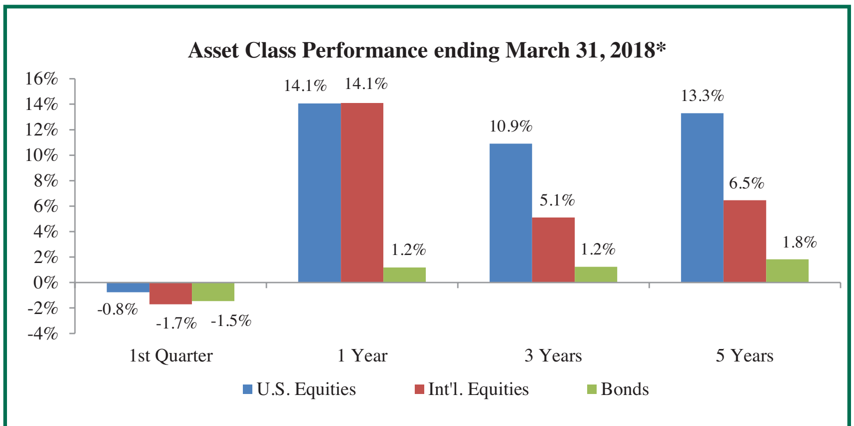
We highly recommend a family meeting. It is a comfortable, effective forum to introduce your estate plan and the vision that brought you to this point. It is also an opportunity to introduce your children and possibly grandchildren into the process of preparing for inherited wealth that could substantially change their lives. Contact us to discuss how we can assist you in starting the conversation.

Portfolio Review & Strategy

Craig J. Holston
Chief Operating Officer

Global stock markets moved modestly higher during the first quarter of 2018. For the first time in more than a year, day-to-day stock market volatility has returned to historically normal levels. Last year was unusually calm as markets moved steadily higher throughout most of 2017 with minimal interruption. In fact, 2017 was the least volatile stock market year since the CBOE's Volatility Index® (VIX®) was established in the early 1990's.[1] With that context, we view recent stock market movements as rather normal. We encourage our clients to avoid focusing on the short-term market "noise" and instead look to the fundamentals of the economy and the companies we follow. From our perspective, corporate earnings were quite strong in the fourth quarter of 2017, which portends well for this year and next, particularly when we factor in the tailwind of corporate tax reform.

On March 21st, the Federal Reserve Board announced their decision to raise the federal funds rate by another 0.25%. The Fed will also continue to reduce the size of its balance sheet by letting Treasury and mortgage-backed securities mature over the next few years. This was largely anticipated by most market participants. Nonetheless, it is another signal that monetary "tightening" clearly is occurring. Other broad market interest rates have responded this year by moving higher. In the near term, higher interest rates will put price pressures on dividend-paying companies as the relative value between income-producing stocks and bonds readjusts. Though we continue to view higher interest rates as a symptom of a positive overall economy, we will continue to watch the shape of the yield curve. An inverted (negative sloping) yield curve generally portends poorly for economic activity. We have seen some flattening in the curve over the past year as short-term interest rates have risen faster than long-term rates.



**The S&P 500, MSCI EAFE, and Barclays US Agg Bond are used as proxies for broader market performance. Three and five year figures are annualized.*

For the first time in years, bond investors are starting to feel the impacts of higher interest rates. Bond prices have moved lower in 2018, and that will continue as long as interest rates continue to move higher. The biggest impact will be felt by investors holding long-term bonds – an asset class we have avoided for years. Short-term bonds will also be impacted, but to a much lesser extent. Our investment team is watching these movements closely and will continue to evaluate the relative value between stocks and bonds as interest rates move higher. For the time being, we believe we still are a long way away from bonds being as attractive as stocks on a risk-adjusted basis. However, as rates rise, our willingness to use bonds in a more meaningful way across client accounts will increase.

[1] The CBOE Volatility Index® (VIX® Index) is a leading measure of market expectations of near-term volatility conveyed by S&P 500 Index (SPX) option prices.

Downsizing—Why, When & How

Robin L. Cook
Wealth Services Advisor

People decide to downsize for a variety of reasons. Perhaps you are a new empty nester or just trying to simplify your life; you are establishing your primary residence in Florida or moving to a retirement community with a full range of activities and levels of care. Whatever the reason, the process of downsizing is downright intimidating. It is a major life event that should be carried out with the support of others and a plan in mind.

Your home is full of cherished memories – family heirlooms, art, collectibles, antiques, and yes, probably a lot of just plain stuff. While it would please most of us to have our children excited about taking these personal possessions, this is often not the case. What we hear much of the time from clients is that "Our kids don't want it."

Other important questions are these: Where should I live? What are the up-front and ongoing costs of the new residence? Can I afford it? Should I withdraw funds from my portfolio or finance the purchase of a new residence, while trying to sell my existing home? How do I properly establish Florida residency to relieve the income and estate tax burdens some states impose?

These are all questions that we help clients work through to find the best solutions. Here are some action plans to get you started:

Start early! By planning ahead – we suggest 2-3 years before you want or need to move – you have plenty of time to research the "new residence" options. Some Southwest Florida retirement communities have long waiting lists and minimum health requirements.

Explore communities in which you have an interest. Is the location convenient for your lifestyle needs, i.e.; shopping, hospitals, doctors, friends, worship? Confirm all anticipated expenses.

Start the process of decluttering. See what items the children and other family members want. Explore options for selling or donating items that won't fit into your new space. Take photos of those you wish to give away and send them to your family members. Give them a deadline to claim their items – perhaps six to eight weeks. You can even set up weekly automatic email reminders.

Evaluate your home. Meet with realtors to help determine the value and marketability of your current home, as well as necessary repairs and updates. Decide what improvements you wish to make and get started on them. This effort plus the decluttering you accomplish will help your home be more marketable and may even increase its value.

Meet with your Wealth Advisor and Portfolio Manager to run the numbers. Investing the cash proceeds after downsizing can often enlarge your nest egg and further enhance your lifestyle. After factoring in the cost of insurance, taxes and maintenance, you may even find renting a home to be a better alternative.

The most important message is that you do not need to face these daunting tasks alone. In fact, with proper planning you may ultimately repeat what many of our clients have said, "This is so liberating, why didn't I do it sooner?" If you are facing some of these downsizing issues, make an appointment with your Wealth Advisor to manage the stress of the process and turn it into an enjoyable experience that enhances your lifestyle options. We are here to help you.

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