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MARKETWATCH

Deeply Rooted in the Community | Third Quarter 2019

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Current Outlook

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'Uncertainty' seemed to be the watchword during the first half of 2019. For example, first quarter U.S. real GDP growth was a better than expected 3.1%, while second quarter estimates have been falling, with many economists expecting annualized real GDP growth of less than 2%. The ongoing 'trade war' with China, though its nationwide impact has been scant so far, is having a large negative impact on economists' growth estimates - and unfortunately there appears to be no assurance that trade negotiations will be resolved soon, and to economists' satisfaction.

The longer the tariffs and trade rhetoric persist, the greater their ultimate effects on corporate profits. What began as limited tariffs mostly impacting farm products and importers of steel and automobiles is showing signs of spreading to other more vital industries, such as consumer products and technology. Compounding the issue is that the U.S. dollar has risen almost 4% in recent months on a trade-weighted basis, as analysts handicap that foreign economies will suffer more than the U.S. in a protracted trade dispute. A rising dollar undercuts the value of U.S. companies' overseas sales and profits. As a result, many Wall Street analysts have cut their S&P 500 corporate earnings growth estimates for 2019 from 8%-9% to 2%-5%.

On a more positive note, U.S. unemployment sits at a 50-year low, and the U.S. core inflation rate was a mere 1.0% in the first half of the year. However, housing data was more varied. While year-over-year new home sales rose 6% over the first four months of 2019, existing home sales fell 5% over the same period. On the other hand, both figures may get a solid boost from the recent plunge in mortgage rates, with the 30-year fixed rate recently falling well below 4%, from approximately 5% last November.

Certainly, the slide in interest rates this year was unanticipated. At the beginning of the year, it was expected the Federal Reserve Board would, at a minimum, keep the Fed Funds rate the same, or continue to gradually increase rates as it has done since December 2015. Now, bond market investors anticipate the next move by the Fed will be to reduce rates given the growing amount of data signaling the economy is slowing. Moreover, the bond futures market is forecasting three or four 0.25% rate cuts over the course of the next 18 months.

Interestingly, while stocks have experienced volatility over the last few months, several of the major U.S. equity indices generated double-digit returns in the first six months of the year. However, for the equity market to move higher in the second half of the year, the Federal Reserve may need to start lowering interest rates again, and relatively soon. Since the beginning of the year, earnings growth projections have declined and stock prices have risen, so valuation metrics have become less attractive. In addition, political tensions with Iran, North Korea and China remain concerning enough to investors to impact stock prices. Therefore, if interest rates are not reduced, it is possible the economy will slow even more than expected, leaving fixed-income investments more in competition for investor dollars on a risk-adjusted basis.

Plan Smart for Continuing Care

Cherry W. Smith
Wealth Services

There are nearly 47 million Americans over the age of 65, and every day another 10,000 Baby Boomers reach that age. This trend will continue until 2030, when 18% of the country will be at least 65 years old. As life expectancy continues to increase, retirees are recognizing the stark reality that their longevity may ultimately require increasing care and medical support. They also need to identify – sometimes well in advance – who will provide that care and how they will pay for it.

For seniors with the financial means, a Continuing Care Retirement Community (CCRC) is a popular and effective way to plan for the increasing levels of healthcare services that may be needed. There are many different CCRC's available in which to live, and they come with an array of pricing options and fees – including entrance fees, monthly fees, insurance requirements, conditions for transfer within the community to higher levels of care, partial refundability of entrance fees, and stated levels of healthcare quality at every step.

This "continuum of care" lifestyle begins with **Independent Living** for which a CCRC can offer a wide variety of housing choices, amenities, dining, transportation, social activities and health/wellness centers that promote functioning, motivated and active social lives. Thanks to advanced assistive medical technologies and improvements in ambulatory devices, more seniors can opt for independent living far longer than previous generations.

The next level of CCRC care is **Assisted Living**, defined as non-medical care for those who require help with one of the six activities of daily living **(eating, bathing, dressing, toileting, grooming and mobility).** It may also include medication management. While assisted living recipients are not capable of living independently, they do not require 24-hour medical care.

From there, progressive levels of service at a CCRC include **Skilled Care** and **Skilled Nursing Care** that encompass both healthcare and rehabilitative therapies. Patient management, observation, and evaluation often are administered by licensed practical nurses, licensed vocational nurses, or registered nurses.

As more seniors are being diagnosed with cognitive disorders such as dementia and Alzheimer's disease, an increasingly common component of CCRC living is **Memory Care.** It is typically offered in a community residential setting with the level of care increasing as the illness progresses, often leading to increased costs for 24-hour medical attention.

If you are considering the transition into CCRC living, sit down with your team of advisors – your attorney, CPA, investment or insurance professionals – to assess your options. They can review the CCRC contract or help determine what your long-term health-care policies will pay toward this lifestyle. Your financial advisors can use software tools to project how your portfolio can support CCRC living, or recommend changes to your portfolio to support such a move in the future.

A successful transition to a CCRC takes planning that is best conducted well in advance so your financial plan meets your needs. We at The Trust Company are here to help you analyze and support your efforts in making this important decision.

Portfolio Review & Strategy

Ian N. Breusch, CFA
Chief Investment Officer

We began 2019 with a strong rebound in global equity markets on the back of an intense, but short-lived market decline last December. Stock market volatility continues as exogenous macro-economic considerations weigh on investors. Uncertainty around interest rate policy and the ongoing tariff tension between the U.S. and China make it difficult for market participants to discern whether we are indeed slowing or this is just another chapter in our economic expansion that now spans a decade. On one hand, the bond market is clearly signaling a slowdown as the yield curve remains inverted and rates have been pushed to historic lows once again. However, other broad based economic data remains quite constructive, such as modest GDP growth, solid corporate profits, and low unemployment.

It now seems plausible (if not expected) that the Federal Reserve Board will lower interest rates beginning as early as this summer. This stands in stark contrast to the tighter monetary policy that most expected would persist for some time. If we have indeed already experienced peak interest rates during this current economic expansion, it is feasible that rates not only move lower, but stay lower for a lengthy period of time.

For years now, we have been steadfast in our belief that stocks offer a better risk-adjusted value than bonds – all else being equal. Given the movement lower in bond yields, we still maintain that stocks offer better forward return prospects in most cases. However, we also acknowledge that many of our clients, particularly those looking to reduce risk in their portfolios, would benefit by considering a modest allocation to high quality, short-term bonds. We make this argument entirely based on risk reduction, not on forward return potential. As always, we ask our clients to consult with their portfolio manager to consider these sorts of tweaks as a way of achieving their unique goals.

At our Annual Outlook events we hosted in our various markets earlier this year, we made the case for a strong stock market in 2019, with the caveat that we are most likely closer to the next slowdown/recession than further away. While the timing of these eventualities is interesting to consider, we remain less focused on what we can't control and much more focused on what we can. For example, an important part of any long-term investment strategy is deciding on an appropriate asset allocation plan that coincides with your unique goals and constraints. This plan can (and should be) reviewed and discussed with your portfolio manager on a regular basis. However, the agreed upon plan should stay relatively consistent through time, assuming there are no major changes with your personal circumstances.

Regardless of the relative proportion of stocks, bonds and cash that makes sense for your individual portfolio, our investment team remains focused on owning and sourcing the highest quality assets. From a stock perspective, this means finding companies with good revenue and earnings foresight, strong cash flows, stable balance sheets, and modest debt levels. To the extent bonds are appropriate, we are intentionally staying very short-term with our bond purchases and focusing on good credit quality.

The long-term objectives we set forth with our clients continue to be very attainable. We know corrections and recessions are going to occur, it's a matter of when – not if. The investment objectives we implement on behalf of our clients already assume we are going to have periods of time that are uncomfortable. It's the long-term average rate of return we are shooting for, not the avoidance of short-term volatility. For that reason, despite some of the risks we highlight above, we remain quite optimistic heading towards the latter half of 2019.

Who Will Advocate for Your Estate?

Peter Knize, J.D., LL.M.
Trust Administration

In 1909, Samuel Langhorne Clemens (better known as Mark Twain) penned one last request as his health failed:

> *'I came in with Halley's Comet in 1835. It is coming again next year, and I expect to go out with it... The Almighty has said, 'no doubt: Now here are these two unaccountable freaks, they came together, they must go out together.'"*

He did. Twain's wistful prognostication turned prescient when in April 1910, he passed away one day after the comet's closest approach to Earth. A month later, his last will and testament was admitted by a Connecticut Probate Court appointing three friends – a railroad executive, a businessman and a banker – as executor trustees to administer his estate. This last formal decision of Twain's proved to be one of his biggest financial mistakes.

Like many of us, Twain thought long and hard about both the timing of his death and how to disburse his then considerable estate. But not just to whom; the humorist carefully considered the most important question, by whom? Who would actually "execute" the terms of his will, advocating for his intent generations later?

Twain's dual concerns were 1) to protect his daughter and sole heir, Clara Clemens, from repeating his own investment mistakes and 2) "to keep the money in the family." He believed the complexity of his estate – priceless manuscripts, stocks, bonds, copyrights, real estate, and book deals – as well as managing The Mark Twain Company, and reigning in a spendthrift daughter were enough to cause any executor undue ordeals ahead. He believed the solution was to appoint three independent laymen to be his advocate.

Twain intended the executor trustees to hold his estate in trust for Clara, who in addition to being cavalier with money was disposed to marry, divorce, and remarry. His trust directed quarterly income payments to Clara "free from any control or interference from any husband she may have."

Little did Twain know that all three executors soon would be gone; one died, one quit under duress, the third forced to resign. Without the backstop of perpetual successor trustees to implement Twain's wishes, the estate came up for grabs. Clara remarried, and her next husband took liberties against the estate and borrowed $350,000 against it. Clara disinherited her daughter Nina, before dying herself, prompting Nina to file an undue influence suit against her step-dad. A probate judge eventually awarded Clara's second husband (Nina's step-dad) 65% of Twain's estate for life!

How could this happen? Who was advocating for Mr. Twain's intent? The sad answer is inescapable—no one.

Whether estates pass via a last will or revocable trust, selecting a proper executor and trustee(s) is the key ingredient to a successful estate plan. Our modern heirs – minor children and grandchildren, elder children, step-children, siblings, dysfunctional relatives, charities, and ex-spouses – have only added to the significant emotional and psychological burden placed on today's executors and Trustees. Twain, with just one apparent heir to consider, knew Clara all too well; planned right, but selected wrong. He relied on three trusted friends who, no matter their business skills and stature in the community, were not up to the task of managing a complex estate over generations. Few laypeople are. The irony is that Twain could just as easily have appointed the neighborhood Connecticut law firm or Trust Company to serve as Trustees – firms that still exist to this day. So take time to consider by whom. The proper advocate matters more than you may ever live to know.

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