

Praetorian Guard

QUARTERLY NEWSLETTER • 4TH QUARTER 2016



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Third Quarter 2016 Market Review and Discussion

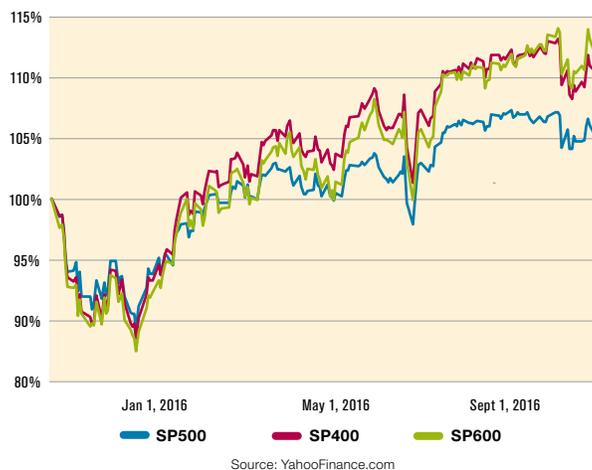
The “stacked” graphs show the 2016 year to date returns (top) for the U.S. equity markets and the implied volatility of the S&P 500 index for the same period. These reinforce an important perspective as the graphs reflect the benefits of remaining calm and allowing others to surrender to their need to “do something” in the midst of volatile markets. A wise global investment guru from the past often said the best rule to follow is: “Don’t just do something, stand there.” Markets are always going to receive, digest, and (over) react to events before settling to *reflect* on what took place and what it actually means. We want our clients to understand that an overreaction needs to fall into one of two categories: first, an opportunity to add to your holdings while others are selling irrationally OR second, an interesting sideshow to watch but recognize you do not have to participate.

There are a few economic “shocks” we can anticipate in the 4th quarter. Obviously, the result of the upcoming Presidential election will dominate the headlines, but what matters more is the ultimate control of the U.S. Senate. In crunching our crystal ball, we project the Republicans maintaining majority control.

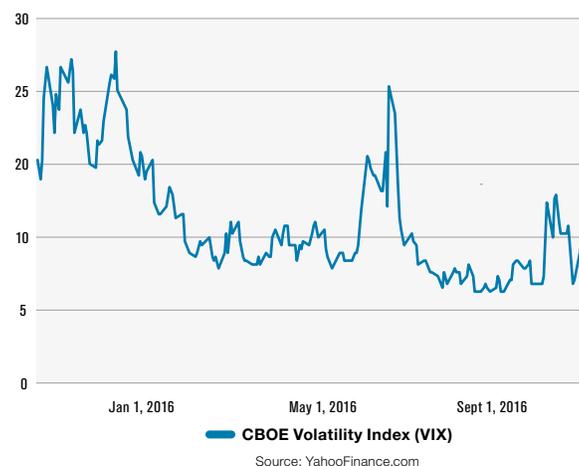
The second shock may be the OPEC meeting on November 30th. A production “freeze” agreement was tentatively reached in late September and oil prices responded by rising close to \$50/barrel. However, that is not enough to significantly help struggling OPEC members Nigeria and the economic catastrophe that is now Venezuela. We also do not see significant support by Iran, Iraq or critical (but non OPEC) member Russia.

The final shock will be the Federal Reserve Open Market Committee Meeting on 13-14 December. Expect a 0.25% rate increase to be announced. More importantly, recognize this increase brings the Fed Funds target rate to a “massive” (!!) 0.75% rate. This is not so much a rate hike in practice as it is a start to return to a less accommodative monetary policy stance. 🍷

2016 YTD US Equity Market Performance



2016 YTD S&P 500 Volatility



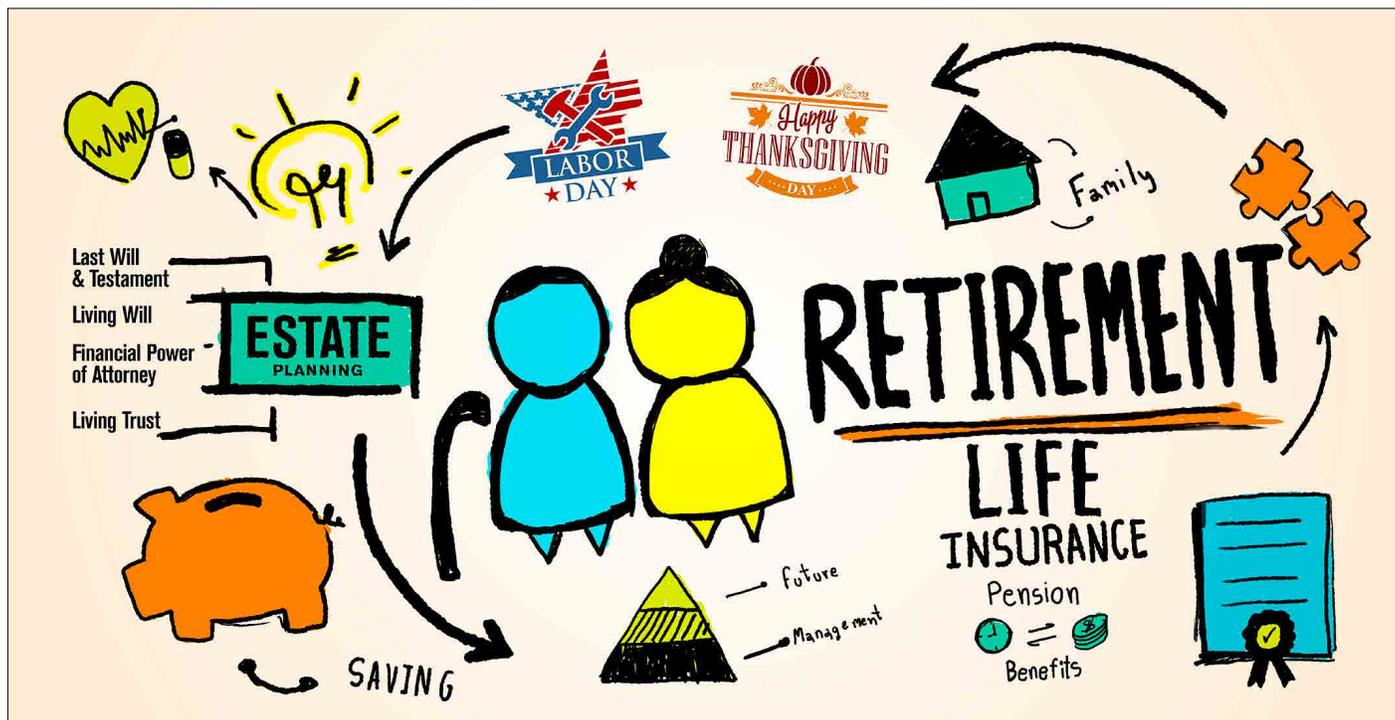
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END OF YEAR TAX AND INVESTMENT PLANNING DISCUSSION



The period after Labor Day up to Thanksgiving is a great window to make sure you have your financial affairs up to date and take advantage of some potential tax saving moves before the year closes out on December 31st. We have attempted to break the following into topic areas to aid you in focusing time/efforts on those things that are most important to you:

RETIREMENT ACCOUNTS

Have you or your spouse attained age 50 (or will do so prior to 01/01/2017)? If yes, have you looked at increasing your 401(k) or 403(b) retirement account payroll deferrals to take advantage of the “catch up” provision? You can contribute an additional \$6,000 if you are 50 or older but it is important to note that you can do less than that if your budget won’t support the full amount.

Have you had any life changes? The birth of a child or grandchild or perhaps a death in the family that would necessitate a beneficiary update to reflect your present situation? Job changes which may leave a retirement account with a former employer can be consolidated in several ways. Please get in touch with us if you find yourself having one of these life changes.

Lastly, if you cannot remember the last time you logged on and rebalanced your 401(k)/403(b), it’s overdue. If you need help, please contact us and we’ll gladly help make the process simple and painless.

ESTATE PLANNING DOCUMENTS

The first and most obvious question: do you have these [Will, Durable Power of Attorney, Power of Attorney for Health Care, Guardian named for minor children, Trust(s)]? If not, we need to talk yesterday, not tomorrow. This could create a gap in your financial plan that will wreak havoc on a lifetime of planning, saving and investing.

Next, put all the Trust, Will, Power of Attorney and Guardian forms on the table. Review the people you have named to act as co-trustees, executors, guardians: are they still living, willing and capable of performing the tasks you are possibly entrusting to them? If you are not sure, a phone call with them can save a great deal of administrative pain should the documents spring into existence. Are the people you have named still the ones you would select if you were drafting up the documents today? If not, it’s time for an update.

LIFE INSURANCE

The policy which was vital when the kids were younger may no longer be needed now that they are out conquering the world. If you have testamentary trusts set up for children or minors, compare the named Trustee(s) with the Estate Planning documents—for example, do the guardians of the children have access to/serve as trustees for the trusts set up for the children’s benefit? If needed, you may want to revisit this language in the trust. 🍂



Economics Basics

Since we have a nearly “economics free” presidential race, it seemed timely to return to the basics for a few of those topics prominently discussed by talking heads, candidates and “spin doctors.”

THE \$15/HOUR MINIMUM WAGE. Labor, like any other economic input, by definition must create more value than it costs or its use will cease and the enterprise will go out of business. Thus the relative question is *not* if \$15/hour is a “livable wage” or one sufficient to have a family of four move above the poverty line. The only question that matters is whether or not the worker, who costs the firm more than \$15, creates sufficient value to cover the \$15 + payroll taxes + other taxes + some allocation to the firm’s overhead + profit. If yes, the business owner’s response is to hire the employee and grow the business. If no, the job goes away or is replaced with technology (been to a fast food place lately with touch screen drink ordering?). In that case, the well-intended increase just dropped the former worker’s hourly wage to \$0. Many politicians do not want to hear it: when they mandate a “minimum” wage they are also setting a maximum wage of \$0 for many who want to grab a hold of the first rung on the economic ladder---they end up hurting the very people they purport to want to help.



INCOME TAXES. Every politician running for office has a “tax plan” but sadly most (on both sides of the aisle) are detached from the reality that there has to be income before there can be tax revenue receipts. Economic activity is a necessary precursor to taxation. Taxation does not generate economic activity—it is always and forever a drag on economic activity and thus the focus should be on the maximum revenue to be obtained at the minimum distortion to the economy. Our tax code is a huge impediment to sustained growth, causing distortions to investment and allocation of resources. We are increasingly pessimistic that we will ever see a 1986 style simplification and clean up of the tax code. Its pernicious roots are sinking in deeper and grabbing on tighter making it all that much harder to widen the base, lower the rates and stop trying to “guide” the economy from Washington. 🍷



PRESIDENT'S COMMENTARY



Viewing the political landscape, I have the sensation of viewing a multi-car accident on California Interstate 5—can't stop looking but wish I did not have to watch the wreckage. Since part of my role is to have a crystal ball, here are my predictions:

Hillary Clinton wins the White House narrowly in the popular vote (electoral vote count will be larger but not a mandate and limited coat tails). The House (for sure) and the Senate (60% probability) remain controlled by the Republican party (see same projection on page 1). There are several Senate races that will determine control. We'll know early in the evening on November 8th how those break.

These projections mean that for the 2017-2018 Congressional term we will have continued gridlock on domestic legislation, Clinton's tax proposals will be DOA on the Hill and the cumulative weight of gridlock plus the dead hand of regulation will keep the economy stumbling along with a maximum growth rate of 2%. Frustrating because every problem our nation faces requires revenue as a necessary condition and a crawling economy generates less than a healthy, robust one.

The good news: as of this writing, only 1,489 days until the 2020 Presidential election. 🍀



CLOSING THOUGHT

“Politics is the art of looking for trouble, finding it everywhere, diagnosing it incorrectly and applying the wrong remedies.”

—Groucho Marx

Stimulus-Response



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